Sino Agro Food

Plans and Recent Developments

March 30, 2020

The last web update explained how Sino Agro Food Inc. has restructured its businesses and business plans to concentrate on prospects with the most promise while de-risking other areas. Most of the post explained the new "de-risked" business models for four of SIAF's subsidiaries: SJAP, JHST. MEIJI, and HSA. The company will now focus its energies on its equity investee, Tri-way Industries Ltd. ("TW") and its corporate division.

Tri-way Industries Ltd.

Primary Fishery Operations

In its fiscal year ending September 30, 2019, TW produced over 12,000 metric tons of fish and prawns (or shrimps) from 5 indoor (APM) farms and 9 open dam (ODRAS) farms using the A Power Re-circulating Aquaculture Systems and Technology (APRAS). TW contributed USD income 12.01M to SIAF in 2017 and USD 14.25M in 2018.

There was no production from aquafarms 4 and 5 (the "megafarm") after the first half of 2018. In 2019, 83% of production was composed of various fish species, while 17% derived from Mexican White Prawns. The feed and supplement cost for prawns is much lower than for the other seafood, reducing the overall cost of goods from approximately 75% of sales to approximately 65% of sales. For this reason, TW has reconfigured tanks to flip the composition of sales, projecting prawns to account for 73% of sales starting in 2020.

In the beginning of its 2020 fiscal year, starting October 1, 2019, TW's planning pro forma showed "natural production growth" of 15% for 2020 and 2021 and 20% for 2022 and 2023. Conservatively, this assumes no substantial external financing to fund growth. At that time, assuming operations would run roughly in line with 2019 metrics, targeted consolidated profit in 2020 would approximate USD 25M, growing thereafter. TW intends to limit capital expenditure prudently, targeting USD 8M in development to be performed by SIAF's Capital Award division.

However, the current COVID-19 pandemic has affected all operations of the Company as well as the domestic market conditions, Consequently, the Company anticipates up to six more months before the spending power of the consumers recovers to pre-pandemic conditions. The Company roughly estimates that operations have and will lose approximately RMB80 million (USD 11.5 million) between January 18th 2020 and June 30th 2020, obviously delaying the planned growth curve of the Company's fishery activities.

While generating good income in 2019, TW already faced a significant constraint with respect to cash flow. In 2017 TW acquired the fixed assets of Sino Agro's joint venture aquaculture farms by issuing shares as paid up capital of an appraised value of USD 340M. However, TW did not acquire some of the current assets, which were in the form of Foundational Biological Stocks ("FBS") including breeding and brood stocks, and nursery and grow out stocks, and amounting to USD 75M.

The following table shows the cash flow relating to FBS from 2017-2019.

		2017 (USD M)	2018 (USD M)	2019 (USD M)
Opening Balance			11.9	60.3
Original FBS Sold to T-W By Old Farmers		74.9		
Deferred Billing of Orig FBS		-51.6		
Replacement/Additional FBS		13.2	26.4	11.7
Billing of Deferred Entry of FBS			51.6	
Payments Contrasted for FBS from T-W Farms		-5.9	-12.7	-12.1
Debiting orig FBS owned by T-W (from AF1)				
Sales of low productivity FBS				
End Balance		11.9	60.2	40.5
Represented in T-W Financials under:				
Amount due to members (non-SIAF)			60.2	40.5
Amount due to members (SIAF)		11.9		
Total Due		11.9	60.2	40.5

The foundation stocks provide an operational basis for TW's income, as well as the growth of evolving FBS. TW projects strong income and positive cash flow to equity holders from its primary fishery production from mid-2021 once the FBS assets are fully paid for. In the interim, TW will endeavor to improve cash flow to equity by expanding its trading business, to the extent and in a time period unconstrained by the effects of COVID-19, after market and financing dislocations correct.

The company intends to list on the Hong Kong Stock Exchange ("HKSE") sometime in 2022. HKSE requires an accounting of assets. Because an account of the biological assets of the farms is impossible without incurring heavy mortality, Tri-way reorganized its financial recognition to comply with HKSE rules, starting in 2019. Now each farm's operations are being contracted out to its management who pays a royalty to TW. This royalty averages 20% of sales. Also, each farm sells its production to an intermediate trading company in China ("ITC") that operates as a sole agent of TW to market and distribute all production for and on behalf of Tri-way. Under this arrangement TW's primary fishery activity is similar to many other businesses required to pay value added tax and income tax. This structure was designed to be more acceptable to HKSE listing rules, and also to replicate the historic profit margins in normal times that define contributions to SIAF's net income.

In normal times, Tri-way's fishery operation is essentially a profitable business with long-term growth potential because the live seafood market of China provides an opportunity no other global markets can offer. However it is a capital intensive business, needing very high capital expenditures in fixed assets (i.e. infrastructure and construction and technologies etc). In addition, it can take years of sustained working capital to build sufficient production stock to support growth, as live fishery stock are required to be supplied on a daily basis and is susceptible to seasonal and market variations.

Trading Business

Over the years SIAF has developed relationships with suppliers and customers for the distribution of frozen seafood and other products. TW started its international trading activity in June of 2018 by importing and exporting food commodities to and from China and other countries.

Being a HK company, TW is situated within a global trading environment that provides opportunities to import various fish products for JFD to resell in China by way of direct sales or from value added processing, This provides JFD with an entry into the value added market much sooner than were it to solely depend on its own production.

Tri-way started the import and sales of frozen seafood since mid-term of 2018 on a trial basis, intending to expand the trading division in tandem with SIAF by developing and sharing part of this business activity with SIAF starting in 2020.

SIAF estimates that its supply/demand capacity for both SIAF and TW could approach 100,000 metric tons in the first year of operation and ramp subsequently. These levels are unattainable without sufficient outside financing to fund larger and more frequent inventory turns. For planning purposes SIAF/TW targets reaching 20% of said potential capacity, or 20,000 metric tons in the first full year. This would generate approximately USD 175M in first year revenue, with a net income margin of 11%.

The Company has currently available lines of credits granted by a Hong Kong based trading house for up to USD 15M which are expanded into suppliers credits (i.e. credit terms from suppliers and trade credits granted by trade loan establishments etc.). The Company targets the above referenced revenue with these currently existing credit lines.

However the current COVID-19 pandemic also affects the development of the trading business, causing depressed market conditions and disruptions in supplier and transportation services. Like the primary fishery business, it may take six months to recover to normal operations.

After recovery from COVID-19, Tri-way plans to expand its trading activity steadily and conservatively without depending on substantial additional loan financing. Tri-way's plans to be cap the import trading business to a reasonable level of its primary production activity. TW 's market valuation will be based on its fully integrated fishery activities, with trading an adjunct to its primary fishing operations, which have better margins and command better multiples as public companies.

SIAF and TW are working with financing brokers to obtain further a supplier credit facility of up to USD $30M to finance our purchases of goods from overseas suppliers for sales in China's domestic markets. In essence, such a facility would guarantee payment of transactions each time on each drawn amount. By way of example TW is seeking to locate and secure additional financing. In the current environment with the global recession, this will be very difficult. When the recession ends and banks are again providing financing for trade, TW will engage with banks to seek to secure additional financing. If TW secures new trade financing we will look to expand this business as strongly as the financing allows. At this time, we cannot project when or to what extent.

Conclusion

SIAF has restructured its businesses in several ways resulting in new emphases and plans, as below:

- SIAF ceased operational control of SJAP, JHST. MEIJI, and HSA and now derives revenue from leasing facilities or sharing in a percentage of revenue.

- This arrangement "de-risked" these businesses, which incurred negative cash flow of USD 2.8M in 2019 and now expects positive cash flow of USD 2.5M in 2020.

- Capital Award is seeking contracts for fishery product development internationally, with negotiations currently on-going for projects in Malaysia and India.

- TW will continue its primary fishery production business, targeting a reasonably conservative natural growth rate. Cash flow from these operations are hampered or negated until TW fully develops and pays for its foundational biological stocks. This is scheduled to occur in mid 2021, when cash flow will be boosted significantly in accordance.

- SIAF booked USD 65M in its trading business in 2019, with TW conducting trial import trading operations to complement its primary fish sales. Both companies foresee trading as a viable vehicle to increase 2020 cash flow significantly, having established supply side and demand side relationships to support large production capacities. The magnitude of expected cash flow boost will depend on procuring financing arrangements and their size.

  The Company believes the trading business in food products has great potential due to demands in the rapidly growing value added industries in China. Once established, trading businesses will surely provide stable income for both companies. These products are not subject to much seasonal variations nor heavily locked down capital. Like the primary fishery sector, there are so many developed and developing countries happy to supply the China markets at a pricing environment compatible with efficient distribution profits.

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Recent Developments

Share Count

The Company recently increased its outstanding share count to 60M shares. This was done in large part to accommodate an offering of preferred equity shares. As envisioned, a provision in this offering would allow an exchange of common shares for preferred shares. If fully exercised, there must still remain an adequate number of outstanding common shares.

The preferred offering initiative is progressing well through the SEC process.

2020 10-K filing / Coronavirus

The Company has applied for a 45 day extension to file its 2020 annual 10-K. The SEC is offering this extension to companies adversely affected by the COVID-19. Among other impacts, SIAF's audit is/was delayed because of quarantines and travel restrictions on company accountants in China and its auditor's personnel in Hong Kong.