



# Alibaba (9988 HK/BABA US) Poise to rebound

- Improving regulatory clarity after the conclusion of the antitrust investigation and Ant's formulation of rectification plan; investors to refocus on its fundamentals
- Intact medium-term business outlook driven by ongoing technological advancement and structural industry uptrend
- Maintain **BUY** on intact fundamentals and lessening regulatory uncertainty

**Refocusing on fundamentals.** In our view, the recent conclusion of the antitrust investigation, which led to an RMB 18.2bn fine, represents a soft-landing scenario as the fine only accounted for 5.8% of its cash level at end-2020; also, the regulator have not requested any significant business restructuring of the core ecommerce business. In addition, Ant Group has completed the formulation of its rectification plan, including setting up a financial holding company to operate its fintech businesses and fulfilling corresponding regulatory requirements. With regulatory uncertainties lessening, investors are likely to refocus on Alibaba's longer-term prospects, in our view.

**Strengthen merchants' support.** In the near term, the Group might strengthen its support to merchants via providing more value-added technological services to increase loyalty. We view it as a client retention initiative as the merchants might be incentivized to operate on multiple online ecommerce platforms under the new regulatory environment.

**Business outlook.** For FY3/21-23E, we expect GMV to grow at 10% CAGR to RMB 9.0tr by FY3/23E, driven by the growing number of active users and higher user spending. Revenue would increase at 27% CAGR in FY3/21-23E while core net margin (excl. impacts of share-based compensation and other non-operating items) would be 21.6% for FY3/23E. We estimate FY3/21-23E core net profit CAGR to be 20%.

**Valuation and recommendation.** We maintain **BUY** on Alibaba given its intact medium-term fundamentals and reducing regulatory uncertainty. Our SOTP-based TP for Alibaba-SW (9988 HK) and Alibaba-ADR (BABA US) are HK\$ 320 and US\$ 330, respectively.

## Results and Valuation

FY end Mar 31	FY20A	FY21E	FY22E	FY23E
Revenue (RMB mn)	509,711	714,692	915,575	1,152,530
Chg (% YoY)	35.3	40.2	28.1	25.9
Net profit (RMB mn)	149,263	161,939	206,030	242,277
Chg (% YoY)	70.4	8.5	27.2	17.6
Core net profit (RMB mn)	141,344	174,532	200,961	249,516
Chg (% YoY)	40.3	23.5	15.1	24.2
Underlying EPS (RMB)	7.1	7.5	9.6	11.3
Chg (% YoY)	67.3	6.3	27.2	17.6
Core EPS (RMB)*	6.6	8.1	9.4	11.6
Chg (% YoY)	35.0	23.5	15.1	24.2
Core P/E (x)- ADR*	29.8	24.2	21.0	16.9
Core P/E (x)-SW share*	28.9	24.5	21.3	17.1
ROAE (%)	20.2	16.7	17.3	16.7
ROAA (%)	13.1	11.2	11.9	11.6

1 ADR = 8 ordinary shares

HKD/RMB=0.8407

\*Excluding share-based compensation, impairments, fair value changes of investment, etc.

Source (s): Bloomberg, ABCI Securities estimates

## Company Report

Rating (SW-share): BUY  
TP (SW-share): HK\$ 320  
Rating (ADR): BUY  
TP (ADR): US\$ 330

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Price (ADR/SW-share)	US\$241.8/ HK\$237.6
Est. share price return (ADR/SW-share)	36.4%/34.7%
Est. dividend yield (ADR/SW-share)	NA/NA
Est. total return (ADR/SW-share)	36.4%/34.7%
Last Rating & TP (ADR/SW-share)	BUY, US\$351/ BUY, HK\$340

Previous Report Date Feb 10, 2021

Source(s): Bloomberg, ABCI Securities estimates

### Key Data

52Wk H/L (HK\$) (SW-share)	309.4/186.9
52Wk H/L (US\$) (ADR)	319.3/189.5
Issued shares (mn)	21,645
Market cap (HK\$ mn) (all share)	5,142,852
3-mth avg daily turnover (HK\$ mn) (SW-share)	6,592
3-mth avg daily turnover (US\$ mn) (ADR)	4,258
Major shareholder(s) (%):	
Softbank	25.1%
Jack Ma	6.0%
Joseph Tsai	1.9%

Source(s): Bloomberg, HKEx, Company



## Lessening regularity uncertainties, though investigation in existing strategic investments continues

In our view, the recent conclusion of the antitrust investigation, which led to an RMB 18.2bn fine, represents a soft-landing scenario as the fine only accounted for 5.8% of its cash level at end-2020. The fine will be booked in its upcoming 4QFY3/21 results.

In addition, unlike the Ant Group case where the regulator requests a significant business restructuring, the regulator has not made a similar restructuring request on Alibaba's core ecommerce business. Instead, Alibaba is requested to implement a rectification program to strengthen its internal controls and compliance, uphold fair competition, and protect the lawful rights and interests of the platform's merchants and consumers. Alibaba needs to submit a self-assessment and compliance report to the regulator for three consecutive years.

The management claims that they are not aware of any further ongoing antitrust investigation, except for the ongoing investigation in its existing strategic investments.

Looking forward, the management will continue to invest to strengthen its support to merchants through providing more value-added technological services to increase loyalty. We view it as a retention initiative as merchants can operate on multiple online ecommerce platforms more easily. We do not see any significant risk in merchants' stickiness given Alibaba's overwhelming customer base. The Group had 779m annual active customers in 4Q20, vs. 472m for JD and 788mn for Pinduoduo. Alibaba's annual spending per active customer is ~RMB 9K at present, based on our estimate, significantly higher than RMB 5.5K for JD and RMB 2.1K for Pinduoduo.

In addition, Ant Group (33% owned by Alibaba) has completed the formulation of its rectification plan:

- Ant Group will apply to set up a financial holding company to ensure its financial-related businesses are fully regulated.
- Its payment business will return to serving consumers and SMEs by focusing on micro-payments.
- Ant Group will set up a personal credit reporting company and apply for a personal credit reporting license. It will conduct the personal credit reporting business to comply with relevant laws and regulations, strengthen the protection of personal information, and effectively prevent the abuse of data.
- Consumer finance products, "Jiebei" and "Huabei", will be operated by its consumer finance company in compliance with relevant laws and regulations.
- Ant Group will strengthen consumer rights protection. It will also further enhance its corporate governance, adhere to fair competition rules, bring related-party transactions into line, strengthen risk prevention and control, create a fair market environment, and further strengthen its corporate social responsibility commitments.

Overall, Ant's rectification plan is largely within market expectation. In addition, Alibaba's financial exposure in Ant is manageable – the latter accounted for 8.3% of Alibaba's core net profit in 9MFY3/21.

With regulatory uncertainties gradually dissipating, investors are likely to refocus on Alibaba's fundamentals, in our view.



## Financial outlook

For FY3/21-23E, we expect GMV to grow at 10% CAGR to RMB 9.0by FY3/23, driven by the growing number of active users (CAGR 8.0%) and increased user spending (CAGR 2.0%). We expect revenue to grow at 27% CAGR in FY3/21-23E. Among Alibaba's major business segments, core commerce would expand at 24% CAGR; revenue from cloud computing and media/innovative initiatives would grow at 60% and 12% CAGRs. Alibaba's revenue growth has been higher than GMV growth in recent years, thanks to ongoing improvement of technological valued-added services to merchants, and we expect such trend to continue.

### Exhibit 1: Major assumptions

	FY3/20	FY3/21E	FY3/22E	FY3/23E
Annual active buyers (mn)	726	820	886	957
Annual GMV per customer (RMB)	9,076	9,085	9,266	9,452
Total GMV (RMB bn)	6,589	7,453	8,210	9,044

Source(s): Company, ABCI Securities estimates

### Exhibit 2: Revenue forecasts

(RMB mn)	FY3/20	FY3/21E	FY3/22E	FY3/23E
China retail revenue	332,750	482,488	603,109	723,731
China wholesale	12,427	14,291	17,149	20,579
International commerce	33,917	46,805	58,507	73,134
Cainiao logistics	22,233	35,573	53,359	80,039
Consumer service (Ele.me)	25,440	30,528	35,107	40,373
Others	9,337	13,539	16,923	20,308
<b>Core commerce</b>	<b>436,104</b>	<b>623,223</b>	<b>784,155</b>	<b>958,164</b>
Cloud computing	40,016	62,025	99,240	158,783
Digital media/ Innovation initiatives	33,591	36,286	40,732	45,846
<b>Total revenue</b>	<b>509,711</b>	<b>721,534</b>	<b>924,127</b>	<b>1,162,793</b>

Source(s): Company, ABCI Securities estimates

**Gross margin:** We expect gross margin to decline from 44.6% in FY3/20 to 43.0% in FY3/23E due to ongoing investments in new businesses such as logistics and consumer services.

**Product development expense:** We expect non-GAAP product development expenses/sales ratio be ~6.0% in FY3/22E and FY3/23E due to ongoing R&D investments in new services for merchants and consumers to increase merchants' loyalty.

**Sales and marketing expenses:** We expect non-GAAP sales and marketing expenses/sales ratio to remain largely stable at 9.0% in FY3/21-23E.

**General & admin expenses:** We expect non-GAAP general & admin expenses /sales ratio to stay at 3.5% in FY3/21-23E.

We expect core net margin (excl. impacts of share-based compensation and other non-operating items) to be 21.6% for FY3/23E. This would result in a core net profit CAGR of 20% for FY3/21-23E. Note that the RMB18.2bn fine related to the antitrust investigation will be charged in FY3/21 but we have excluded it in our core profit calculation due to its exceptional nature.

### Exhibit 3: Non-GAAP cost trend (RMB mn)

(FY end Mar 31)	FY3/20	FY3/21E	FY3/22E	FY3/23E
Cost of revenue	275,045	400,228	512,722	645,417
Product development expenses	29,426	46,455	54,934	69,152
Sales & marketing expenses	46,843	64,322	82,402	103,728
General & admin expenses	21,261	25,014	32,045	40,339
Amortization of intangible assets	13,964	16,438	23,805	29,966
<b>Total</b>	<b>386,539</b>	<b>552,457</b>	<b>705,908</b>	<b>888,601</b>
<b>% of revenue</b>				
Cost of revenue	54.0%	56.0%	56.0%	56.0%
Product development expenses	5.8%	6.5%	6.0%	6.0%
Sales & marketing expenses	9.2%	9.0%	9.0%	9.0%
General & admin expenses	4.2%	3.5%	3.5%	3.5%
Amortization of intangible assets	2.7%	2.3%	2.6%	2.6%
<b>Total</b>	<b>75.8%</b>	<b>77.3%</b>	<b>77.1%</b>	<b>77.1%</b>

Note. Excluding impacts of share-based compensation and other non-operating items

Source(s): Group, ABCI Securities estimates

### Exhibit 4: Forecast changes for FY3/21E

(RMB mn)	old	new	Diff	Comment
Revenues	687,325	714,692	4.0%	Higher growth assumption
Core profit	165,994	174,532	5.1%	

Source(s): ABCI Securities estimates

### Exhibit 5: Forecast changes for FY3/22E

(RMB mn)	old	new	Diff	Comment
Revenues	881,366	915,575	3.9%	
Core profit	210,883	200,961	-4.7%	Higher cost assumption

Source(s): ABCI Securities estimates



## Valuation and TP

We derive Alibaba’s valuation range based on the SOTP approach. For Alibaba’s core business, we apply a target multiple range of 23x-28x on its FY3/22E core profit. For its strategic investments, we refer to the latest book value and our estimates. The SOTP approach results in a valuation range of HK\$ 292-HK\$ 348 for Alibaba-SW (9988 HK).

**Alibaba-SW (9988 HK):** We set our TP at HK\$ 320.

**Alibaba-ADR (BABA US):** Based on our TP of Alibaba-SW, we set the corresponding TP of Alibaba-ADR at US\$ 330 (1 ADR represents 8 shares).

Overall, our valuation range implies a wide trading range. Our TP indicates a medium-term target but we notice that short-term share price might deviate from it due to regulatory uncertainties and technical factors such as supply/demand dynamics of shares, etc.

### Exhibit 6: SOTP valuation range for Alibaba-SW (9988 HK)

(HKD per share)	Low	High	Remarks
Core business	255	311	23-28x FY3/22E core profit
Strategic investments*	37	37	Latest book value, ABCI Securities estimates
<b>Total</b>	<b>292</b>	<b>348</b>	
Total (ex-Ant)	275	331	For reference only

\*Including HK\$17 per share for 33% stakes in Ant Group based on US\$ 150bn valuation (100%), which implies 8x 2019 P/S

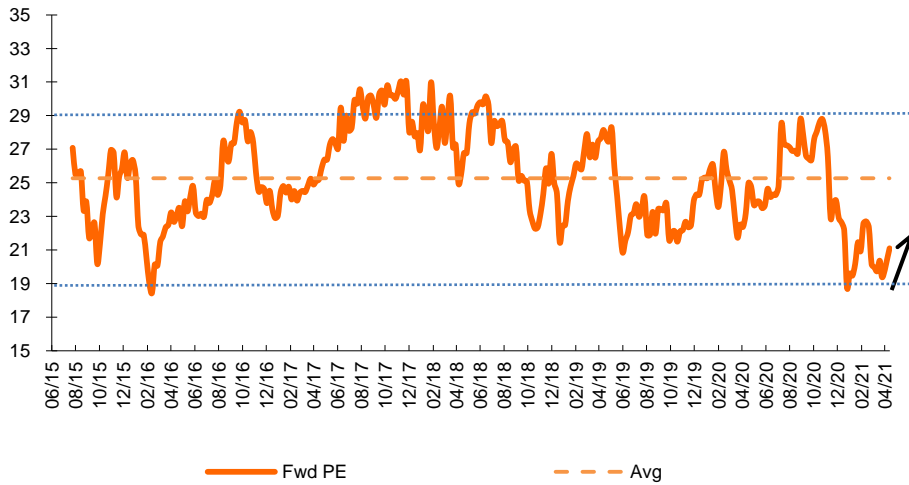
Source(s): ABCI Securities estimates

Overall, the tightening regulations have led to divergent valuations among the major listed ecommerce platforms in recent months. Alibaba’s valuation is substantially below its long-term average. Valuation of JD and Meituan continues to trade at above their respective historical averages. With the regulatory uncertainties gradually lessening, the divergent trend has started to reverse recently and we expect the trend to continue in the near term.

During 4Q20, Alibaba’s forward P/E has retracted from about 29x to 19x due to delay in Ant’s IPO and rising regulatory concern. With lessening uncertainties, its valuation has started to recover gradually. Looking forward, we expect the trend to continue but a full restoration of valuation back to pre-crisis levels could take time as regaining investor confidence is a gradual process.

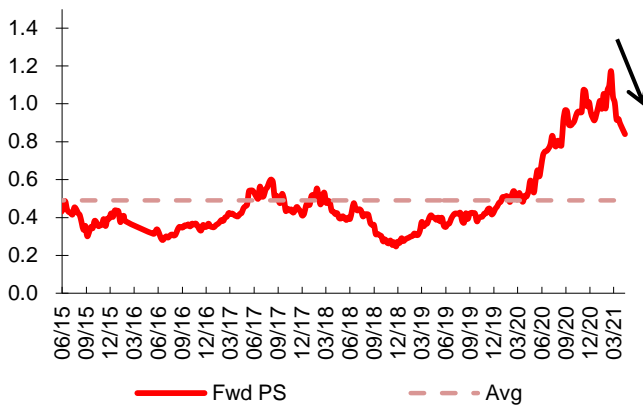


Exhibit 7: Alibaba's fwd P/E



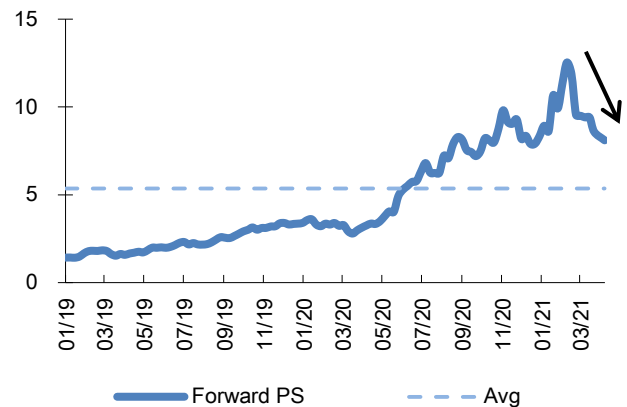
Source(s): Bloomberg, ABCI Securities

Exhibit 8: JD – fwd P/S



Source(s): Bloomberg, ABCI Securities

Exhibit 9: Meituan – fwd P/S



Source(s): Bloomberg, ABCI Securities

Exhibit 10: TP changes of Alibaba-SW (9988 HK) (HK\$ per share)

Segment	Old	New	Methodology -old	Methodology - new
Overall	340	320	27.5x FY3/22E core profit	25x FY3/22E core profit

Source(s): ABCI Securities estimates



Financial forecast

Consolidated income statement (FY20A-FY23E)

FY Ended Mar 31 (RMB mn)	FY20A	FY21E	FY22E	FY23E
Core commerce	436,104	616,382	775,603	947,901
Cloud computing & Internet infrastructure	40,016	62,025	99,240	158,783
Others	33,591	36,286	40,732	45,846
<b>Total revenue</b>	<b>509,711</b>	<b>714,692</b>	<b>915,575</b>	<b>1,152,530</b>
Cost of sales	(282,367)	(410,119)	(523,282)	(657,381)
<b>Gross profit</b>	<b>227,344</b>	<b>304,573</b>	<b>392,293</b>	<b>495,150</b>
Product development expenses	(43,080)	(64,901)	(74,626)	(91,461)
Selling & marketing expenses	(50,673)	(69,496)	(87,925)	(109,986)
General & admin expenses	(28,197)	(34,384)	(42,048)	(51,671)
Amortization/Impairment	(13,964)	(16,438)	(23,805)	(29,966)
<b>Operating Profits</b>	<b>91,430</b>	<b>119,354</b>	<b>163,888</b>	<b>212,066</b>
Interest and investment income	72,956	75,000	75,000	75,000
Interest expenses	(5,180)	(5,700)	(5,900)	(6,200)
Other income	7,439	(18,000)	-	-
Share of results of equity investees	(5,733)	1,000	1,000	1,000
<b>Profit before tax</b>	<b>160,912</b>	<b>171,654</b>	<b>233,988</b>	<b>281,866</b>
Tax	(20,562)	(17,165)	(37,438)	(50,736)
<b>Profit after tax</b>	<b>140,350</b>	<b>154,488</b>	<b>196,550</b>	<b>231,130</b>
Minority interests	9,083	7,724	9,827	11,556
Accretion of mezzanine equity	(170)	(273)	(348)	(409)
<b>Profits attributable to ordinary shareholders</b>	<b>149,263</b>	<b>161,939</b>	<b>206,030</b>	<b>242,277</b>
Share-based compensation	31,742	42,882	45,779	51,864
Amortization and impairment	39,044	26,438	23,805	29,966
Gains on disposals/revaluation of investments	(4,764)	(75,000)	(75,000)	(75,000)
Other non-core items	(73,941)	18,273	348	409
<b>Non-GAAP profits attributable to ordinary shareholders (Core net profit)</b>	<b>141,344</b>	<b>174,532</b>	<b>200,961</b>	<b>249,516</b>
<b>Growth</b>				
Total revenue (%)	35.3	40.2	28.1	25.9
Gross Profits (%)	33.8	34.0	28.8	26.2
Operating Profits (%)	60.2	30.5	37.3	29.4
Net profit (%)	70.4	8.5	27.2	17.6
Core net profit (%)	40.3	23.5	15.1	24.2
<b>Operating performance</b>				
Operating margin (%)	17.9	16.7	17.9	18.4
Net margin (%)	29.3	22.7	22.5	21.0
Core net margin (%)	27.7	24.4	21.9	21.6

Note. Individual items may not sum to total due to rounding differences

Source(s): Company, ABCI Securities estimates





**Consolidated balance sheet (FY20A-FY23E)**

As of Mar 31 (RMB mn)	FY20A	FY21E	FY22E	FY23E
Fixed assets	103,387	158,387	213,387	268,387
Investments	350,961	551,961	752,961	953,961
Other non-current assets	395,714	419,276	435,471	445,505
<b>Total non-current assets</b>	<b>850,062</b>	<b>1,129,624</b>	<b>1,401,819</b>	<b>1,667,853</b>
Cash & equivalents	330,503	315,712	360,970	466,545
Restricted cash and escrow receivables	15,479	15,479	15,479	15,479
Short-term investments and investment securities	32,712	32,712	32,712	32,712
Prepayments, deposits & other assets	84,229	84,229	84,229	84,229
<b>Total current assets</b>	<b>462,923</b>	<b>448,132</b>	<b>493,390</b>	<b>598,965</b>
<b>Total assets</b>	<b>1,312,985</b>	<b>1,577,756</b>	<b>1,895,209</b>	<b>2,266,818</b>
Accrued expenses, accounts payable and other liabilities	161,536	195,806	250,842	315,762
Other payables & accruals	23,204	23,204	23,204	23,204
Borrowings and notes	5,154	5,154	5,154	5,154
Deferred revenue	38,338	71,469	91,557	115,253
Merchants deposits	13,640	13,640	13,640	13,640
<b>Total current liabilities</b>	<b>241,872</b>	<b>309,273</b>	<b>384,398</b>	<b>473,013</b>
Borrowings and notes	120,276	120,276	120,276	120,276
Other non-current liabilities	71,186	71,186	71,186	71,186
<b>Total non-current liabilities</b>	<b>191,462</b>	<b>191,462</b>	<b>191,462</b>	<b>191,462</b>
<b>Total liabilities</b>	<b>433,334</b>	<b>500,735</b>	<b>575,860</b>	<b>664,475</b>
<b>Net current assets</b>	<b>221,051</b>	<b>138,859</b>	<b>108,992</b>	<b>125,952</b>
<b>Mezzanine equity</b>	9,103	9,376	9,724	10,133
Equity attributable to shareholders	755,401	960,222	1,212,030	1,506,171
Non-controlling interests	115,147	107,423	97,595	86,039
<b>Total equity</b>	<b>870,548</b>	<b>1,067,644</b>	<b>1,309,625</b>	<b>1,592,210</b>

Note. Individual items may not sum to total due to rounding differences

Individual items may varies from reported figures due to rounding differences/definition differences

Source(s): Company, ABCI Securities estimates





## Risk factors

### Violation of the anti-monopoly law in China

According to State Administration for Market Regulation of the People's Republic of China (the "SAMR"), Alibaba has violated the anti-monopoly law, which states that a business operator that has a dominant market position is prohibited from restricting business counterparties through exclusive arrangements without justifiable cause.

The SAMR ordered Alibaba Group to cease violating acts and imposed on Alibaba a fine of RMB 18.228bn. The SAMR also issued an administrative guidance, instructing Alibaba Group to implement a comprehensive program of rectification, through strictly fulfilling its responsibility as a platform operator, strengthening its internal controls and compliance, upholding fair competition, and protecting the lawful rights and interests of the platform's merchants and consumers. The administrative guidance requires Alibaba Group to submit a self-assessment and compliance report to the SAMR for three consecutive years.

### Market competition

The ecommerce industry is competitive. The competition will be on commission rate, promotion discount, brand advertising, technological investment, and more.

### Slowdown in ecommerce consumption

As the industry is dependent on consumer spending, any significant slowdown of consumption in China would hamper the Group's performance. In the long term, we believe consumption growth in domestic market would converge with income growth, which is usually in line with GDP growth.

### Non-GAAP financials

Ecommerce platforms generally disclosed the non-GAAP financial metrics, such as the non-GAAP net profit, to supplement its GAAP financial measures. Historically, there were differences between its GAAP net profit and non-GAAP net profit due to inclusion of items such as share-based compensation and other non-core items in the former.

Among these items, share-based compensation expense is related to various factors including price movement of ordinary shares, expected volatility, risk-free interest rate, etc.

While investors tend to exclude these items when performing analysis given their non-cash nature, we believe these non-GAAP financial measures should only serve as references.



## Disclosures

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The analyst, CHOW Sau Shing, primarily responsible for the content of this research report, in whole or in part, hereby certify that all of the views expressed in this report accurately reflect my personal view about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report. I and/or my associates have no financial interests in relation to the listed company(ies) covered in this report, and I and/or my associates do not serve as officer(s) of the listed company (ies) covered in this report.

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ABCI Securities Company Limited and/or its affiliates, within the past 12 months, have investment banking relationship with Alibaba and JD.com.

### Definition of equity rating

Rating	Definition
Buy	Stock return rate $\geq$ Market return rate ( $\sim 10\%$ )
Hold	- Market return rate ( $\sim 10\%$ ) $\leq$ Stock return rate $<$ Market return rate ( $\sim 10\%$ )
Sell	Stock return $<$ - Market return ( $\sim 10\%$ )

Notes: Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months  
Market return rate: average market return rate since 2008 (HSI total return index 2008-20 CAGR at 9.2%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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