CHINA MENGNIU DAIRY COMPANY LIMITED
中國蒙牛乳業有限公司*

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 2319)

ANNOUNCEMENT OF THE ANNUAL RESULTS FOR THE YEAR ENDED 31 DECEMBER 2016

HIGHLIGHTS

- Mengniu focuses on product quality and innovation, and is in the vanguard of the premium product consumption trend. During the year, Mengniu's liquid milk and chilled dairy products continued to lead the market with the largest market share.
- Continued with integration of the milk formula business, drawing on the resources support of Danone Group and the research and development expertise of Dumex Baby Food Co., Ltd. ("Dumex China") to improve its product development capabilities and augment the positioning of its product portfolio.
- Implemented new reforms for its business divisions in order to develop the independent room temperature, chilled, milk formula and ice cream product business segments. This has facilitated resource coordination and risk control, and thereby enabled the Group to achieve a balanced development.
- Entered into cooperative relations with international brands such as Shanghai Disney and NBA China to enhance the value of the Mengniu brand.
- Visionary deployment of upstream and downstream resources by increasing Mengniu's shareholding in China Modern Dairy Holdings Ltd. ("Modern Dairy"; stock code: 1117) in 2017, which is expected to help the Group to build smoother cooperative ties between upstream and downstream and ensure the supply of quality raw milk.

The board (the "Board") of directors (the "Directors") of China Mengniu Dairy Company Limited (the "Company") is pleased to present the results of the Company and its subsidiaries (the "Group" or "Mengniu") for the year ended 31 December 2016, together with the comparative amounts.

* *For identification purposes only*

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

Year ended 31 December 2016

	Notes	2016 RMB'000	2015 RMB'000
CONTINUING OPERATIONS			
REVENUE	4	**53,779,339**	49,026,516
Cost of sales		**(36,143,937)**	(33,651,042)
GROSS PROFIT		**17,635,402**	15,375,474
Other income and gains	4	**701,784**	521,268
Selling and distribution expenses		**(13,435,206)**	(10,985,039)
Administrative expenses		**(2,471,365)**	(1,871,250)
Other expenses	5	**(2,850,668)**	(392,591)
Interest income		**477,844**	563,273
Finance costs	7	**(293,700)**	(318,634)
Share of profits/(losses) of associates		**(225,477)**	137,669
PROFIT/(LOSS) BEFORE TAX FROM CONTINUING OPERATIONS	6	**(461,386)**	3,030,170
Income tax expense	8	**(351,379)**	(510,038)
PROFIT/(LOSS) FOR THE YEAR FROM CONTINUING OPERATIONS		**(812,765)**	2,520,132
DISCONTINUED OPERATION			
Profit for the year from a discontinued operation		**–**	122
PROFIT/(LOSS) FOR THE YEAR		**(812,765)**	2,520,254
Attributable to:			
Owners of the Company		**(751,155)**	2,367,291
Non-controlling interests		**(61,610)**	152,963
		(812,765)	2,520,254
EARNINGS/(LOSS) PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY (EXPRESSED IN RMB PER SHARE)	10		
Basic			
– For profit/(loss) for the year		**(0.193)**	0.609
– For profit/(loss) from continuing operations		**(0.193)**	0.609
Diluted			
– For profit/(loss) for the year		**(0.193)**	0.607
– For profit/(loss) from continuing operations		**(0.193)**	0.607

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December 2016

	2016 *RMB'000*	2015 *RMB'000*
PROFIT/(LOSS) FOR THE YEAR	**(812,765)**	2,520,254
OTHER COMPREHENSIVE INCOME/(LOSS)		
Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods:		
Exchange differences:		
Exchange differences on translation of foreign operations	**(128,597)**	(66,650)
Cash flow hedges:		
Effective portion of changes in fair value of hedging instruments arising during the year	**–**	9,645
Income tax effect	**–**	(1,257)
Net other comprehensive loss to be reclassified to profit or loss in subsequent periods	**(128,597)**	(58,262)
Other comprehensive income/(loss) not to be reclassified to profit or loss in subsequent periods:		
Equity investments designated as fair value through other comprehensive income:		
Changes in fair value	**94,371**	(117,050)
Net other comprehensive income/(loss) not to be reclassified to profit or loss in subsequent periods	**94,371**	(117,050)
OTHER COMPREHENSIVE LOSS, NET OF TAX	**(34,226)**	(175,312)
TOTAL COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR	**(846,991)**	2,344,942
Attributable to:		
Owners of the Company	**(823,053)**	2,157,043
Non-controlling interests	**(23,938)**	187,899
	(846,991)	2,344,942

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2016

	Note	2016 RMB'000	2015 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment		**12,698,374**	11,637,977
Construction in progress		**1,271,844**	900,939
Investment properties		**67,486**	20,078
Land use rights		**983,794**	888,680
Goodwill		**4,527,518**	5,850,599
Other intangible assets		**2,086,247**	1,731,018
Investments in associates		**4,132,099**	4,185,883
Deferred tax assets		**529,123**	307,534
Biological assets		**479,386**	289,823
Non-current financial assets		**2,495,681**	2,327,916
Long term prepayments		**15,566**	91,738
Total non-current assets		**29,287,118**	28,232,185
CURRENT ASSETS			
Other current financial assets		**4,195,737**	5,255,273
Derivative financial instruments		**36,501**	10,944
Inventories		**3,314,282**	4,339,506
Trade and bills receivables	*11*	**2,340,099**	1,617,757
Prepayments, deposits and other receivables		**2,704,611**	2,158,884
Pledged deposits		**960,863**	722,402
Cash and bank balances		**6,070,078**	7,931,237
		19,622,171	22,036,003
Assets of disposal groups classified as held for sale		**215,138**	384,353
Total current assets		**19,837,309**	22,420,356

CONSOLIDATED STATEMENT OF FINANCIAL POSITION *(continued)*
As at 31 December 2016

	Note	2016 RMB'000	2015 RMB'000
CURRENT LIABILITIES			
Trade and bills payables	12	**5,405,620**	4,644,298
Other payables and accruals		**6,510,886**	4,989,524
Interest-bearing bank and other borrowings		**3,045,417**	6,080,751
Other loans		**52,559**	43,915
Derivative financial instruments		**–**	3,160
Deferred income		**135,093**	45,652
Income tax payable		**145,242**	153,367
		15,294,817	15,960,667
Liabilities directly associated with the assets classified as held for sale		**7,852**	15,708
Total current liabilities		**15,302,669**	15,976,375
NET CURRENT ASSETS		**4,534,640**	6,443,981
TOTAL ASSETS LESS CURRENT LIABILITIES		**33,821,758**	34,676,166
NON-CURRENT LIABILITIES			
Interest-bearing bank and other borrowings		**5,542,163**	4,969,511
Long term payables		**36,914**	68,399
Deferred income		**533,385**	303,116
Deferred tax liabilities		**62,190**	76,050
Other non-current financial liabilities		**2,143,378**	2,643,936
Total non-current liabilities		**8,318,030**	8,061,012
NET ASSETS		**25,503,728**	26,615,154
EQUITY			
Equity attributable to owners of the Company			
Share capital		**357,374**	357,262
Treasury shares held under share award scheme		**(354,409)**	(415,762)
Other reserves		**12,940,822**	13,321,140
Retained earnings		**7,901,126**	8,873,599
		20,844,913	22,136,239
Non-controlling interests		**4,658,815**	4,478,915
TOTAL EQUITY		**25,503,728**	26,615,154

Notes:

1. CORPORATE AND GROUP INFORMATION

The Company was incorporated as an exempted company with limited liability in the Cayman Islands. The registered office of the Company is located at P.O. Box 309, Ugland House, Grand Cayman KY1-1104, Cayman Islands. The Company is an investment holding company and its subsidiaries are engaged in the manufacture and distribution of dairy products mainly in the People's Republic of China (the "PRC").

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs") issued by the International Accounting Standards Board ("IASB") and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared on a historical cost basis except for share options, certain financial assets and derivative financial instruments which have been measured at fair value. Certain biological assets and agricultural produce upon harvest are measured at fair value less costs to sell. Disposal groups classified as held for sale are stated at the lower of their carrying amounts and fair values less costs to sell. These financial statements are presented in Renminbi ("RMB") and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries (collectively referred to as the "Group") for the year ended 31 December 2016. A subsidiary is an entity (including a structured entity), directly or indirectly, controlled by the Company. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (i.e., existing rights that give the Group the current ability to direct the relevant activities of the investee).

When the Company has, directly or indirectly, less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

(a) the contractual arrangement with the other vote holders of the investee;

(b) rights arising from other contractual arrangements; and

(c) the Group's voting rights and potential voting rights.

The financial statements of the subsidiaries are prepared for the same reporting period as the Company, using consistent accounting policies. The results of subsidiaries are consolidated from the date on which the Group obtains control, and continue to be consolidated until the day that such control ceases.

Profit or loss and each component of other comprehensive income are attributed to the owners of the Company and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control described above. A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises (i) the assets (including goodwill) and liabilities of the subsidiary, (ii) the carrying amount of any non-controlling interest and (iii) the cumulative translation differences recorded in equity; and recognises (i) the fair value of the consideration received, (ii) the fair value of any investment retained and (iii) any resulting surplus or deficit in profit or loss. The Group's share of components previously recognised in other comprehensive income is reclassified to profit or loss or retained profits, as appropriate, on the same basis as would be required if the Group had directly disposed of the related assets or liabilities.

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES

The Group has adopted the following new and revised IFRSs for the first time for the current year's financial statements.

Amendments to IFRS 10, IFRS 12 and IAS 28	*Investment Entities: Applying the Consolidation Exception*
Amendments to IFRS 11	*Accounting for Acquisitions of Interests in Joint Operations*
IFRS 14	*Regulatory Deferral Accounts*
Amendments to IAS 1	*Disclosure Initiative*
Amendments to IAS 16 and IAS 38	*Clarification of Acceptable Methods of Depreciation and Amortisation*
Amendments to IAS 16 and IAS 41	*Agriculture: Bearer Plants*
Amendments to IAS 27	*Equity Method in Separate Financial Statements*
Annual Improvements 2012-2014 Cycle	Amendments to a number of IFRSs

Except for the amendments to IFRS 10, IFRS 12 and IAS 28, amendments to IFRS 11, IFRS 14, amendments to IAS 16 and IAS 41, amendments to IAS 27, and certain amendments included in the *Annual Improvements 2012-2014 Cycle*, which are not relevant to the preparation of the Group's financial statements, the nature and the impact of the amendments are described below:

(a) Amendments to IAS 1 include narrow-focus improvements in respect of the presentation and disclosure in financial statements. The amendments clarify:

(i) the materiality requirements in IAS 1;

(ii) that specific line items in the statement of profit or loss and the statement of financial position may be disaggregated;

(iii) that entities have flexibility as to the order in which they present the notes to financial statements; and

(iv) that the share of other comprehensive income of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statement of profit or loss. The amendments have had no significant impact on the Group's financial statements.

(b) Amendments to IAS 16 and IAS 38 clarify the principle in IAS 16 and IAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through the use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. The amendments are applied prospectively. The amendments have had no impact on the financial position or performance of the Group as the Group has not used a revenue-based method for the calculation of depreciation of its non-current assets.

(c) *Annual Improvements to IFRSs 2012-2014 Cycle* issued in September 2014 sets out amendments to a number of IFRSs. Details of the amendments are as follows:

- IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations:* Clarifies that changes to a plan of sale or a plan of distribution to owners should not be considered to be a new plan of disposal, rather it is a continuation of the original plan. Accordingly, there is no change in the application of the requirements in IFRS 5. The amendments also clarify that changing the disposal method does not change the date of classification of the non-current assets or disposal group held for sale. The amendments are applied prospectively. The amendments have had no impact on the Group as the Group did not have any change in the plan of sale or disposal method in respect of the disposal group held for sale during the year.

3. OPERATING SEGMENT INFORMATION

For management purposes, the Group is organised into business units based on their products and services and has four reportable operating segments as follows:

- Liquid milk products segment – manufacture and distribution of ultra-high temperature milk ("UHT milk"), milk beverages and yogurt;

- Ice cream products segment – manufacture and distribution of ice cream;

- Milk powder products segment – manufacture and distribution of milk powder; and

- Others segment – principally the Group's cheese, plant-based nutrition product and trading business.

Management monitors the results of the Group's operating segments separately for the purpose of making decisions about resources allocation and performance assessment. Segment performance is evaluated based on reportable segment profit/(loss), which is a measure of adjusted profit/(loss) before tax from continuing operations. The adjusted profit/(loss) before tax from continuing operations is measured consistently with the Group's profit/(loss) before tax from continuing operations except that interest income, finance costs, share of profits of associates, income tax expense, as well as head office and corporate expenses are excluded from such measurement.

Segment assets exclude equity investments and other unallocated head office and corporate assets as these assets are managed on a group basis.

Segment liabilities exclude other unallocated head office and corporate liabilities as these liabilities are managed on a group basis.

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

3. **OPERATING SEGMENT INFORMATION** *(continued)*

Year ended 31 December 2016

	Liquid milk products *RMB'000*	**Ice cream products** *RMB'000*	**Milk powder products** *RMB'000*	**Others** *RMB'000*	**Total** *RMB'000*
Segment revenue:					
Sales to external customers	**48,102,872**	**2,179,940**	**3,150,895**	**345,632**	**53,779,339**
Intersegment sales	**536,786**	**128,143**	**–**	**274,220**	**939,149**
	48,639,658	**2,308,083**	**3,150,895**	**619,852**	**54,718,488**
Reconciliation:					
Elimination of intersegment sales					**(939,149)**
Revenue from continuing operations					**53,779,339**
Segment results	**2,708,266**	**(258,975)**	**(2,724,266)**	**(132,689)**	**(407,664)**
Reconciliation:					
Interest income					**477,844**
Finance costs					**(293,700)**
Share of losses of associates					**(225,477)**
Corporate and other unallocated expenses					**(12,389)**
Loss before tax from continuing operations					**(461,386)**
Income tax expense					**(351,379)**
Loss for the year from continuing operations					**(812,765)**
Segment assets	**28,933,430**	**2,309,669**	**12,829,812**	**632,420**	**44,705,331**
Reconciliation:					
Elimination of intersegment receivables					**(8,691,755)**
Corporate and other unallocated assets					**12,895,713**
Assets related to disposal groups					**215,138**
Total assets					**49,124,427**
Segment liabilities	**14,579,687**	**2,183,081**	**3,010,372**	**903,729**	**20,676,869**
Reconciliation:					
Elimination of intersegment payables					**(8,691,755)**
Corporate and other unallocated liabilities					**11,627,733**
Liabilities related to disposal groups					**7,852**
Total liabilities					**23,620,699**

3. **OPERATING SEGMENT INFORMATION** *(continued)*

Year ended 31 December 2016

	Liquid milk products *RMB'000*	Ice cream products *RMB'000*	Milk powder products *RMB'000*	Others *RMB'000*	Total *RMB'000*
Other segment information:					
Depreciation and amortisation	**1,178,533**	**130,095**	**195,193**	**34,671**	**1,538,492**
Unallocated amounts					**63,032**
Total depreciation and amortisation					**1,601,524**
Capital expenditure	**2,422,710**	**304,224**	**1,453,539**	**4,352**	**4,184,825**
Unallocated amounts					**167,663**
Total capital expenditure*					**4,352,488**
Impairment losses recognised in the consolidated statement of profit or loss	**102,113**	**5,801**	**2,338,850**	**2,129**	**2,448,893**
Impairment losses reversed in the consolidated statement of profit or loss	**(14,125)**	**(6,210)**	**(216)**	**(189)**	**(20,740)**
Impairment losses recognised/ (reversed) in the consolidated statement of profit or loss	**87,988**	**(409)**	**2,338,634**	**1,940**	**2,428,153**
Unallocated amounts relating to share option scheme and share award scheme					**40,939**
Total non-cash expenses relating to share option scheme and share award scheme					**40,939**

3. **OPERATING SEGMENT INFORMATION** *(continued)*

Year ended 31 December 2015

	Liquid milk products *RMB'000*	Ice cream products *RMB'000*	Milk powder products *RMB'000*	Others *RMB'000*	Total *RMB'000*
Segment revenue:					
Sales to external customers	43,326,642	2,141,192	3,228,800	329,882	49,026,516
Intersegment sales	417,043	188,830	50,378	236,331	892,582
	43,743,685	2,330,022	3,279,178	566,213	49,919,098
Reconciliation:					
Elimination of intersegment sales					(892,582)
Revenue from continuing operations					49,026,516
Segment results	3,166,684	(235,084)	(67,127)	(244,527)	2,619,946
Reconciliation:					
Interest income					563,273
Finance costs					(318,634)
Share of profits of associates					137,669
Corporate and other unallocated expenses					27,916
Profit before tax from continuing operations					3,030,170
Income tax expense					(510,038)
Profit for the year from continuing operations					2,520,132
Segment assets	26,601,192	1,896,127	14,331,373	1,324,122	44,152,814
Reconciliation:					
Elimination of intersegment receivables					(9,681,088)
Corporate and other unallocated assets					15,796,462
Assets related to disposal groups					384,353
Total assets					50,652,541
Segment liabilities	14,552,301	1,483,008	2,058,501	1,464,801	19,558,611
Reconciliation:					
Elimination of intersegment payables					(9,681,088)
Corporate and other unallocated liabilities					14,144,156
Liabilities related to disposal groups					15,708
Total liabilities					24,037,387

3. **OPERATING SEGMENT INFORMATION** *(continued)*

Year ended 31 December 2015

	Liquid milk products *RMB'000*	Ice cream products *RMB'000*	Milk powder products *RMB'000*	Others *RMB'000*	Total *RMB'000*
Other segment information:					
Depreciation and amortisation	1,096,485	92,171	162,242	35,416	1,386,314
Unallocated amounts					57,974
Total depreciation and amortisation					1,444,288
Capital expenditure	2,100,021	211,880	456,555	8,489	2,776,945
Unallocated amounts					249,975
Total capital expenditure*					3,026,920
Impairment losses recognised in the consolidated statement of profit or loss	45,044	4,893	2,182	1,190	53,309
Impairment losses reversed in the consolidated statement of profit or loss	(81,442)	(2,313)	(200)	–	(83,955)
Impairment losses recognised/ (reversed) in the consolidated statement of profit or loss	(36,398)	2,580	1,982	1,190	(30,646)
Net amortised/(reversal of) fair value relating to share option scheme and share award scheme	12,640	(6,118)	5,726	–	12,248
Unallocated amounts relating to share option scheme and share award scheme					10,117
Total non-cash expenses relating to share option scheme and share award scheme					22,365

* Capital expenditure consists of cash paid for the purchase of property, plant and equipment, construction in progress, intangible assets, land use rights, biological assets, equity interests in subsidiaries, associates and other equity investments.

Geographical information

a. *Revenue from external customers*

Over 90% of the revenue is contributed by customers in Mainland China.

b. *Non-current assets*

Over 90% of the Group's non-current assets are located in Mainland China.

Information about major customers

There was no sales to a single customer which amounted for 10% or more of the Group's revenue for the year ended 31 December 2016 and 2015.

4. REVENUE, OTHER INCOME AND GAINS

Revenue represents the net invoiced value of goods sold, after allowances for goods returns and trade discounts, and after eliminations of all significant intra-group transactions.

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

	2016 ***RMB'000***	2015 *RMB'000*
Revenue:		
Sale of goods	**53,779,339**	49,026,516
Other income and gains:		
Government grants related to		
– Recognition of deferred income	**37,494**	32,939
– Income and biological assets	**183,308**	228,475
Gain on disposal of subsidiaries	**–**	60,232
Gain on disposal of a disposal group classified as held for sale	**29,127**	–
Gain arising from changes in contingent considerations	**–**	95,022
Gain on disposal of items of property, plant and equipment	**–**	10,412
Promotion service income	**134,090**	–
Gross rental income	**47,468**	47,357
Foreign exchange gains, net	**134,235**	–
Others	**136,062**	46,831
	701,784	521,268
	54,481,123	49,547,784

5. OTHER EXPENSES

	Note	**2016** ***RMB'000***	2015 *RMB'000*
Donations		**13,209**	12,362
Fair value change of biological assets		**25,696**	19,323
Loss on disposal of items of property, plant and equipment		**20,634**	–
Impairment of goodwill	*(a)*	**2,253,794**	–
Provision for construction in progress		**1,712**	–
Write-down of inventories to net realisable value		**129,857**	43,806
Provision for trade receivables and other receivables		**63,530**	9,503
Write-back of provision for trade receivables and other receivables		**(20,740)**	(83,955)
Educational surcharges and city construction tax		**235,761**	235,546
Foreign exchange losses, net		**–**	53,754
Net fair value loss on forward currency contracts		**2,371**	12,444
Loss on deemed disposal of partial interests in an associate		**–**	33,045
Others		**124,844**	56,763
		2,850,668	392,591

Note:

(a) During 2016, due to the deterioration of the performance of the Group's milk powder product group of cash-generating units (the "CGU Group"), the carrying amount of the milk powder products CGU Group exceeded its recoverable amount. As such, the Group recognised an impairment loss of RMB2,253,794,000.

6. PROFIT/(LOSS) BEFORE TAX

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

	2016	2015
	RMB'000	*RMB'000*
Cost of inventories sold	**36,157,504**	33,663,028
Realised and unrealised fair value gains of commodity futures contracts, net	**(13,567)**	(11,986)
Cost of sales	**36,143,937**	33,651,042
Employee benefit expense (including directors' and chief executive's remuneration)		
– Wages, salaries, housing benefits and other allowances	**4,051,872**	3,095,035
– Retirement benefit contributions	**386,663**	321,522
– Share option scheme expense	**–**	(69,359)
– Share award scheme expense	**40,939**	91,724
	4,479,474	3,438,922
Depreciation of items of property, plant and equipment	**1,536,404**	1,391,302
Depreciation of investment properties	**2,457**	3,030
Amortisation of land use rights	**24,760**	26,005
Amortisation of other intangible assets	**37,903**	23,951
Research and development costs – current year expenditure	**108,141**	81,900
Outsourcing expense	**256,752**	483,914
Minimum lease payments under operating leases	**230,752**	196,825
Display space leasing fees	**949,638**	789,301
Auditor's remuneration *(a)*	**6,795**	7,510

(a) In addition to the above fees paid or payable to the auditors, Yashili International Holdings Ltd ("Yashili"), a Hong Kong Main Board listed subsidiary of the Group, had an amount of RMB3,190,000 (2015: RMB2,930,000) paid/payable as auditors' remuneration during the year.

7. FINANCE COSTS

An analysis of finance costs from continuing operations is as follows:

	2016 *RMB'000*	2015 *RMB'000*
Interest on bank loans	**186,731**	188,110
Interest on US$500,000,000 3.50% bond due 2018	**125,914**	114,423
Interest on long term payables	**6,744**	6,502
Increase in discounted amounts of contingent considerations arising from the passage of time	**549**	8,918
Net fair value loss/(gain) on interest rate forward contracts	**(26,238)**	681
	293,700	318,634

8. INCOME TAX EXPENSE

Under the Law of the People's Republic of China on Corporate Income Tax ("PRC CIT law"), except for certain preferential tax treatment available to certain subsidiaries of the Group, the entities within the Group are subject to PRC corporate income tax ("CIT") at a rate of 25% (2015: 25%) on the taxable income as reported in their statutory accounts which are prepared in accordance with the PRC accounting standards and financial regulations.

	2016 *RMB'000*	2015 *RMB'000*
Current income tax		
Current charge for the year	**515,010**	444,910
Adjustments recognised in the year for current tax of prior years	**28,200**	13,196
Deferred income tax	**(191,831)**	51,932
	351,379	510,038

A reconciliation of the income tax expense applicable to profit/(loss) before tax at the statutory income tax rate to the income tax expense at the Group's effective income tax rate for the year is as follows:

	Notes	2016 *RMB'000*	2015 *RMB'000*
Profit/(loss) before tax from continuing operations		**(461,386)**	3,030,170
At CIT rate of 25% (2015: 25%)		**(115,347)**	757,543
Non-deductible items and others, net	*(a)*	**553,309**	(4,896)
Adjustment recognised in the year for current tax of prior years		**28,200**	13,196
Effect of lower tax rates	*(b)*	**(132,385)**	(94,433)
Effect of tax exemptions	*(b)*	**(191,709)**	(201,942)
Losses/(profits) attributable to associates		**56,369**	(25,912)
Tax losses utilised from previous periods		**(83,056)**	(38,357)
Tax losses not recognised		**235,998**	104,839
At the effective income tax rate		**351,379**	510,038

8. INCOME TAX EXPENSE *(continued)*

Notes:

(a) Included in the non-deductible items was an item relating to the impairment provision of goodwill related to the milk powder product CGU Group amounting to RMB563,449,000 in 2016 (2015: Nil).

(b) Thirteen (2015: fifteen) subsidiaries were granted lower tax rates by the state tax bureau in accordance with the PRC CIT law and the corresponding transitional tax concession policy and "The notice of tax policies relating to the implementation of the western China development strategy."

Twenty-eight (2015: twenty-two) subsidiaries were granted tax exemptions in accordance with the policy of "The notice of preferential tax policy for preliminary processing of agriculture products".

The total taxable profits of the subsidiaries that are subject to tax concessions amounted to approximately RMB1,635,273,000 (2015: RMB1,102,545,000) in aggregate.

(c) The share of tax attributable to associates amounting to approximately RMB7,491,000 (2015: RMB3,641,000) is included in the share of profits of associates on the face of the consolidated statement of profit or loss.

9. DIVIDENDS

	Notes	**2016** ***RMB'000***	2015 *RMB'000*
Declared and paid during the year			
Equity dividends on ordinary shares		**552,697**	546,923
Proposed for approval at the AGM			
Equity dividends on ordinary shares: Proposed final – RMB0.089 (2015: RMB0.140) per ordinary share	*(a)/(b)*	**349,327**	549,357

Notes:

(a) The proposed final dividend for the year is subject to the approval of the Company's shareholders at the forthcoming Annual General Meeting (the "AGM").

(b) This dividend was not recognised as a liability in the consolidated financial statements as at 31 December 2016 but will be reflected as an appropriation of share premium account for the year ending 31 December 2017.

10. EARNINGS/(LOSS) PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY

(a) Basic earnings/(loss) per share

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

A reconciliation of the weighted average number of shares used in calculating the basic earnings/(loss) per share amount is as follows:

	2016 Number of shares ***'000***	2015 Number of shares *'000*
Issued ordinary shares at 1 January	**3,923,977**	1,958,591
Effect of shares repurchase and cancellation	**(5,052)**	–
Effect of bonus shares	**–**	1,961,292
Effect of share options exercised	**2,550**	2,391
Effect of shares purchased under share award scheme	**(35,300)**	(33,073)
Weighted average number of ordinary shares for the purpose of the basic earnings/(loss) per share calculation	**3,886,175**	3,889,201

(b) Diluted earnings/(loss) per share

The diluted earnings/(loss) per share is calculated by dividing the profit/(loss) for the year attributable to ordinary equity holders of the Company by the weighted average number of ordinary shares in issue during the year, as used in the basic earnings/(loss) per share calculation, and the weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed exercise or conversion of all dilutive potential ordinary shares into ordinary shares.

No adjustment has been made to the basic loss per share amount presented for the year ended 31 December 2016 in respect of a dilution because the impact of the share options and shares under share award scheme outstanding had an anti-dilutive effect on the basic loss per share amount presented.

For the year ended 31 December 2015, the reconciliation of the weighted average number of shares used in calculating the diluted earnings per share amount is as follows:

	2015 Number of shares *'000*
Weighted average number of ordinary shares for the purpose of the basic earnings per share calculation	3,889,201
Weighted average number of ordinary shares, assuming issued at no consideration on the deemed exercise of all share options during the year	3,281
Adjustments for share award scheme	4,761
Weighted average number of ordinary shares for the purpose of the diluted earnings per share calculation	3,897,243

11. TRADE AND BILLS RECEIVABLES

	2016	2015
	RMB'000	*RMB'000*
Bills receivable	**212,780**	191,462
Trade receivables	**2,198,968**	1,500,562
Impairment	**(71,649)**	(74,267)
	2,340,099	1,617,757

The Group normally allows a credit limit to its customers which is adjustable in certain circumstances. The Group closely monitors overdue balances. In view of the aforementioned and the fact that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. The Group does not hold any collateral or other credit enhancements over its trade receivables. The trade receivables are non-interest-bearing.

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

	2016	2015
	RMB'000	*RMB'000*
Within 3 months	**2,041,533**	1,389,573
4 to 6 months	**224,670**	94,581
7 to 12 months	**63,584**	50,881
Over 1 year	**10,312**	82,722
	2,340,099	1,617,757

12. TRADE AND BILLS PAYABLES

An aging analysis of the trade and bills payables of the Group, based on the invoice date, is as follows:

	2016	2015
	RMB'000	*RMB'000*
Within 3 months	**4,733,321**	4,005,836
4 to 6 months	**638,773**	602,214
7 to 12 months	**23,768**	29,781
Over 1 year	**9,758**	6,467
	5,405,620	4,644,298

13. A MATERIAL BUSINESS COMBINATION

Acquisition of Dumex China

On 31 May 2016, Yashili, a 51.01% indirectly owned subsidiary of the Company, acquired a 100% equity interest in Dumex China from Danone Asia Pacific Holdings Pte. Ltd. ("Danone"). Dumex China is mainly engaged in the manufacture and sale of infant milk formula products of Dumex brand. The acquisition was made as part of the Group's strategy to expand its market share of infant milk formula products in Mainland China.

The purchase consideration for the acquisition was in the form of cash, with RMB1,099,695,000 paid at the acquisition date and RMB72,437,000 of purchase price adjustments received from Danone after the closing of the transaction.

The fair values of the identifiable assets and liabilities of Dumex China as at the date of acquisition were as follows:

	Fair value recognised on acquisition *RMB'000*
Assets	
Property, plant and equipment	**68,290**
Construction in progress	**7,473**
Land use rights	**41,527**
Other intangible assets	**283,120**
Inventories	**64,945**
Trade and bills receivables	**63,887**
Prepayments, deposits and other receivables	**14,116**
Cash and bank balances	**112,071**
Total assets	**655,429**
Liabilities	
Trade and bills payables	**(43,626)**
Other payables and accruals	**(302,909)**
Current tax payable	**(112)**
Total liabilities	**(346,647)**
Total identifiable net assets at fair value	**308,782**
Add: Goodwill arising on acquisition	**718,476**
Purchase consideration at fair value	**1,027,258**

13. A MATERIAL BUSINESS COMBINATION *(continued)*

Acquisition of Dumex China *(continued)*

The fair values of the trade receivables and other receivables as at the date of acquisition were same as the gross contractual amounts of trade receivables and other receivables, which amounted to RMB63,887,000 and RMB14,116,000, respectively.

The Group incurred transaction costs of RMB5,510,000 for this acquisition. These transaction costs have been expensed and are included in administrative expenses in the consolidated statement of profit or loss.

An analysis of the cash flows in respect of the acquisition of Dumex China for the current year is as follows:

	RMB'000
Cash consideration	**1,099,695**
Receipt of purchase price adjustments	**(72,437)**
Cash and cash equivalents acquired	**(112,071)**
Net outflow of cash and cash equivalents included in cash flows from investing activities	**915,187**
Transaction costs of the acquisition included in cash flows from operating activities	**5,510**
	920,697

Since the acquisition, Dumex China contributed RMB101,089,000 to the Group's revenue and caused net loss of RMB55,905,000 to the consolidated profit for the year ended 31 December 2016.

Had the combination taken place at the beginning of the year, the revenue from continuing operations of the Group and net loss of the Group for the year ended 31 December 2016 would have been RMB53,908,797,000 and RMB961,984,000 respectively.

14. EVENTS AFTER THE REPORTING PERIOD

The Group held 1,347,903,000 shares in Modern Dairy, representing 25.4% of the issued share capital of Modern Dairy as at 31 December 2016.

On 7 February 2017, the Group completed the acquisition of 965,465,750 Modern Dairy's shares, with cash consideration of HK$1,873,003,555, which is equivalent to HK$1.94 per Modern Dairy's share. As such, up to 7 February 2017, the Group owned an aggregate of 2,313,368,750 Modern Dairy's shares, representing approximately 37.7% of the issued share capital of Modern Dairy. Accordingly, the Group made a conditional mandatory cash offer (i) for all the issued Modern Dairy's shares (other than those already owned or agreed to be acquired by the Group), and (ii) for cancellation of all outstanding Modern Dairy's options (the "Cash Offer") on 14 February 2017.

On the final closing date of the Cash Offer on 21 March 2017, taking into account the valid acceptances in respect of 1,442,400,662 Modern Dairy's shares, the Group would hold an aggregate of 3,755,769,412 Modern Dairy's shares (representing approximately 61.3% of the issued share capital of Modern Dairy as of 21 March 2017).

Further details of the above transactions were included in the Company's announcement dated 4 January 2017, 25 January 2017, 7 February 2017, 14 February 2017, 7 March 2017 and 21 March 2017, respectively.

MANAGEMENT DISCUSSION AND ANALYSIS

INDUSTRY REVIEW

In 2016, the market continued to be laden with challenges with the Chinese economy facing downward pressure. The dairy industry in China, however, revived with dairy products output up and price relatively stable. At the same time, dairy consumption moved obviously toward the high-end, as reflected in the gradually increasing consumption volume of high added-value products such as high-end UHT milk and yogurt. With improvement in the consumption level, brand awareness and health consciousness of the Chinese people, as well as dairy enterprises keep enhancing their products structure and business strategy, the impending consumption upgrade will drive the industry to further development. High-end products, especially high-end UHT milk and chilled products, will continue to boast relatively more rapid growth and make up a major share of the liquid milk product category. Furthermore, new dairy products such as cheese are likely to become new star products of the industry.

International raw milk price went through cyclical adjustments in 2016, and milk price in the domestic market also tuned as a result of improvement in the demand and supply structure. Competition among domestic dairy enterprises remained fierce; however, with the cost structure changing, it is likely that competitive landscape will ease in the future for the industry. On the other hand, the domestic dairy industry, especially the infant milk formula sector, has been facing challenges on various aspects, such as the sales system, from the impact of international players and cross-border e-commerce merchants. Against this backdrop, domestic dairy enterprises have not only strengthened internal management and monitoring of food safety to keep improving product quality, but are also embracing Internet marketing, using innovative and interactive online tactics to engage and communicate with consumers, building a new type of sales and marketing platform.

Since 2016, the regulatory authorities in China have tightened supervision on and inspection of infant milk formula products. The effects of these moves on market discipline are expected to manifest gradually. Under the impact of the infant milk formula registration system and the full rollout of the two-child policy, the demand and supply structure of the domestic milk formula industry has been improving, with enterprises and production capacities unable to meet relevant regulatory requirements to be ousted from the market. High-end products will be the main battle field in the future.

BUSINESS REVIEW

In 2016, Mengniu continued to perfect its international resources setup, which enabled it to fully utilize its global resources and industrial chain advantages to guard the product safety of Chinese dairy products on par with relevant international standards, and to make Chinese brands stronger. On top of continuously improving product quality, the Group has also worked hard on product differentiation in terms of brands and product categories, and, has allocated more resources to research and development of innovative products and product upgrade, thereby guiding the new nutritional demands of consumers. Furthermore, Mengniu has been active in optimizing its organizational structure and improving overall operational efficiency with the consumer and market demands in mind. At the end of 2016, Mengniu started to implement a new business division system that comprises independent business segments including room temperature, chilled, milk formula and ice cream products, aiming for a balanced development of the different business segments and to strengthen synergy among the resources and risk management. Moreover, through digitalized management, Mengniu has built itself into an intelligent dairy enterprise using Big Data. It was able to manage product quality and sales and marketing with innovation by employing a management and tracking system that covers its entire industrial chain.

Mengniu kept its leading position in the liquid milk market in 2016. Despite the fierce market competition, the room temperature products *Milk Deluxe* reported growth surpassing that of the industry, and *Just Yoghurt* also recorded substantial increase in revenue and market share. As for chilled products, Mengniu has kept the top spot in terms of market share throughout the year, maintaining its solid market leadership position. In regard to milk formula business, with challenges coming from international brands and cross-border e-commerce merchants and the brand upgrade and sales channel transformation, the improvement in operational efficiency and production capacity is expected to be seen gradually.

During the year, Mengniu once again made it among the top 20 on the BrandZ™ 2016 list of the most valuable Chinese brands. In addition, the Group's liquid milk and yogurt topped their respective categories in the sixth China Brand Power Index (C-BPI) published by the Ministry of Industry and Information Technology of the PRC in 2016. That was the third consecutive year Mengniu made the two top C-BPI rankings and for its yogurt products the sixth consecutive win, taking home the "Golden Brand" title. In the third Media Cooperation Forum on Belt and Road organized by the *People's Daily*, Mengniu was awarded the "Case Prize of the Belt & Road Initiative in 2016". Mengniu was also honored "The Best Corporate Governance Awards 2016 – Gold Award" by *Asset Magazine*, being the only dairy enterprise to be honored. In addition, at the 10th Global Dairy Congress, *Hi Milk*, Mengniu's premium customized milk, garnered the "Best Dairy Product" and "Best Packaging of Dairy Products" awards under the World Dairy Innovation Awards. Mengniu was the only Chinese dairy enterprise that won two major awards at that event. And, *Yashiliy* and *Ruipuen*, the Group's infant milk formula products, were both awarded "Gold Prize – Quality" from the China Dairy Industry Association in 2016, a reflection of the market recognition and confidence that Mengniu enjoys for its quality products.

Strategic Cooperation and Integration

– *Chilled product business: Danone S.A. and its subsidiaries ("Danone Group")*

Danone Group, which owns 9.9% stake in Mengniu, is Mengniu's second largest strategic shareholder. Inner Mongolia Mengniu Danone Dairy Co., Ltd. ("Mengniu Danone") is a joint-equity company held 80% by Mengniu and 20% by Danone Group.

In 2016, Mengniu Danone continued to boast leadership in the domestic chilled dairy products market, placing first in the market by virtue of commendable growth in sales. Applying a digitalized management system, Mengniu Danone was able to enhance matching of sales demand with raw material procurement and production capacity, starting at the beginning of its production management system, thus achieving a better balance between production and sales. In addition, the Group was able to improve cost management effectiveness by using PET bottles and optimizing product formula.

Regarding the Ma'anshan plant of Mengniu Danone, it completed a capacity upgrade during the year, stepped up cost control and notably reduced wastage, which translated into a substantial increase in production efficiency. The successful experience of the plant will be promoted at the other 15 fresh dairy products plants. Mengniu Danone's Jinhua plant officially began operation in 2016 adopting the unified food safety and quality standards used by Danone Group, making it the plant with the highest level of digitalization in the Group. The plant is able to maintain to the largest extent the original texture and taste of products and, at the same time, afford production processes that are more environmentally-friendly and conducive to energy conservation.

Mengniu Danone is dedicated to ensuring product quality and also innovation. It released five new products to the market during the year. Among them, *Yoyi C* launched the innovative cross-segment Live Tea series, a perfect blend of Indian black tea, the Longjing green tea, and probiotics. The Live Tea series launched had complemented a series of online and offline promotional initiatives enabling it to attract patronage of young consumers. And, *Yoyi C* obtained patent for its proprietary "Temperature Self-regulation Digital System", which can effectively ensure the stability of probiotics in the products. *Champion* added the Red+ yogurt series to its name, the first yogurt series – pomegranate & rose and cherry & rose – in the market that features red super fruit and fragrant flower flavors, which has won the heart of many female consumers. Furthermore, to its basic yogurt products, Mengniu Danone included the new product *Nourishing Oats and Red Dates Flavor Yogurt* in small bottle in January 2016. Driven by product innovation, the chilled product business segment achieved continuous growth in sales during the year. Drawing on Danone Group's advanced international technologies and capabilities in quality management and product innovation, and Mengniu's own strength in distribution, Mengniu Danone will continue to develop high-end dairy products and set the trend for the country's chilled dairy products market.

– *Arla Foods*

Mengniu has tapped into Arla Foods' century-long experience to optimize the quality of milk source thereby consolidating its core competitiveness. The Group also brought in Arla Foods' advanced ranch management system to help establish China's own dairy farming economy that embraces a new technology management model and fostered personnel with professional expertise in dairy production as well as in management. In 2016, Mengniu and Arla Foods stepped up cooperation on ranch management. The Standard Operational Procedure ("SOP") brought in from Arla Foods was modified and localized based on the practical situations and management experience of ranches in China, and detailed specifications were drawn up for several hundred key points in the production process, thereby standardizing every aspect of production control. At the same time, Mengniu introduced more lean management projects, and organized training programs on SOP and lean management in November 2016 for technical managers of the milk source operation from the headquarters and regional offices, to ensure that the Group has access to quality milk sources of international standard.

Mengniu and Arla Foods continued to exhume more synergies on the research and development and production fronts. Reaching deep into the experiences of the organic farms and agricultural research centers in Denmark for insights, the Group was able to promote product and nutrition innovation in categories including room temperature products, high-end organic milk formula and cheese products. Such endeavors have enabled Mengniu to pilot consumption upgrade and build a Chinese dairy brand which is confident of the quality of its products and its ability to innovate.

– *Milk formula business: Yashili International Holdings Ltd ("Yashili"; stock code: 1230)*

Mengniu holds an approximately 51% stake in Yashili and is its controlling shareholder. Yashili completed the acquisition of Dumex China from Danone Group on 31 May 2016. Dumex China mainly engages in the business of infant milk formula products. Through acquiring Dumex China, Yashili improved its production network by integrating the advanced manufacturing facilities of Dumex China with its own and optimizing those facilities. Furthermore, Yashili also has access to the research and development capabilities of Dumex China and the resources support of Danone Group, which raises the product development standards.

During the year, the size of the domestic infant formula market remained the same as last year with prices up and sales down. In general, the industry faced huge challenges from imported international brands and cross-border e-commerce merchants. In 2016, Yashili was in a critical stage of reform, embarking on sales channel transformation and integration of production capacity to enhance supply chain operations and boost its responsiveness to the market. On this basis, Yashili changed its marketing and sales structure to "four CBUs plus one project department", which provided the sales team more clearly defined objectives and facilitated sales channel transformation. Feeling the detrimental blow of the Internet, traditional business channels have continued to shrink. Yashili has actively coped with this new development trend by investing in the sales and marketing team and enhancing the model of the mother-and-baby store and e-commerce channels. On the e-commerce front, Yashili has transformed its single sales platform into a multi-dimensional and consumer-oriented business platform, and has been adopting delicacy management for more differentiated product lines, as a result of which, online sales have been on steady climb. As for mother-and-baby channels, Yashili has increased the proportion of such channels among all channels via promoting its "all staff engaging in mother-and-baby store channel" program.

Yashili is the only milk formula brand in China with its own factory in New Zealand. Yashili's New Zealand factory signed a strategic cooperation supply agreement with Danone Group, which will allow it to improve utilization rate of its production capacity thereby reducing production cost. In April 2016, Yashili's *Super α-Golden*, a newly developed milk formula product directly canned in New Zealand, was launched for sale via various channels including mother-and-baby channels and e-commerce platforms in China and New Zealand, helping Yashili build a "professional, international, high-quality" image.

Furthermore, Yashili has brought in the superior high-end brand of Arla Foods to enrich its product lines, gradually optimizing the positioning of its product portfolio. By strengthening collaboration with its partners such as Danone Group and Arla Foods, Yashili has been propelling growth of brands including *Baby & Me*, *Dumex* and *Ruipuen* in high-end markets and first-tier cities, which will bear positively on its future operation.

With the implementation of the milk formula registration system and the positive impact of the full rollout of the two-child policy in China gradually noticeable, the infant milk formula sector is expecting to see the surface of new opportunities. Yashili will continue to improve its operations on such fronts as brand upgrade, sales channel transformation, product research and development, quality management and system support, and strive for stronger synergies with its partners, as well as to capture any promising development opportunities.

– *Plant-based nutrition product business: The WhiteWave Foods Company ("WhiteWave")*

Mengniu and WhiteWave formed an equity joint venture in April 2014, in which Mengniu and WhiteWave holds 51% and 49% equity interest respectively.

Produced using the world-leading advanced μ-Grind™ grinding technology, the plant-based beverage brand *Silk ZhiPuMoFang* jointly developed by Mengniu and WhiteWave retains the nutritional content of the original ingredients and presents the most healthy taste to consumers. After launching the plant protein beverage of two flavors, namely walnut and almond, the joint venture marketed in May 2016 a series of new products of various flavors. In addition to refining the existing two flavors, it also launched the Mellow Soy Milk series. New products are developed using WhiteWave's leading technology in the field of plant-based nutritional products, with taste and feel more agreeable with the palate and preference of consumers. The low sugar content formula also fits in with the healthy diet need of today's consumers. The product series adds to the portfolio of the high-end plant protein beverage market and gives more nutritional choices to consumers in China.

In addition, Mengniu updated the packaging of the product with the English logo *Silk* highlighted even more vividly to emphasize that the products have "superior genes" originated in the United States. Thanks to product innovation and Mengniu's existing market and channel advantages, sales of *ZhiPuMoFang* increased notably in the second half of 2016.

The plant protein beverage market has seen rapid growth in recent years. As consumers' income level and food consumption level continue to rise, foods of better quality and that offer more balanced nutrition have become increasingly popular, thus plant protein beverages deemed natural, nutritious and healthy have tremendous market potential in China. The acquisition of WhiteWave by Danone Group is expected to give Mengniu's plant protein beverage business more access to support from Danone Group. The joint venture will step up integration with the existing market and channel resources of Mengniu's core business and continue to diversify its product lines, building the competitive strengths of its products in the plant-based nutritional product arena. Such moves will give Mengniu the differentiating edge to stand out in the industry.

– *China Modern Dairy Holdings Ltd. ("Modern Dairy", stock code:1117)*

On 4 January 2017, Mengniu announced to purchase 965,465,750 additional shares of Modern Dairy, representing approximately 15.7% of the total issued share capital of Modern Dairy upon completion of the relevant share purchase agreement, for a consideration of approximately HK$1.9 billion. Upon completion of such acquisition, Mengniu beneficially held approximately 37.7% of the total issued share capital of Modern Dairy, and conditional mandatory cash offers (the "Offers") were triggered to acquire all the issued shares in Modern Dairy (other than those already owned or agreed to be acquired by Mengniu) and for cancellation of all outstanding options in Modern Dairy. Such transaction was approved at the extraordinary general meeting of the Company held on 3 February 2017. Mengniu announced on 7 March 2017 that the Offers were unconditional in all aspects, and announced on 21 March 2017 that the Offers were closed at 4:00 p.m. of that day. Under the Offers, Mengniu received valid acceptances in respect of a total of 1,442,400,662 shares of Modern Dairy (representing approximately 23.5% of the entire issued share capital of Modern Dairy) and in respect of a total of 264,320,873 outstanding options in Modern Dairy (representing approximately 83.8% of the total number of outstanding options in Modern Dairy). Immediately following the close of the Offers, taking into account the valid acceptances in respect of 1,442,400,662 shares of Modern Dairy under the Offers, Mengniu would hold an aggregate of 3,755,769,412 shares of Modern Dairy (representing approximately 61.3% of the issued share capital of Modern Dairy). The listing status of Modern Dairy was maintained after the close of the Offers. Please refer to the Company's announcements dated 4 January 2017, 25 January 2017, 7 February 2017, 14 February 2017, 7 March 2017 and 21 March 2017 for details.

According to the Dairy Association of China, in terms of herd size, Modern Dairy is the largest dairy farming company as well as the largest raw milk producer in China. It is the first to bring in advanced international management model to China's dairy breeding industry, in its hope to provide safe and quality dairy products to consumers. Modern Dairy is a long-term partner of Mengniu and its largest raw milk supplier. The further equity investment in Modern Dairy will enable Mengniu to smoothen upstream and downstream cooperation, thus creating a more harmonious industry ecosystem. The strict raw milk production process of Modern Dairy will assure Mengniu of supply of quality milk sources, conducive to the development of chilled products business, and also to help enrich its mid-range and high-end product lines and fortify its leadership in the high-end dairy products market.

Quality Management

"Perfect products" is the new milestone in quality management development that Mengniu is pushing forward as it embraces the strategic mission of giving the perfect experience to consumers by providing them with safer, healthier and more nutritious products. During the year, Mengniu continued to apply end-to-end quality management to strictly control risks throughout the entire industrial chain from milk source to production and sales. A quality information system has been established with coverage that stretches from the ranch to the dining table to improve overall product quality. Through achieving constant synergistic operation of the Laboratory Information Management System ("LIMS") and SAP system combined with its own quality management and laboratory management systems, Mengniu has been able to assure quality systematically using intelligent technologies throughout the entire industrial chain, from delivery of raw milk to factories, procurement of raw/auxiliary materials, production processes to the point-of-sale. It is able to track information forward and backward at all quality control points along the industrial chain of the products. The LIMS-SAP system has since been introduced in the entire industrial chain, including to the Dumex plant in Shanghai, the ZhiPuMoFang plant in Jiaozuo and Yiqing plant in Linxia.

In alignment with the food safety management model of Danone Group, Mengniu's quality and safety management system is constantly upgraded and applied in the food safety and risk management mechanism that covers the entire industrial chain. It has built a digitalized "Real-time Food Safety and Quality Monitoring and Control Platform" of international standard that monitors real time food safety in every stage covering ranches, production plants and major sales regions. Product quality data are uploaded onto a "Food Safety Cloud" platform, realizing informatization of the entire industrial chain from ranches and factories to markets, for maintaining transparent communication with regulators as well as consumers. In 2016, Mengniu and Beijing Entry-Exit Inspection and Quarantine Bureau jointly implemented the "Quality and Safety Tracing System of Beijing Entry-Exit Inspection and Quarantine Bureau – Mengniu Project", which involved the implementation and application of information tracing management system. Mengniu is the first dairy enterprise to join and be covered by the system.

Mengniu is a pioneer in China dairy industry in building a quality cloud platform, which provides advanced international management platform for Mengniu's quality management systematization. During the year, supported by the salesforcePaaS cloud platform, Mengniu's quality information assessment system QA-Cloud has permitted the Group to realize multi-platform interaction, dynamic monitoring of food safety and sharing and exchange of quality assessment index. With the system, Mengniu can communicate and interact real time with quality-relevant parties including Danone Group, which laid a solid foundation for advancing the quality informationization in the future. By strengthening internal review, using advanced quality analysis tools to analyze Big Data as collected via the Group's quality risk warning system, the Group could timely grasp the quality trend and thus able to prevent quality risks. Mengniu has also been improving its quality management through the implementation of seasonal quality prevention management that entails warning and preventive control with regard to specific links in the entire industrial chain.

Mengniu has optimized a food safety security matrix which covers horizontally the entire industrial chain and vertically five major dimensions, namely standard specification, source management, process control, assessment improvement and digitalized assurance. General management covers six major dimensions, namely personnel, equipment, materials, environment, methods and inspection, forming a food safety security network system that guards all procedures. Through adopting procedural control and inspection means, products are given dual guarantee to their quality and safety standards. During the year, Mengniu started to develop a "One-stop Position Management System" to establish a scientific management mechanism for ensuring its business operations complying with quality management, food safety management requirements and relevant laws and regulations. Such a move can facilitate thorough implementation of the Total Food Security Quality Management (TFSQM) system that serves the entire industrial chain. And the Group's "Quality 100 Talent" training platform has enabled it to groom teams of quality experts. Mengniu also worked with third party institutions on food safety monitoring, testing and studying food safety standards from the perspective of consumers' nutrition and health.

On quality management of milk sources, all of the Group's business divisions actively responded to the stricter national standards. In particular, they enhanced their self-inspection capability in four major areas, namely dairy cattle, milk, fodder and equipment, and at the same time, increased the frequency of inspection on milk suppliers and tightened inspection requirements as well. During the year, milk suppliers of Mengniu's various business divisions passed 100% the tests conducted by inspection organizations on samples of raw milk.

The operation quality management center has quantified the definition and benchmark of a "perfect product", and the assessment was carried out in various aspects of the product including its content, exterior packaging and consumer experience. Two interactive sessions to help the alignment of perfect product benchmarks throughout the entire industrial chain were organized during the year, the purpose of which was to ensure consumers would have an experience that exceeds their expectation. At the same time, the Group made sure it has full control over various operational stages such as formula design, packaging design, maintenance of production process and storage and delivery logistics, allowing it to boost the core competitiveness of its products with quality assured. Also, using Internet technology, Mengniu has built an online platform dedicated to craftsmanship standards and, taking reference of IBM's intelligent factory management resources, has come up with its own Total Quality Management ("TQM") analysis model. Moreover, it made technological innovation breakthroughs, empowering it for delicacy management and substantial reduction of quality safety risks. During the year, the laboratories in Jiaozuo, Shenyang, Ma'anshan and Wuhan were examined by the China National Accreditation Service for Conformity Assessment, and worked with the authority on compiling the "Guidance on technical requirements of enterprise internal testing laboratory", helping to lead the development of accreditation procedures for in-house laboratories of Chinese enterprises.

The sales quality management center has further propelled construction of cold chain at the sales terminals by conducting qualification reviews and risks investigation on distributors to ensure proper execution of cold chain management standards by them. Risk assessments on distributors in respect of their operating qualifications for chilled dairy products was completed during the year. And, the cold chain temperature control system which was already in trial operation performed well. Mengniu continued to strengthen traceability of products from delivery out of plants to the point-of-sale, with tracking of key products and markets on weekly basis. It has compiled full product batch records for 80 major markets in the country and informationized technologies are applied in tracing major products. To help its partners enhance quality safety management, Mengniu has signed approximately 10,000 letters of commitment in respect of food safety with distributors, with execution rate amounting to 100%, to assure the quality and safety of its products.

The first domestic ranch food safety standards, which were jointly developed by Mengniu and New Zealand state-owned enterprise AsureQuality, have been applied at 119 control points, focusing on food safety management in ranches. Mengniu, in collaboration with third party institutions, have conducted food safety reviews on operations of its strategic partners to identify potential defects and risks and offer remedies and improvement suggestions, thereby helping the Group's strategic ranches execute food safety management system to assure food safety at the source. In 2016, Mengniu assisted its five strategic partners, namely Modern Dairy, Fuyuan Farming, Shengmu Group, Saikexing Group and YuanShengTai Dairy Farm, to conduct food safety reviews over a total of 21 ranches. Mengniu, together with third parties, recommended to the National Animal Husbandry Service to use these standards as code of conduct applicable for the entire industry, targeting to improve the overall food safety management of the industry.

Development of milk sources

Mengniu continued to develop the "2020 Sustainable Ecosystem of Milk Sources", and effectively promoted the improvement of the management techniques of milk suppliers with focus on five aspects – "Control of Regional Risk", "Upgrade of Production Bases", "SOP Standardization in Ranches", "W-W Virtual Dairy Farming" and "P+ Project of Milk Source Bases". By bringing in advanced international resources and technologies, as well as employing digitalization, informatization and other new technologies, Mengniu has continued to strengthen its milk sources foundation in aspects including deployment, structure, quality and technology, in order to optimize milk quality and minimize food safety risks. During the year, the percentage of Mengniu's milk sourced from standardized ranches and scaled farms reached 100%.

Braced by the advanced and century-long experience of Arla Garden in ranch management and heeding local conditions and situations, Mengniu has built the Mengniu Garden ranch management ecosystem to speed up construction of a modernized milk source system. The system has standards in relation to nutrients of raw milk, quality safety, animal welfare and the breeding environment that aligns with those of Arla Foods. During the year, Mengniu together with third party strategic milk supplying partners conducted food safety reviews to make sure applicable food safety standards were implemented at strategic ranches and helped drive improvement of the overall level of food safety management in the industry.

Mengniu has adopted advanced ranch management SOP standard from Denmark-based Arla Foods, to help it fortify the foundation for establishing standardized ranches and strengthen its ability to apply delicacy management of technologies, and in turn enhance the operational capability of ranches in China. For the raw milk production chain, Mengniu cooperated with the National Dairy Industry Technology System, the SEGES (formerly known as Knowledge Center of Agriculture of Denmanrk) and expert ranch operators to establish the "Mengniu

Ranch Technology SOP" for general application, and for specific regions, dedicated terms were drawn up with the help of regional experts across the nation. Ranches in different regions can apply SOP standards befitting the cattle rearing conditions of their respective regions to improve their operation and contribute to the healthy development of the country's dairy industry.

During the year, Mengniu went ahead in full scope with promotion of the "W-W Virtual Dairy Farming" project, targeting to tighten cooperation with milk suppliers and improve operating performance of ranches. During the year, the project achieved coverage of more than 500 milk suppliers and approximately 80% of the front-line staff of milk sources department, and the concept of contractual responsibility was applied in selected ranches. Mengniu aligned the advanced assessment management system of Arla Garden with its own, focusing on four major modules namely source management, outcome assessment, technology management and financial management, to help milk suppliers effectively enhance profitability and minimize internal operating costs. The "W-W Virtual Dairy Farming" project was presented the "Second Class National Innovation Award" in 2016.

Guided by the central government's "Grain to Fodder" policy, Mengniu has given support, in terms of capital aid and technical guidance, to ranches in the scientific use of corn silage in feeding. The use of silage in scaled farms has reached 100%, which effectively resolved the problem concerning the feeding of milk cattle. At the same time, to improve the overall milk cattle rearing husbandry standard in the country, Mengniu completed infrastructural upgrade during the year to improve the living environment of milk cattle, hence laid the foundation for enhancement of raw milk quality.

To strengthen supervision on and management of raw milk production at ranches, and gradually realize digitalized and intelligent management of raw milk production and the entire delivery process of raw milk, Mengniu implemented the "Ranch Monitor Project" in five selected business units in two major sales regions, namely northern China and Liaoning & eastern Inner Mongolia regions, during the year. The monitoring facilities in ranches were connected via the Internet with the business units' monitoring terminals, enabling Mengniu to remotely monitor ranch operations using Internet-of-Things (IoT) technology. The project allows digitalized ranch management and IoT-enabled monitoring of key areas in the production process including feed storage, veterinary drugs room, milking hall, laboratory and milk transportation vehicles. As such, the entire production process of raw milk is traceable and can be reviewed, which can help assure the quality and safety of raw milk. In the future, Mengniu will keep optimizing the project and implement it in related facilities across the nation, hence realize seamless monitoring of ranch operations as well as lay a solid foundation for overall digitalized ranch management. Mengniu also developed the "Milk Vehicle GPS Project" during the year to strengthen safety management and lower safety risks during transportation of raw milk. As at the end of 2016, about half of its raw milk transportation vehicles had GPS positioning system and shooting lens installed, enabling visual tracking of transportation routes of the vehicles and any abnormalities on the way to guarantee safety of raw milk on its "last kilometer" transportation.

To safeguard the supply of *Milk Deluxe* and give full support to the strategic upgrade of *Milk Deluxe* products, Mengniu focused on implementing the "P+ Project of Milk Source Bases" in 2016. It promoted in full scope management measures in relation to three core technologies relevant to dairy cattle welfare, refined feeding and species improvement. Four management approaches – 10 rounds of experiments, devising of technological solutions, hiring exclusive contractors and pricing support, plus daily reporting of monitoring findings and warning mechanism were used.

Management system

In 2013, Mengniu adopted the SAP system to boost its management capabilities in six areas: precision marketing and in-depth sales channel management; integrated business and financial management platform; a responsive synergetic system for supply, production and sales; integrated quality management and gradually refined quality tracking; scientific and rational industry deployment, and highly effective management of procurement and logistics.

There are three phases in the roll out of the SAP project. The first was foundation implementation, which was completed in March 2015. Mengniu achieved integration of businesses throughout the entire supply chain, integration of finance and business functions as well as integration of production, supply and sales functions, enhancing substantially the level of standardization and transparency of Mengniu's business data. On top of improving the efficiency of internal work-related undertakings, management and decision-making, the Group now has boosted strength in data mining and application.

The second phase involves operational refinements for roll out between 2015 and 2016. It includes four sub-projects, namely Business Intelligence ("BI"), Plant Maintenance ("PM"), Integration of Business and Finance of Sales Company ("IBFSC") and Finance Shared Service Center ("FSSC").

The BI marketing project was officially launched in June 2016. The BI system analysis platform provides access to real time sales data of different brands and product categories to facilitate related decision-making. The Group can thus monitor sales and expenses data timely and strengthen sales-end control, freeing the Group from the conventional analysis approach based on single business.

Mengniu is the first dairy enterprise in China to have a FSSC running on a mature operational model. In February 2016, it officially commenced phase II of the FSSC project. Currently, all production plants are FSSC-covered. On the back of innovative SAP-SSF (Share Service Framework) technology, business and finance systems of the Group are now connected and a solid foundation has been laid for establishing shared service centers for human resources, information technology and procurement functions. The FSSC platform provides full support to financial management and will continue to push for procedural upgrades of the center, so as to help the Group improve its management model, intensive cost saving, technology integration and innovation, as well as business transformation, etc. In 2016, the project received the "Best IBM Practice Project of the Globe IBM" award and the "2016 Best Innovation and Practice Prize in SAP Consumers Goods Industry 2016 SAP".

Also, to enjoy the economies of scale in procurement and to strengthen its management standard, core the competitiveness and risk resistance, Mengniu commenced the Supplier Relationship Management ("SRM") project in April 2016, the purpose of which is to provide systematic support to members of the Group to better establish and execute their procurement strategies via developing an efficient, centralized and integrated supplier and procurement information management platform. The platform built over six months was launched in October 2016 giving the Group a centralized procurement tender management platform, a supplier management platform and a supplier portal. The Group's contract management platform and SAP-ERP (Enterprise Resource Planning) system are effectively connected, permitting centralized purchasing of consumables via the system thus improving the efficiency of every procedure in the procurement process.

Currently, the project is in its third phase, going through coordination work and optimization, being improved and adjusted based on actual situations encountered during implementation.

One of the main informatization endeavors of the Group in 2016 was to build a sales information management platform, therefore the construction of region-wide SAP and Wei Sales Platform ("WSP"). SAP+WSP was launched during the year offering the Group a closed-loop model for direct sales channel management that covers sales execution, operation and financial settlement functions. It was quickly promoted countrywide to help physical sales entities effectively implement their operating systems. Mengniu promotes both SAP and WSP at the same time, as the two together can integrate front-end sales execution and back-end business operation, putting them in a closed-loop system for comprehensive management, allowing effective control over critical business procedures. It also provides Mengniu a stronger foundation for pursuing regional business expansion.

With the help of partners in the ecosystem, the Group integrated resources from different segments and completed construction of the southern and northern data centers during the year, in other words, the "Heart of Mengniu Digitalization" has started beating. In 2017, Mengniu will continue to push forward construction of the "Mengniu Cloud" to provide fast and reliable IT infrastructure sharing service to its different business segments, which will reduce the overall cost the Group incurs for its information system and lay a solid foundation for the Group to develop in the "Internet+" market environment.

Branding Strategy

Taking advantage of its access to first-class resources worldwide, Mengniu continued to push for "internationalization" and "digitalization" in its innovative strategic layout targeting to enhance its brand value all-round. Adhering to its "A Little Happiness Matters" brand concept, Mengniu mounted a wide array of interactive marketing activities on three major platforms – food, sport and entertainment – to help it relay messages of living healthy and the concept of happiness to consumers.

Mengniu has been a strategic partner of China's aerospace program for 13 years, during which it has provided high quality dairy products to astronauts and aerospace workers in the country. It has kicked off an "aerospace probiotics program" and developed its proprietary BBMN68 Bifidobacterium Lactis (BL) that was taken into space in Shenzhou 11 for experiments to explore the possibilities in upgrading the nutritional value of dairy products. Mengniu launched a series of aerospace themed activities under the "Support China, Excel in Space" banner, to share with consumers the joy of the successful launch of Shenzhou 11. With the support of integrated online and offline promotions, the activities attracted tremendous consumer attention and helped boost Mengniu's high-tech and high quality brand image. In 2016, the China Space Foundation awarded Mengniu the "Special Award for Contributions to China's Space Program", a clear recognition of Mengniu's strengths and quality in the aerospace aspect.

Mengniu and NBA China are long-standing strategic partners. The two parties have been devoted to promoting basketball culture and the healthy lifestyle of "more milk and more sports" and have cooperated closely in many areas to realize their respective brand value. In 2016, Mengniu initiated the 3V3 National University Basketball Challenge Match, which attracted participation of basketball fans in 48 universities in 12 cities. The champion team won the chance to visit the NBA overall champion, the Cleveland Cavaliers. The event has continued to elevate the influence of Mengniu among young consumers in China. During the NBA Global Game period, Mengniu and NBA China rolled out interactive activities themed "Friends for 10 years, A little happiness matters". Those activities resonated with basketball fans, bringing back for them memories about basketball and healthy living in the past decade. In addition, Mengniu was authorized to use the NBA logo on the packaging of its products and launch unique milk products in China with NBA elements incorporated in the package design to strengthen basketball fans' sense of affiliation to Mengniu.

Taking advantage of the 2016 Rio Olympics, Mengniu, together with its three sports champion ambassadors Jiao Liuyang, Wang Shun and Liu Xiang, initiated the "Tri-Champion Standards" brand proposition to support Chinese athletes taking part in the Rio Olympics. *Champion* mounted a large-scale marketing campaign themed "Everyone is Champion, Excel in Rio". The various marketing events put *Champion's* champion spirit in the news spotlight and the series of related activities that promoted sports and exercises gave consumers memorable experiences in relation to the *Champion* brand. *Champion* also cooperated with Rejoice Sport, a quality sport platform, on a running and accumulating mileage online activity, which was very well received and attracted the participation of a huge number of consumers, thus helping *Champion* build its champion brand image. In addition, Mengniu collaborated with Sina on a running event named "Excel in Rio, Run China", with activities organized in 100 cities nationwide featuring five nature-related themes – Blossoms, Ocean, Forest, Morning Light and Lake – to advocate exercise for all and convey its "High quality milk is definitely pure" brand value, letting participants experience the happiness of being with nature and exercising. Mengniu has married the value of sports with the pursuit of high nutritional standard in milk and is supporting consumers as a provider of nutritional dairy products.

The strategic alliance with Shanghai Disney Resort, which opened in June 2016, represented another milestone for Mengniu in taking its brand international. As the official dairy provider of Shanghai Disney Resort, Mengniu has an integrated brand presence at a variety of locations in the resort. Meanwhile, visitors from all over the world can enjoy Mengniu's quality products including milk, yogurt and ice cream in the resort. Many innovative delights are exclusively created for Shanghai Disney Resort, such as *Mickey's Ice Cream Classic*, *Minnie's Sweet Treat* and *Donald's Duckburg Ice*. In addition, Mengniu also launched several themed marketing campaigns with the resort, such as the "Happy Start to a Wonderful Journey" marketing activity featuring Future Star from June to July 2016 and the "A Wonderful Journey to Happy Festivals" activities between September and October 2016 to that coincided with Mid-Autumn Festival and National Day celebrations.

Innovation has been the driving force behind *Milk Deluxe* product upgrades, explaining its leadership in the development of premium UHT milk in China. Mengniu has redefined "premium" by enhancing the nutritional standard of all *Milk Deluxe* products and appointed the famous artist Chen Daoming as its ambassador, who perfectly represents its "New Nutrition Level Makes a Better Life" brand essence. Using the new media and offline activities combined, *Milk Deluxe* gained considerable exposure for its products and built for itself a high-end brand image that stands for "golden quality". Consumers responded very positively to *Milk Deluxe*'s marketing efforts for its upgraded new products, with those efforts winning for the Group the "Best Integrated Social Marketing Case – Gold Award" at the "China Content Marketing Awards Ceremony Gold Award".

Just Yoghurt again worked with Hunan TV, tapping into the popular prime-time variety show "Run for Time" in its second season to plant brand elements in the show setting. And, with strong ties to the show forged through its ambassador, awareness of the brand was markedly enhanced at the influence of fans of the show. At the same time, by sparking hot discussions on WeChat and Sina Weibo and interacting with consumers, the mass consumers came to appreciate the concept of "No additives, pure and delicious taste" of the brand and such appreciation turned into sales. *Just Yoghurt* also instilled its brand presence into the movie "The Mermaid", which won for it the "Best Video Content Marketing Case – Silver Award" at the "China Content Marketing Awards Ceremony Gold Award" in June 2016.

In June 2016, Mengniu cooperated with the Hollywood production "Independence Day: Resurgence". It demonstrated innovation in product development and created "Mengniu Moon Milk", which was seamlessly embedded in the movie, taking cooperation between Chinese brands and Hollywood movies to a new height. In addition, Mengniu embarked on a series of comprehensive online and offline movie-themed communications, which successfully grabbed the attention of young consumers and also strengthened the high-tech and high quality image of Mengniu's products befitting for consumption by Chinese astronauts. Through perfect integration of Moon Milk with the movie and entertainment resources, Mengniu's "Independence Day: Resurgence" integrated marketing program won the "2016 Best Innovative Marketing Award – Gold Award 2016" at the China Innovative Marketing Award, the "Annual Marketing Communication – Case Award" and "Innovative Interaction – Gold Award" at the China Advertising Great Wall Awards – Advertisers Awards, the "Non-alcohol and Non-carbonate Beverage Bronze Award" and "Single Effect Interactive Communication Bronze Award" at the Greater China Effie Awards and other awards in 2016.

Mengniu organized a charitable campaign named "Salute to Great Parents" that echoed with the focus of its *Awakening Youth Milk* brand on the nutrition and health of the middle-aged and elderly. The campaign had the support of ambassadors including celebrities, social elites and staff members of Mengniu in different positions. And, through the social media, this campaign was widely publicized and the *Awakening Youth Milk* brand gained vigor and fame, while encouraging more people to care about their parents. Furthermore, the *Awakening Youth Milk* brand has also integrated the resources of the Chinese national swimming team, with the products supplied to the parents of the swimming team members and the coaches, showing Mengniu's care for the heroes behind the "champions" and highlighting the brand spirit and character of *Awakening Youth Milk*.

Mengniu was the title sponsor of "Chef Nic", a leading food variety show that boasts high rating nationwide, for two years in a row. The program through delicious foods inspires people to "live the essence of life" and Mengniu through the program advocated the "Healthy Intestines Keep You Young" brand proposition of *Yoyi C* encouraging people to live healthy and happy and setting a new standard for the pursuit of quality living. The *Yoyi C* brand was incorporated into the show in various forms, and was complemented with interactive marketing via both online and offline communications. *Yoyi C* also made use of different social media platforms to roll out a series of interactive activities surrounding highlights of the show for fans, aiming to boost its brand influence.

Suan Suan Ru became the title sponsor of "Super Girl" in 2016. With classic IP as its vehicle, Mengniu explored new online marketing approaches in association with the reality show in the new Internet era. *Suan Suan Ru* was the first in the industry to adopt the one barcode per pack technology to connect product marketing with the voting activities of "Super Girl", forging close ties between the product and the program and stimulating actual sales. At the same time, offline caravan roadshows were presented bringing with it the contestants to communicate with brand consumers, turning fans of the show into patrons of the brand and in turn driving sales. That was a new example of cooperation between reality shows and brands in the new Internet era.

Future Star is the first milk product designed specifically for kids in China. In cooperation with the movie "Ice Age: Collision Course", it introduced the Ice Age limited edition packaging and engaged a host of different channels, including video and print, for marketing, building its premium image as a quality brand that helps children grow healthily. The movie with ice and coolness as elements also gave marketing leverage to Mengniu's *Ice+* products. The Group put out Ice Age limited edition *Ice+* products and mounted a variety of supportive promotion that succeeded in catching the eyes of many fans of the movie. It offered consumers soothingly cool products in the hot summer and received commendation from the partner.

Based on consumer Big Data research findings, Mengniu and JD upgraded strategic cooperation and jointly created the new brand *Tianxiaohai* that has unique Internet genes. The "Advisor Office of the *Tianxiaohai*" was set up online which kept coming up with interesting marketing topics and events and, via live shows featuring Jiang Jinfu, daily humorous Weibo and WeChat messages and videos, etc., communicated with and touched the heart of young consumers from various aspects. With humor and a sense of ease, the marketing activities helped publicized the positive and optimistic "Drink Sweet, Be Happy" life attitude.

The first high quality "Internet milk" (sold exclusively online) – *Hi Milk* which Mengniu launched jointly with its "Star Partner" the singer group Yu Quan contains 3.6g of lactoprotein per 100ml of milk. The product harvested tremendous success in IP customized marketing in 2016. Special packaging was launched respectively for the "Angry Birds" animated movie, the movie adapted from the best-selling book "Time Raiders" and the launch of the Logitech mouse, which were all hailed high among consumers. *Hi Milk* garnered many international honors in 2016, including two awards – "Best Dairy Product" and "Best Packaging of Dairy Products" – at the 10th Global Dairy Congress, and the "iF Product Design Award" dubbed the Oscar in the product design field, symbolizing the high acclaims Mengniu enjoys internationally for its innovative product designs.

Mengniu will continue to put consumers first and, through innovative marketing, rally the support of consumers to its brand value building efforts, thereby create for itself a more forward-looking and younger brand image.

Sales Channels

Mengniu pushed forward with pragmatism the reform direction that emphasizes "vertical flattening, horizontal integration, function optimization and enhancement of sales regions", strengthened its Route to Market ("RTM") project and created an operation mode centered around distributors and developed together by distributors, sales companies and the Central Business Units ("CBU"). With role and responsibility system improved and management mechanism implemented, the regional entities set up were able to fully deliver their functions. By increasing the number of its business representatives and distributors and employing system tools to standardize operations, Mengniu was able to carry out standardized management throughout its retail network. Furthermore, through establishing direct sales teams and strengthening their capacities in serving point-of-sale directly, Mengniu has been gradually boosting point-of-sale control and its core competitiveness, giving it a solid foundation for building an omni-channel delicacy management system.

Mengniu uses the WSP project to manage sales personnel's work at the point-of-sale, applying a closed-loop management system that covers from objective setting to sales execution. The project performs such functions as standardizing sales visits, setting parameters for management of employee attendance, guiding target management, carrying out standardized management, and collecting and analyzing real-time point-of-sale data. Armed with the advantages of access to basic information and data and having standardized operational procedures, WSP helps connect the relevant functions of different business segments in the internal operation of the sales system, and as such contributes to channel management upgrade and the professional, regulated, standardized and integrated management of the overall system platform. The WSP project has been promoted by Mengniu in full scope to sales companies and the CBUs.

By enhancing the overall Key Account ("KA") management structure, Mengniu has enabled closer exchange and communication among the different parties in three-tier organizational structure – the client teams at the headquarters, key account teams at sales regions and the distributor KA teams. Mengniu has established a customer data analysis platform for major point-of-sale of the key accounts, by which it closely monitored each point-of-sale of major customers and product delivery rate data, giving it a full grasp of and control on sales progress at each outlet and also boosting its responsiveness to changes in consumer demand, as well as linking it seamlessly with retailers. The platform also provided reference for effective sales decision making for achieving sales targets. In addition, Mengniu adopted differentiated marketing strategies, launching products and marketing activities customized according to the characteristics of major customers, thus created new growth opportunities in line with local conditions. By forming strategic alliance with major retailers, Mengniu was able to direct limited resources to key markets and product categories, building together with retailers a win-win platform for the business ecosystem. At the same time, Mengniu has kicked off in full scale an enhancement program for the convenience store sales channel pinpointing such areas as product structure, pricing system, delivery logistics, customization and marketing.

With an appreciation of the power of the Internet, Mengniu is forging ahead with expanding e-commerce sales channels and connecting with consumers through all possible means. During the year, Mengniu consolidated its business layout on quality e-commerce platforms and signed strategic cooperation agreements with Tmall and JD. Currently, its products are sold on all major e-commerce platforms in China including Tmall, JD, Yhd.com, Suning and Womai.com. In 2016, Mengniu recorded outstanding results on e-commerce platforms. Thanks to well-tailored traffic plans and marketing efforts to zest up demands, Mengniu attracted considerable consumer attention during the "Double 11" period, achieving sales totaling near RMB100 million, and snatched the top spot in sales on major e-commerce platforms such as Tmall and JD.

Mengniu has been expanding its overseas business footprint actively. It now sells products in oversea markets such as Hong Kong, Macau, Mongolia, Myanmar and Singapore. The room temperature products included *Pure Milk, Low-Fat High Calcium Milk*, *Milk Deluxe*, *Fruit Milk Drink*, *Just Yoghurt*; and the chilled products included mainly *Yoyi C*, and ice cream product brands such as *Deluxe*, *Suibian* and *Mood for Green*, etc. Mengniu further adjusted its product structure and carried forward the introduction of chilled products and ice cream products into the market. Also, Mengniu increased product exposure and stimulated sales by employing diverse and innovative promotion activities. It achieved good sales performance in Hong Kong and Macau, and other overseas markets during the year.

FINANCIAL REVIEW

Revenue

Benefiting from the upgrade in product structure and brands, and active promotion and marketing efforts, the Group's total revenue for 2016 was RMB53,779.3 million (2015: RMB49,026.5 million), representing an increase of 9.7% year-on-year. Excluding Yashili, the Group's revenue increased by 10.2% to RMB51,576.0 million (2015: RMB46,814.7 million). Products with greater contributions to revenue growth were *Milk Deluxe, Just Yoghurt* and *Mengniu Pure Milk*.

Gross Profit

With the declined average price of raw milk during the year and continued optimization of product mix, the Group's gross profit for the year increased to RMB17,635.4 million (2015: RMB15,375.5 million) and gross profit margin increased by 1.4 percentage points to 32.8% as compared with last year (2015: 31.4%). Excluding Yashili, the Group's gross profit was RMB16,583.7 million (2015: RMB14,242.4 million), while gross profit margin increased by 1.8 percentage points year-on-year to 32.2%.

Operating Expenses

To cope with market competition, the Group implemented proactive channel expansion strategies and invested more heavily on branding. The Group also recognized an impairment provision on goodwill relating to milk powder product business, a non-cash expense, during the year. As such, its operating expenses increased to RMB18,757.3 million (2015: RMB13,248.9 million), representing an increase to 34.9% (2015: 27.0%) of the Group's revenue. Excluding Yashili's operating expenses and the impairment of goodwill, the Group's operating expenses were RMB14,731.2 million (2015: RMB11,883.1 million), representing 28.6% of its revenue (2015: 25.4%).

Selling and distribution expenses for the year increased by 22.3% to RMB13,435.2 million (2015: RMB10,985.0 million), representing an increase of 2.6 percentage points to 25.0% (2015: 22.4%) of the Group's revenue. Excluding Yashili, the selling and distribution expenses of the Group were RMB12,264.2 million (2015: RMB9,872.6 million), representing 23.8% of its revenue (2015: 21.1%), an increase of 2.7 percentage points year-on-year.

Advertising and promotion expenses included in selling and distribution expenses, for the year increased by 30.6% to RMB5,333.7 million (2015: RMB4,085.1 million), representing an increase to 9.9% (2015: 8.3%) of the Group's revenue. Excluding Yashili, the Group's advertising and promotion expenses increased by 35.1% to RMB4,835.5 million (2015: RMB3,578.2 million), representing 9.4% of its revenue (2015: 7.6%), an increase of 1.8 percentage points year-on-year.

As Yashili recorded a loss during the year and took into consideration the operating condition and financial performance of Yashili in recent years, the Group recognized an impairment provision of RMB2,253.8 million against the goodwill recorded in the related milk powder product business during the year (2015: nil).

Excluding the impairment of goodwill, administrative and other operating expenses increased by 35.5% to RMB3,068.2 million (2015: RMB2,263.8 million), representing an increase to 5.7% (2015: 4.6%) of the Group's revenue. The increase was mainly attributable to the inclusion of the costs arising from underutilized production capacity of certain milk powder plants during the year and the increase in staff costs. Excluding Yashili, the Group's administrative and other operating expenses were RMB2,466.9 million (2015: RMB2,010.5 million), representing 4.8% of its revenue (2015: 4.3%), an increase of 0.5 percentage points year-on-year.

Profit from Operating Activities and Net Profit or Loss

As a result of i) the loss recorded by Yashili during the year and the impairment of goodwill of the Group; ii) the optimization of raw milk powder inventory level including selling excessive quantity at market price; and iii) a significant loss incurred by an associate during the year, the EBITDA of the Group decreased by 77.4% to RMB956.0 million (2015: RMB4,229.9 million), and the EBITDA margin declined to 1.8% (2015: 8.6%). Excluding Yashili and the impairment of goodwill, the EBITDA of the Group was RMB3,524.7 million (2015: RMB4,228.7 million), with the EBITDA margin decreased to 6.8% (2015: 9.0%).

Loss attributable to owners of the Company amounted to RMB751.2 million (profit attributable to owners of the Company in 2015: RMB2,367.3 million). Basic loss per share was RMB0.193 (basic earnings per share in 2015: RMB0.609). Excluding Yashili and the impairment of goodwill, profit attributable to owners of the Company was RMB1,686.9 million (2015: RMB2,331.0 million), representing a decrease of 27.6% year-on-year.

Income Tax Expenses

The loss before tax of the Group in 2016 was RMB461.4 million (2015: profit before tax of RMB3,030.2 million), while the income tax expense was RMB351.4 million (2015: RMB510 million). It was mainly due to the impairment loss of goodwill amounting to RMB2,253.8 million being a non-deductible item.

Excluding the impairment of goodwill, the effective income tax rate of the Group for 2016 was 19.6% (2015: 16.8%), increased by 2.8 percentage points year-on-year, mainly due to the contribution of Yashili and a major associate turned from profit last year to loss during the year. Excluding Yashili and impairment of goodwill, the effective income tax rate of the Group was at 17.2%, which was comparable with last year (2015: 17.1%).

Capital Expenditure

As of 31 December 2016, the capital expenditure ("CAPEX") of the Group was RMB4,352.5 million (2015: RMB3,026.9 million), increased 43.8% year-on-year. The CAPEX consisted of expenditure that were spent on building new and modifying existing production facilities and related investment amounting to RMB3,037.5 million, purchasing biological assets amounting to RMB230.8 million and addition of equity investment (including Dumex China) amounting to RMB1,084.2 million. Excluding Yashili, the CAPEX of the Group was RMB3,365.2 million (2015: RMB2,682.2 million).

Working Capital, Financial Resources and Capital Structure

As of 31 December 2016, the Group's net cash inflow from operating activities increased to RMB4,512.9 million (2015: RMB1,909.2 million), primarily due to (i) a significant decrease of raw materials inventories; (ii) an increase of trade payables; and (iii) an increase of other payables.

As at 31 December 2016, outstanding bank loans and bonds of the Group decreased to RMB8,587.6 million (31 December 2015: RMB11,050.3 million), of which bank loans amounted to RMB3,045.4 million (31 December 2015: RMB6,080.8 million) were repayable within one year. More than 60% of the bank loans and bonds were fixed interest-bearing loans. Excluding Yashili, the outstanding bank loans and bonds of the Group were RMB7,444.5 million (31 December 2015: RMB10,388.6 million).

Net borrowings (total amount of bank loans and bonds net of cash and bank balances) of the Group as at 31 December 2016 were RMB2,517.5 million (31 December 2015: RMB3,119.0 million). Excluding Yashili, the net borrowings of the Group were RMB3,017.2 million (2015: RMB4,938.7 million).

The Group's total equity as at 31 December 2016 was RMB25,503.7 million (31 December 2015: RMB26,615.2 million). Its debt-to-equity ratio (total amount of bank loans and bonds over total equity) was 33.7% (31 December 2015: 41.5%).

Finance costs of the Group for 2016 were RMB293.7 million (2015: RMB318.6 million), accounting for about 0.5% of the revenue (2015: 0.6%). Excluding Yashili, finance costs of the Group were RMB274.9 million (2015: RMB301.0 million), accounting for 0.5% of the revenue excluding that of Yashili (2015: 0.6%), decreased by 0.1 percentage points year-on-year.

Share Repurchase

The Group has full confidence in its long term development. To enhance its shareholder base and value, the Group repurchased in the open market a total of 6,116,000 ordinary shares of the Company, in six batches at the average price of HK$11.09 per ordinary share or a total consideration of RMB58.1 million during the year.

Products

In 2016, Mengniu continued to focus on key products, optimize product mix and innovate in product development and packaging. By undertaking Big Data-based precision marketing research, Mengniu was able to gauge the fine needs of consumers and quickly customize products and contents accordingly with precise input. Taking advantage of the flexibility of the digital media, it promoted the Mengniu brand and sales and enhanced the interaction between consumers and the brand, which has helped improve the brand's reputation.

Liquid milk	Revenue amounted to RMB48,102.9 million (2015: RMB43,326.6 million), accounting for 89.4% of Mengniu's total revenue (2015: 88.4%)	
UHT milk	Revenue amounted to RMB23,851.9 million (2015: RMB21,364.5 million), accounting for 49.6% of the liquid milk segment revenue (2015: 49.3%)	– The new *Milk Deluxe* products, upgraded and in new packaging, which contain 3.6g of quality lactoprotein and 120mg of original calcium per 100ml of milk, are leader in the development of high-end UHT milk in China. *Milk Deluxe*'s new ambassador, the famous artist Mr. Chen Daoming is a perfect representation of the "New Nutrition Level Makes a Better Life" essence of the brand – *Miao Miao Kid Growth Milk* in the *Future Star* series contains fortified calcium, iron and zinc as well as probiotics, conducive to the healthy growth of children. During the year, the series cooperated with the movie "Ice Age: Collision Course", releasing limited edition Ice Age packaging to help build the image of a quality brand dedicated to fostering the healthy growth of children – Mengniu and the Hollywood movie "Independence Day: Resurgence" joined force and seamlessly incorporated "Mengniu Moon Milk" into the movie, a move of strategic importance in improving Mengniu's international brand image. Also, a limited edition of *Mengniu Pure Milk* kicked off sales in Tmall coinciding with the release of the movie in theaters – *XinYangDao* tied in promotion with the movie "Warcraft", complementing it with a limited edition milk product sold in Tmall for fans of the movie. In addition, the brand was planted in the TV drama "The Mystic Nine" of Iqiyi innovatively, tapping into hot talks among the consumers to interact with the audience and drive sales – Mengniu worked with the "Star partner" singer group Yu Quan to launch the first high-quality "Internet milk" (sold exclusively online) – *Hi Milk*. The product contains 3.6g of lactoprotein per 100ml of milk, which is 20% higher than the international standard

		– *Awakening Youth Milk* rallied, through charitable bodies, the participation of members of the China Swimming Team, stars and celebrities and social elites in the "Salute to Great Parents" activity to show their gratitude to their parents and encourage consumers to care about their parents. The activity aimed to let the middle-aged and elderly enjoy the nutritious products and feel the warmth of care from others
Milk beverages	Revenue amounted to RMB9,380.2 million (2015: RMB10,434.7 million), accounting for 19.5% of the liquid milk segment revenue (2015: 24.1%)	– *Fruit Milk Drink* took on new thematic packaging designs, allowing it to leverage such broadcast channels as TV dramas, variety shows and Internet videos to publicize the "Milk + Fruit Pulps, Natural and Fun" brand attitude
		– *Yoyi C* upholds the brand motto of "Healthy Intestines Keep You Young" and is firmly founded on its offer of "30 billion live bacteria C" and "the only bacteria authorized by Denmark Chr. Hansen". It has built itself into a leading brand among functional beverages that contain active probiotics. During the year, *Yoyi C* launched an innovative cross-segment product – Live Tea, which integrates the exotic and unique characteristics of tea – Indian red and Longjing green – with probiotics, a combination of two very different flavors. A special edition packaging for the products was launched to complement the movie "Batman v Superman: Dawn of Justice". *Yoyi C* also introduced to the market a low sugar version of the sea salt and lemon flavor drink that contains quality sea salt from Australia and 30 billion live bacteria C. With a lower sugar content and added micronutrients, it promises to taste better and be more health-enhancing for consumers

Yogurt	Revenue amounted to RMB14,870.8 million (2015: RMB11,527.4 million), accounting for 30.9% of the liquid milk segment revenue (2015: 26.6%)	– *Just Yoghurt* is made with strictly selected quality milk from exclusive farms and fermented with bacteria imported from Denmark. It has a pure and simple taste and is high in nutrients, hence suitable for all members in a family. *Just Yoghurt* again worked with the variety show "Run for Time" of Hunan TV and had its brand presence instilled into the movie "The Mermaid" to promote the brand concept of "Good taste, no additives" – *Champion* launched the Red+ yogurt series, which contains BB bifidobacterium from Denmark, American pomegranates, cherries, plus roses from Yunnan and milk from exclusive farms in China. The two flavors of the Super Red Fruit Flower Yogurt series are Pomegranate & Rose and Cherry & Rose, which have set off a wave of "Red Fever" at the success of the Group's dedicated image building efforts – *Bio* launched a new product series that conveys a leisurely French-style ease. The products contain 10 billion Danone-patented B-Probiotics and taste exceptionally smooth thanks to Danone-patented production technique. They come in three flavors – blueberry, vanilla and red grape, which are perfect interpretations of French craftsmanship and romance – *200g Nourishing Oats and Red Dates Flavor Yogurt* was launched, featuring concentrated pure red dates extract, imported oats of premium quality and live bacteria from Denmark. It has a smooth and creamy texture and is nourishing and invigorating for consumers – *Xiao Jian* introduced the 180g *Ecolean Yogurt* made with selected raw materials from Bulgaria, Taiwan and China, and rich and pure ranch milk for enhancing health of the Chinese people

Ice Cream	Revenue amounted to RMB2,179.9 million (2015: RMB2,141.2 million), accounting for 4.1% of the total revenue (2015: 4.4%)	– Following the launch of the first fully-fermented pure yogurt ice cream in China in 2015 which was much-welcomed by the market, *Deluxe* launched another industry-leading product in 2016, the only fruit yogurt ice cream in the market, blending jam, fruit and yogurt with ice cream creating for consumers a probiotics-rich creamy treat that comes in many palate pleasing flavors – A new series named SuiXinGuo was added under the *Suibian* brand in 2016, leading the new jams plus ice cream product trend. It is rich in structure and innovative, and has up to seven layers, combining jams with chocolate, ice cream, cookies and cocoa beans. The product is an international first – *Ice+* released a brand new XuanCaiBing sea salt and pineapple flavor ice cream and also a brand new blueberry and lemon sorbet during the year. The XuanCaiBing series features delicious yogurt ice cream with real fruit pulps in an icy shell, presenting a new interpretation of the *Ice+* brand to consumers. In 2016, the XuanCaiBing series had an upgrade and added sorbets to the original *Ice+* ice cream family – Mengniu created eight different ice creams specifically for the Shanghai Disney Resort. They included *Mickey's Ice Cream Classic*, *Minnie's Sweet Treat* and *Donald's Duckburg Ice*, which were inspired by classic Disney cartoon characters. Coming in different flavors, they promise to surprise the palate and win the preference of consumers

Milk formula	Revenue amounted to RMB3,150.9 million (2015: RMB3,228.8 million), accounting for 5.9% of the total revenue of the Group (2015: 6.6%)	– Yashili's *Oushi Mengniu* continued to expand its organic product offerings. To add to the existing local organic infant milk formula *Ruipuen* it sells, the Group has begun final stage preparation importing organic infant milk formula which will be released to the market soon – Yashili upgraded the nutritional content and product packaging of the existing *Youyi* series milk powder, *Future Star Kid* milk powder products, and Mengniu's ordinary multi-dimensional and student milk powder products to satisfy the demand of consumers for not only more nutritious products but also for packaging at the forefront of time – Imported from New Zealand, *Yashily Super α-Golden Stage* boasts the patented INFAT active energy system that can promote growth of probiotics in the intestines of babies thus encourages good bowel activities. The formula was also launched in New Zealand simultaneously offering babies there quality milk formula
Other Products	Revenue amounted to RMB345.6 million (2015: RMB329.9 million), accounting for 0.6% of Mengniu's total revenue (2015: 0.6%)	– Mengniu and WhiteWave upgraded the flavors of the existing walnut and almond series of *ZhiPuMoFang*, a plant-based protein beverage jointly created by the two parties, and also released a Mellow Soy Milk series more agreeable with the Chinese palate. Using the world-leading nanoparticles milling technique μ-Grind™ and at temperature below 4℃, fruits can be milled into nanoparticles with the original nutrients kept intact for consumers to enjoy the original and most healthy taste

PRODUCTION

Mengniu deploys its production capacity taking into account market potential and its product strategies. As at December 2016, Mengniu had 33 production bases across the country and one production base in New Zealand, with total production capacity reaching 9.21 million tons (December 2015: 8.68 million tons).

CORPORATE SOCIAL RESPONSIBILITY

Mengniu has embedded the philosophy of sustainable development into its corporate culture, and carried out the mission of "Focus on nutrition and health, deliver a drop of happiness for every moment and every day to more people", with the support of its project implementation strategy that emphasizes "Leading standards, pragmatism, touching charity, top-level communication and pioneering guidance".

Mengniu's "Have a Lecture in My Hometown" program with "companionship" at its core, carried out in four modes involving lectures given by celebrities, tutoring by university students, support from partners in the ecosystem and public participation. And, to echo with the Rio Olympics, in 2016, the program took on the key directions of "higher, faster and stronger" and three Olympic champions, namely, Yang Wei, Zhao Ruirui and Jiao Liuyang, were invited to visit and show their care and love to children in rural areas. Since 2012, Mengniu has, together with 108 charity partners, involved 92 celebrities in the program, who visited over 600 schools in remote villages and showed their care and support to more than 100,000 children.

In August 2016, Mengniu hosted the "Codoon Micro Marathon • Shenzhen" capitalizing on the Rio Olympics craze, and together with Codoon, organized the charitable donation campaign "Exchange of Calories" on the competition day. The event had the in-person support of Zhao Ruirui, an Olympic champion and former member of the Chinese Women's Volleyball Team, and attracted the participation of 2,000 enthusiastic runners offline and over 100,000 online. The number of kilometers accomplished by the runners was converted into milk for donating to primary school pupils in rural villages. The activity provided participants a platform for charity on which they could render practical help to children living in rural areas of the country.

Mengniu spares no effort in supporting AIDS prevention in the community. It engaged staff and partners in the on-campus AIDS prevention campaign "Red-ribbon Health Ambassador Campaign on Campuses Advocating a Beautiful Youth" and encouraged students to take part in its "Scanning Barcode for Milk" activity to obtain tips on AIDS prevention and light up the red-ribbon symbol of the WeChat Avatar as a show of support to the on-campus campaign. During the year, Mengniu visited 10 universities across the country and organized offline activities for students (e.g. Red-ribbon Running Race) at Northeastern University and the South China University of Technology.

Mengniu is committed to enhancing public confidence in Chinese milk brands and maintaining the long-term healthy development of the dairy industry in China. To these ends, it has continued to push forward the "2020 Sustainable Ecosystem of Milk Sources", made up of such projects as “University of Ranchers”, “Star Ranchers” and “Gold Key Project”. In 2016, the “University of Ranchers” ran 15 sessions of theoretical and practical courses of different levels at 12 practice bases and the theoretical training courses had an attendance of over 1,500 person-time. During the year, this project offered 10 sessions of milk source management and technology improvement demonstration activities and 470 ranch-based practical technology innovation topics in major milk source areas across the country, and “Corporate Social Responsibility code of conduct” was signed with ranchers, helping over 800 ranches to improve on 24 aspects including herd structure and feeding management. The “Star Ranchers” program gathered together groups of industry experts and lecturers from around the world, who provided professional courses via satellite to attendees at the ranches. In 2016, the program covered 24 routine professional video courses. Mengniu also engaged Holstein Farmer Satellite Auditorium to produce two sessions of courses on practical ranch management skills and advanced industry technologies specially for Mengniu. These satellite courses were availed to over 1,500 ranch employees. And, for the “Gold Key Project”, Mengniu organized special technology demonstration coursework systematically in 10 major milk source areas across the country, and provided comprehensive guidance and carried out assessment on ranches using professional assessment tools and by means of on-site assessment, Q&A session, technical salon and special topic reporting. The program covered more than 1,000 ranches in 29 cities in 15 provinces, benefiting more than 2,000 people and translating into economic benefit of RMB300 million for the ranches.

Mengniu has actively carried out specialized energy conservation projects during the year, including 10 key projects involving the enhancement of electrical motor systems, air compressors and refrigeration systems, renovation of boilers and cooling systems. These special projects have enabled the Group to reduce coal consumption by approximately 5,000 tons, and to reduce emissions of carbon dioxide by approximately 14,000 tons, sulfur dioxide by about 45 tons and nitrogen oxides by about 40 tons, which is equivalent to planting 270 acres of trees. The Group has gradually optimized its energy structure by increasing its reliance on renewable energy by proactively introducing technologies such as innovative biomass boilers and solar power systems. Also, Mengniu has sought to become a water-conservation enterprise, and has committed to controlling industrial water usage, raising water consumption efficiency and ultimately, preserving the water environment. Utilizing water-saving technologies including solutions for balancing and optimizing water systems and upgrading heavy water-consumed equipments, Mengniu has managed to facilitate more than 40 advancement projects on water conservation techniques and reduced water consumption by more than 3 million tons.

Based on its own practical experience managing social responsibility delivery, Mengniu assisted the China Dairy Industry Association in formulating China’s first “Corporate Social Responsibility Guidance for Dairy Product Manufacturers”, in which the core content regarding the fulfillment of social responsibilities by dairy product manufacturers is clearly defined, to provide the dairy industry with reference and guidance on how to improve its capability in achieving sustainable development.

Mengniu's corporate social responsibility efforts are well recognized by different sectors of the community. In 2016, Mengniu made it among "First Batch of Loving Enterprises in the National Children Food Safety Protection Movement" as named jointly by the China Children and Teenagers' Fund, China Nutrition and Health Food Association, China Children Center and Peopleyuqing.com and also among "Community Enterprises of China 2016" at the 2016 China Annual Conference on Philanthropy, the only dairy enterprise being honored. Mengniu's "University of Ranchers" program was awarded the prizes "China Excellent Corporate Citizen in 2016" and "Excellent CSR Project of China Enterprises in 2016" at the 12th China Excellent Corporate Citizen Annual Convention, and was also honored as one of the "Top 10 Popular Charity Programs" at the Second China CSR 100 Forum. Furthermore, Mengniu ranked first in the Chinese dairy enterprise corporate social responsibility fulfillment level index in the "Blue Book of Corporate Social Responsibility for 2016" issued by the Chinese Academy of Social Sciences and it is one of the only two five-star enterprises among the 39 sample enterprises in the food industry.

HUMAN RESOURCES

As at 31 December 2016, the Group had a total of about 41,613 employees in China and Hong Kong, including around 3,711 employees of Yashili. During the year, total staff costs (including salaries of directors and senior executives) amounted to approximately RMB4,479.5 million (2015: RMB3,438.9 million).

To actively nurture successors to support the Group's sustainable development in the future and to provide solid personnel support for the Group to achieve its strategic objectives, Mengniu established and rolled out a diversified and multi-level curriculum training system in 2016, which covers areas including induction, cultural training, general career development skills and leadership. The "General Skills + Leadership" curriculum, which was launched in June 2016, comprised a total of 42 sessions taught during the year and 1,132 employees had attended the training.

At the same time, Mengniu re-visited and re-positioned its leadership curriculum, involving four programs, namely, the Graduate Trainee ("GT") Program, the Management Trainee ("MT") Program, the Advanced Leadership Development Program ("ALDP") and the Entrepreneurship Leadership Development Program ("ELDP"). Mengniu optimized the GT Program and completed three training sessions. The first class of MT students graduated in October. After launching the first session, the ALDP Program developed nine learning programs and implemented the learning programs as scheduled. The ELDP Program was launched during the year and completed the first session of the entrepreneurship leadership course.

In addition, to help employees with career development, Mengniu continued to formulate and improve career development paths for them. It completed designing the dual channel for professional development in June 2016 and put it on trial in the financial management system to assist the system in completing the dual-channel system design. The program was officially launched at the end of August and completed within the year.

To effectively support its 2020 Strategy, Mengniu reorganized its business setup at the end of 2016. The new setup comprises independent business segments dedicated to room temperature products, chilled products, milk formula, ice cream products and etc., and more resources and support have been provided to each business segment, to the end of facilitating overall and balanced development of the Group's various product categories. Under the new organizational structure, Mengniu will enhance its responsiveness to the market and customers, and improve operational efficiency. At the same time, it will strengthen the role of its headquarters in resource coordination and risk control.

PROSPECTS

With the milk formula registration system taking effect, the two-child policy in full rollout, per capita income of the Chinese people rising and urbanization continuing in China, demand for dairy products in the country will gradually recover. Adhering to the two-pronged strategy of "internationalization + digitalization", Mengniu will press ahead with fortifying resources integration, realizing innovative development, developing new product offerings, and promoting delicacy management and cultivating channels with intensive effort. It aims to continue to lead consumption upgrade with the craftsman spirit of constantly striving for excellence.

Looking ahead, Mengniu will be emphasizing the theme of "Focusing Development and Gathering Strengths", stick to the principle of "No Compromise" on four fronts – product, quality, values and execution to deliver high-quality dairy products to consumers. To make sure each business unit has a stronger focus on its business and is able to develop with a better balance, Mengniu initiated organizational structure adjustment, splitting the original core business into independent business segments: room temperature products, chilled products, ice cream products and milk formula. The new business setup has the merit of allowing focused development of each product segment, facilitating enhancement of the core competitiveness of products and the Group's overall operational efficiency, giving the Group a consumer and market-oriented organizational model which allows the Group to quickly respond to market situations, integrate production, supply and sales of its products, and guide channel development. In particular, heeding the potential of the fast-growing domestic market for chilled products in the next few years, the chilled product division is expected to develop new growth driver.

Milk source is the first quality assurance for dairy enterprises, which is why enhancing quality of the milk sources has always been the most important task of Mengniu. The increased shareholding in Modern Dairy in 2017, a raw milk supplier, will enable the Group to integrate the upstream supply chain resources, which will assure Mengniu of stable and high-quality milk supply, strengthen Mengniu's positioning in the high-end dairy product market and support the development of chilled dairy products. Furthermore, having stronger control over milk sources will further improve the Group's operating efficiency, and lay a good foundation for the Group to achieve its 2020 strategic objectives.

Mengniu will continue to work closely with its three major shareholders namely COFCO Group, Danone Group and Arla Foods, as well as leading international partners including WhiteWave and UC Davis from the United States, to create a global innovation platform. By stepping up efforts in relation to milk sources, products, production and operation, system management, brand strategy, sales channels and other aspects, Mengniu endeavors to promote the deployment of milk sources and research and development of dairy products worldwide, and the alignment with international standards, and ultimately takes the quality of Chinese dairy products to new heights.

Mengniu will continue to leverage on its advantage in the access to supreme resources worldwide to improve its brand value all-round. Mengniu has reached strategic agreement with Universal Beijing Resort, where it will become the exclusive official partner in providing dairy product and ice cream at the resort, hence becoming able to offer extensive product experience to visitors of the resort from all over world. Mengniu is also entitled to merchandising, product development and attraction brand exposure opportunities within the resort. In the future, Mengniu will continue to explore cooperative endeavors with Universal Parks & Resorts outside the theme park, with the aim of bolstering the international clout of the Mengniu brand.

Mengniu will join hands with other partners in the ecosystem on constant innovation, and also focus on brand building and carry out digitalized marketing. Mengniu is committed to in-depth analysis of consumer characteristics based on Big Data, in a bid to realize precision marketing and innovative product customization, enhance interaction with consumers and achieve high value-added brand effect. Relying on its SAP and the LIMS systems, Mengniu will reinforce its digitalized management capabilities, develop a monitoring and tracking system that covers the entire industrial chain, enhance the accuracy in terms of quality and stability of its production, thus provide its products with intellectualized and systematic quality assurance.

With its solid brand presence, a strong shareholder base and formidable strategic partners, Mengniu will steadfastly and with determination follow its clear strategic roadmap and speed up its strides toward becoming China's most dynamic and internationalized hundred-billion-dollar enterprise.

CORPORATE GOVERNANCE CODE

The Company has adopted the code provisions set out in the Corporate Governance Code (the "CG Code") contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") as its own code of corporate governance practices.

The Board has reviewed the Company's corporate governance practices and is satisfied that the Company has been in compliance with all applicable code provisions of the CG Code during the year ended 31 December 2016, except that the Group has deviated from the Code Provision A.5.1 with the reasons explained below.

Code Provision A.5.1 of the Corporate Governance Code provides that an issuer should establish a nomination committee which is chaired by the chairman of the board or an independent non-executive director and comprises a majority of independent non-executive directors. With effect from 15 September 2016, each of Mr. JIAO Shuge and Mr. ZHANG Xiaoya (each an independent non-executive Director) ceased to be a member of the Nomination Committee, and each of Mr. Tim Ørting JØRGENSEN and Mr. Filip KEGELS (each a non-executive Director) became a member of the Nomination Committee. As such, less than half of the members of the Nomination Committee are independent non-executive Directors starting from 15 September 2016. The Directors are of the view that each of Mr. Tim Ørting JØRGENSEN and Mr. Filip KEGELS is able to carry out his responsibilities as a member of the Nomination Committee in the best interest of the Shareholders notwithstanding that he is not an independent non-executive director as required under Code Provision A.5.1.

SECURITIES TRANSACTIONS OF DIRECTORS

The Company has adopted, in terms no less exacting than, the standards required by the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") set out in Appendix 10 to the Listing Rules as the Company's code of conduct and rules governing dealings by all Directors in the securities of the Company. Having made specific enquiry of all the Directors, the Company confirms that, during the year ended 31 December 2016, all the Directors have strictly complied with the Model Code.

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

During the year ended 31 December 2016,

(1) the Company repurchased on the open market a total of 6,116,000 shares of the Company at a total consideration of RMB58.1 million, all of which were cancelled during the year ended 31 December 2016; and

(2) the trustee of the Restricted Share Award Scheme purchased on the open market a total of 2,094,000 shares of the Company at a total consideration of approximately RMB16.9 million.

Save as disclosed above, neither the Company nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the year ended 31 December 2016.

AUDIT COMMITTEE

The audit committee of the Company has reviewed with the Company's management and the external auditors, the accounting principles and practices adopted by the Company and discussed auditing, risk management, internal control, whistleblowing policy and system and financial reporting matters, including the review of the Group's financial statements for the year ended 31 December 2016.

SCOPE OF WORK OF ERNST & YOUNG

The financial information in respect of the preliminary announcement of the Group's results for the year ended 31 December 2016 has been agreed by the Group's auditors, Ernst & Young, to the amounts set out in the Group's draft consolidated financial statements for the year. The work performed by Ernst & Young in this respect did not constitute an assurance engagement in accordance with Hong Kong Standards on Auditing, Hong Kong Standards on Review Engagements or Hong Kong Standards on Assurance Engagements issued by the Hong Kong Institute of Certified Public Accountants and consequently no assurance has been expressed by Ernst & Young on the preliminary announcement.

PROPOSED FINAL DIVIDEND

The Board has recommended the payment of a final dividend of RMB0.089 (2015: RMB0.140) per ordinary share for the year ended 31 December 2016. Upon shareholders' approval at the forthcoming AGM, the proposed final dividend will be paid on or about Wednesday, 21 June 2017 to shareholders whose names appear on the register of members of the Company on Thursday, 8 June 2017.

CLOSURE OF REGISTER OF MEMBERS

The register of members will be closed (i) from Monday, 29 May 2017 to Friday, 2 June 2017, both days inclusive, for determining shareholders' eligibility to attend and vote at the AGM, and (ii) on Thursday, 8 June 2017, for determining shareholders' entitlement to the proposed final dividend, during such periods no transfer of shares will be registered.

In order to qualify for attending and voting at the forthcoming AGM of the Company to be held on Friday, 2 June 2017, all transfers, accompanied by the relevant share certificates must be lodged with the Company's branch share registrar, Computershare Hong Kong Investor Services Limited, at Shops 1712–16, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, for registration no later than 4:30 p.m. on Friday, 26 May 2017.

In order to qualify for the proposed final dividend, all transfers, accompanied by the relevant share certificates must be lodged with the Company's branch share registrar, Computershare Hong Kong Investor Services Limited, at Shops 1712–16, 17th Floor, Hopewell Centre,183 Queen's Road East, Wanchai, Hong Kong, for registration no later than 4:30 p.m. on Wednesday, 7 June 2017.

PUBLICATION OF ANNUAL RESULTS AND ANNUAL REPORT

This results announcement is published on the websites of the Company at *www.mengniuir.com* and Hong Kong Exchanges and Clearing Limited at *www.hkexnews.hk*. The annual report of the Company will be despatched to shareholders and available at the aforesaid websites in due course.

BOARD OF DIRECTORS

As at the date of this announcement, the executive directors of the Company are Mr. Jeffrey, Minfang Lu, Mr. Bai Ying and Ms. Wu Wenting; the non-executive directors of the Company are Mr. Ma Jianping, Mr. Niu Gensheng, Mr. Tim Ørting Jørgensen and Mr. Filip Kegels; and the independent non-executive directors of the Company are Mr. Jiao Shuge (alias Jiao Zhen), Mr. Julian Juul Wolhardt, Mr. Zhang Xiaoya and Mr. Yau Ka Chi.

APPRECIATION

The Board would like to take this opportunity to express gratitude to our shareholders and the public for their continued support, and to all staff for their hard work and commitment.

By order of the Board
China Mengniu Dairy Company Limited
Jeffrey, Minfang Lu
Chief Executive Officer and Executive Director

Hong Kong, 29 March 2017