JD.com (JD US)

Quality play with superior supply chain capability

- Upbeat 1Q20 results with 21% YoY revenue growth, demonstrating solid supply chain capabilities to ensure smooth operation during the COVID-19 outbreak
- Premium brand image backed by superb quality control and powerful in-house supply chain capability; JD.com (JD) secures a leading position in the online market sales of consumer electronics and home appliances.
- Maintain **BUY** and raise TP to US$ 60

Upbeat 1Q20 results despite COVID-19 outbreak. Despite a weakened macro environment amid the COVID-19 outbreak, JD reported a decent set of 1Q20 results. Revenue rose by 21% YoY to RMB 146.2bn. In addition, core net profit declined by 10% YoY to RMB 3.0bn. Overall, JD's 21% YoY revenue growth in 1Q20 significantly outperformed the 5.9% YoY growth in online sales of physical goods during the period.

Superior supply chain capabilities. We attribute JD's robust performance to its in-house business model with its own product inventories and logistic network, which enables a more reliable supply chain during the COVID-19 outbreak than ecommerce platforms relying on third-party suppliers and logistic networks.

A premium brand for online customers. We reiterate our long-term positive view on JD. In our view, JD's direct sales business model, superb quality control, and robust in-house logistic infrastructure are its core competitive edges. It enjoyed pervasive market shares of in online sales of mobile phones (54%), notebook PC (75%), desktop PC (88%), digital camera (62%), and home appliances (61%) in 3Q19, and has successfully replicated its success in various F&B products.

Maintain BUY and raised TP to US$ 60. We maintain **BUY** and raise our SOTP-based TP to US$ 60 because we revise up the 2020-21E revenue by 6% and lower WACC from 11% to 10% to evaluate its core business.

Results and Valuation

	2018A	2019A	2020E	2021E
Revenue (RMB mn)	462,019	576,888	710,178	846,703
Chg (%,YoY)	*27.5*	*24.9*	*23.1*	*19.2*
Net profit (RMB mn)	-2,492	12,184	10,163	16,900
Chg (%,YoY)	*-2,239.3*	*-588.8*	*-16.6*	*66.3*
Core net profit (RMB mn)	3,460	10,750	13,234	19,760
Chg (%,YoY)	*-30.4*	*210.7*	*23.1*	*49.3*
Earnings per ADS (RMB)	-1.7	8.2	6.9	11.4
Chg (%,YoY)	*-2,188.2*	*-580.3*	*-16.6*	*66.3*
Core earnings per ADS (RMB)	2.4	7.2	8.9	13.3
Chg (%,YoY)	*-30.4*	*204.9*	*23.1*	*49.3*
Core P/E (x)	162.3	53.2	43.2	29.0
P/S (x)	1.2	1.0	0.8	0.7
ROAE (%)	-4.4	16.7	11.1	15.6
ROAA (%)	-1.3	5.2	3.6	5.1

1 ADS = 2 common shares
Source(s): Bloomberg, ABCI Securities estimates

Company Report

May 20, 2020
Rating: BUY
TP: US$ 60

Analyst : Steve Chow
Tel: (852) 2147 8809
stevechow@abci.com.hk

ADS price (USD)	54.26
Est. share price return	10.6%
Est. dividend yield	NA
Est. total return	10.6%
Previous Rating &TP	BUY/US$49
Previous Report Date	Mar 26, 2020

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L(USD)	56.5/25.4
Issued shares (mn)	2,912
Market cap (USD mn)	79,003
Avg daily turnover (USD mn)	721
Major shareholder(s)	Voting right
Richard Liu	79.0%
Tencent	4.5%
Walmart	2.5%

Source(s): Bloomberg, HKEx, ABCI Securities

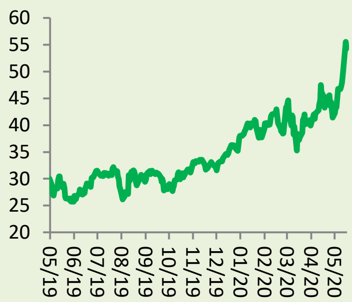
Share Performance (%)

	Absolute	Relative*
1-mth	20.0	16.4
3-mth	30.8	34.9
6-mth	71.3	65.9

*Relative to MXCN

Source(s): Bloomberg, ABCI Securities

Share performance(USD)



Source(s): Bloomberg, ABCI Securities

Content

1Q20 highlights

Amid the COVID-19 outbreak, JD reported a decent set of 1Q20 results. Revenue rose by 21% YoY to RMB 146.2bn, 7% above market expectation. Core net profit (excluding impacts of share-based compensation and other non-operating items) declined by 10% YoY to RMB 3.0bn, significantly better than the market expectation of a 61% YoY core profit decline for the quarter.

JD's 21% YoY revenue growth in 1Q20 outperformed the 5.9% YoY growth in online sales of physical goods in China by a large margin. We attribute JD's robust performance to its in-house business model with its own product inventories and logistic network, which enables a more reliable supply chain operation during the COVID-19 outbreak than other ecommerce platforms replying on third-party suppliers and logistic networks.

By product category, general merchandize product revenue rose by 38% YoY and accounted for 40% of product revenue in 1Q20 vs. 35% YoY in 1Q19. Electronics and home appliance product revenue rose by 10% YoY, accounting for 60% of product revenue in 1Q20 vs. 65% in 1Q19. In our view, the strong growth in general merchandize revenue reflects consumption of groceries shifting from offline to online during the COVID-19 outbreak amid operational disturbance of offline retailers.

Gross margin improved to 15.4% in 1Q20 vs. 15.0% in 1Q19, reflecting an improving revenue mix towards general merchandize products entailing a higher gross margin than electronics and home appliance products. The higher gross margin has helped mitigate the higher fulfillment expenses, which increased by 29.0% YoY in 1Q20. As a result, non-GAAP net margin was 2.0% in 1Q20 vs. 2.7% in 1Q19.

Looking forward, the Company guided for a 20%-30% YoY revenue growth in 2Q20. This implies ongoing outperformance versus the overall industry trend given the 8.6% YoY growth in online sales of physical goods in 4M20 vs. the 5.9% YoY growth in 1Q20, according to NBS.

We revise up our TP from US$49 to US$60 because we revise up the 2020-21E revenue by 6% and lower WACC from 11% to 10% to evaluate its core business.

Exhibit 1: 1Q20 results highlight

Results review:

(RMB mn)	**1Q19**	**1Q20**	***% y-o-y***	**Remark**
Net product	108,652	130,093	20%	Driven by general merchandize product
Net service	12,430	16,112	30%	
Revenue	**121,081**	**146,205**	***21%***	7% above market expectation
Gross profit	**18,184**	**22,535**	***24%***	
Operating profit	**1,226**	**2,320**	***89%***	
Net profit	**7,319**	**1,073**	***-85%***	
Core profit (non-GAAP)	**3,294**	**2,972**	***-10%***	Significantly better than market expectation of a 61% YoY profit decline
Profitability (%):	**1Q19**	**1Q20**	***ppt y-o-y***	
Gross margin	15.0	15.4	*0.4*	
Operating margin	1.0	1.6	*0.6*	
Net margin	6.0	0.7	*(5.3)*	
Core net margin (non-GAAP)	2.7	2.0	*(0.7)*	

Source(s): the Company, ABCI Securities

A quality play in the ecommerce sector

A premium brand for online customer

We reiterate our long-term positive view on JD as a quality play in the ecommerce sector with strengths in its unique direct sales business model as well as an in-house logistic infrastructure. Major peers including Alibaba (BABA US) and Pinduoduo (PDD US) adopt a co-op business model that mainly works with external partners and merchants for product sourcing and logistic.

In our view, JD's unique business model allows it to attain better quality assurance for products and services compared to other ecommerce platforms, helping the Group create a premium brand image for consumers.

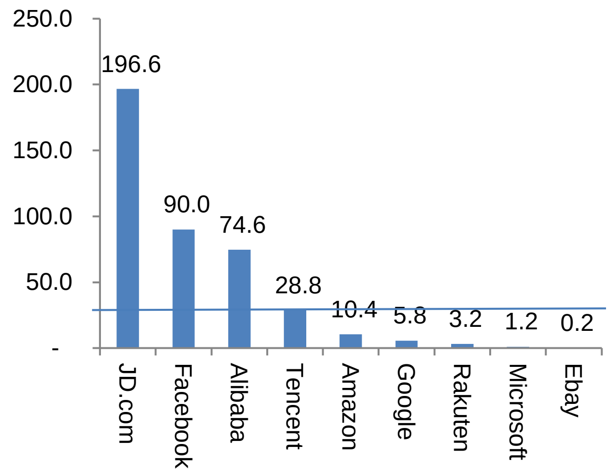
Manageable impact from coronavirus outbreak

A recent example to illustrate JD's operational strength is its defensiveness against the impact of COVID-19 – quarterly revenue growth was 21% YoY in 1Q20 vs. 5.9% growth for online sales of physical goods during the period. In our view, JD's relative resilience can be attributed to its direct sales model and in-house logistic system that enables a strong order fulfillment capability. Indeed, JD's has resumed full operation quickly after the CNY.

High growth in global standard

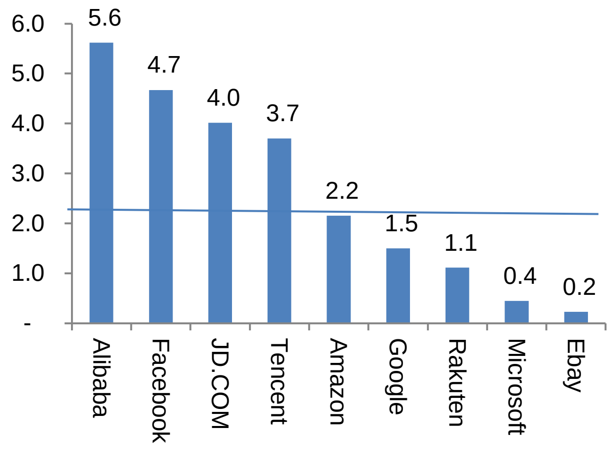
JD has achieved a rapid growth over the past decade, with revenue rising by 196.6x in 2009-19, outperforming global technology companies including Facebook, Amazon, Google, etc. On a five-year horizon (2014-19), JD's revenue increased by 4.0x, ranking the third among global technology peers.

Exhibit 2: 10-year revenue growth (x)



Note: 2019 revenue/2009 revenue
Source(s): Bloomberg, ABCI Securities

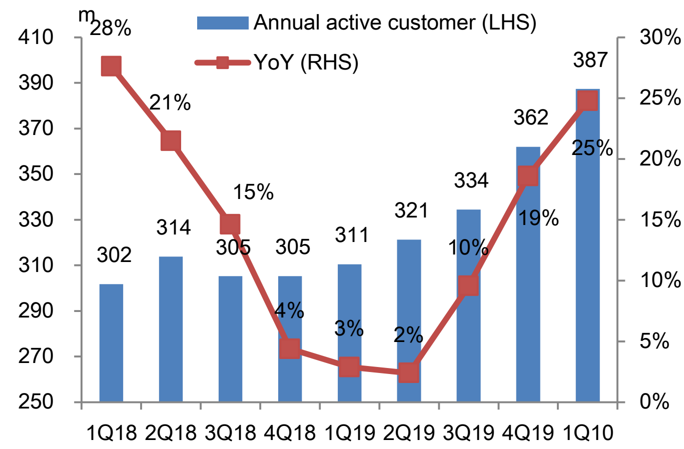
Exhibit 3: Five-year revenue growth (x)



Note: 2019 revenue /2014 revenue
Source(s): Bloomberg, ABCI Securities

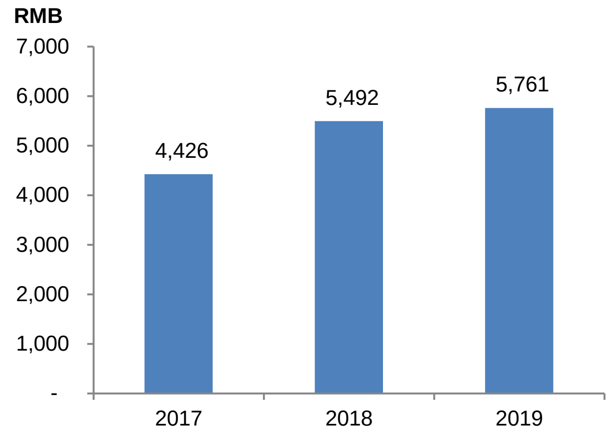
The Group had 387mn of active customers in 1Q20, up 25% YoY. In addition, customer growth rate has accelerated in recent quarters, driven by ongoing expansion into lower-tier cities, product expansion, and new business initiatives such as C2M products (more details below). In addition, average annual spending per customer increased from RMB 4.4K in 2017 to RMB 5.7K in 2019.

Exhibit 4: Annual active customer* trend



Source(s): the Group, ABCI Securities

Exhibit 5: Average annual spending per customer



Source(s): the Group, ABCI Securities

**Customers that made at least one purchase during the twelve months ended on the respective quarters.*

Product differentiation through unique consumer insight

The Group has been utilizing its data analyzing capabilities to gain consumer insight. The Company is helping brands tailor its products to match consumers' demands via its recent Consumer to Manufacturer (C2M) initiatives. Overall, this can shorten the product development cycle and lead time to consumers.

Currently, the Group has affiliated with over 140 appliances brands to innovate new products. E.g., the Group has partnered with TCL to launch three new customized smart appliances and Nestle on two C2M products.

In our view, this helps the Group offer differentiated products closely matching consumers' need.

New social ecommerce platform, Jingxi (京喜), to tap into demand in lower-tier cities

In Sep 2019, the Group has launched a social ecommerce platform, Jingxi, which targets at lower-tier cities. Overall, Jingxi connects consumers and manufactures via social media platforms and Jingxi app to enable consumers to communicate directly with manufacturers to explore value-for-money products. E.g., it offers flash sale deals and items at a bargain price. Consumers could enjoy steep discounts when they share the link info of an item with their friends, or by joining ongoing group-buying deals on the app. More importantly, it has partnered with Tencent to secure WeChat's first-level entry point to leverage the latter's traffic.

This is similar to Pinduoduo's business model that enjoys a huge success in lower-tier cities. As a result, the new initiative, which combines the Group's premium brand image and the right business model more concisely tailored to consumers in lower-tier cities, would allow the Group to compete with Pinduoduo more effectively, in our view. Currently, over 70% of JD's new users are from lower-tier cities.

JD Logistics – the crown jewel

Supply chain capability is one of the Group's greatest assets. JD has adopted a unique business model to build and operate its own warehouses and logistic system since the early days of operation.

Currently, the Group, through its logistics arm JD Logistics, operates one of most advanced nationwide warehouse and logistic system in China with over 650 warehouses (total GFA ~16mn sqm). Supported by AI-driven technology, the Group is able to deliver about 90% of its direct sales orders within 24 hours in China.

Leveraging JD's advanced technology and logistic expertise, JD Logistics was established in Apr 2017 to provide integrated supply chain and logistic services. In Feb 2018, JD Logistics raised USD 2.5bn from third-party investors by selling a 19% stake. As a result, JD's stake in JD Logistics fell to 81%.

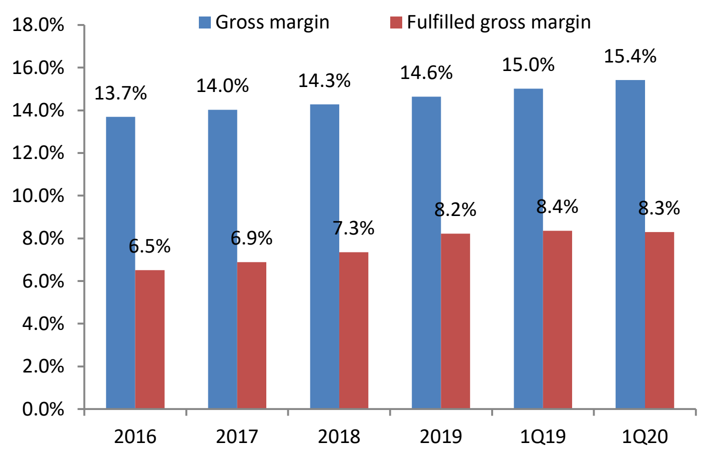
In our view, one of JD's strengths is delivery speed. It has introduced the "211" program since 2010 that guarantees orders received before 11am will be delivered on the same day, and orders received before 11pm will be delivered by 3pm on the following day. In addition, it also provides scheduled delivery services in some cities, which allow consumers to choose a convenient two-hour delivery window to receive their goods.

JD Logistics has launched the "Flash Delivery" initiative in 2Q18, offering delivery time ranging from several minutes to about one hour for selected merchandizes in selected areas.

Currently, external revenue accounted for about 40% of JD Logistics' total revenue.

The success of JD Logistics helped raise the fulfilled gross margin (gross profit minus fulfillment expenses/revenue) by 0.9ppt to 8.2% in 2019, while gross margin improved by 0.3ppt to 14.6% during the same period. Increase in cost efficiency of logistic service has helped lower the fulfillment-to-revenue ratio, which in turn elevate the fulfilled gross margin.

Exhibit 6: Gross margin vs. fulfilled gross margin



Source(s): the Group, ABCI Securities

Unlocking property value with property management fund.

In 2018, JD established a property management group, or JDPM, which owns, develops, and manages its logistics facilities and other real estate properties. In Feb 2019, JDPM established the JD Logistics Properties Core Fund (JD LPC Fund) with Singapore's sovereign wealth fund, GIC, for a total committed capital of over RMB 4.8bn. JD serves as the general partner and has committed 20% of the total capital while GIC has taken up the remaining 80%.

In addition, in Feb 2019, JD entered into a definitive agreement with JD LPC Fund, where JD will dispose of certain logistics facilities to JD LPC Fund for a total gross asset value of RMB 10.9bn. Subsequent to the disposal, JD will lease back these facilities for operational purposes. As a result, JD recorded RMB 3.9bn in gains of sales of properties in 2019. In our view, such sales and leaseback transaction indicates that JD might want to adopt a more asset light approach to boost returns.

Currently, JD Property manages properties with a total GFA of over 10mn sqm.

Strategic partnership with Tencent (700 HK)

Tencent has been JD's major strategic partnership since 2014. As part of the strategic partnership, Tencent agrees to offer JD Level 1 access points in its mobile apps Weixin and Mobile QQ and provide traffic and other support from other key platforms to JD.

Overall, Level 1 access points refer to entries and links that Tencent users can directly access on the interfaces that will launch after one click on the home interface on Tencent's mobile apps. As a result, JD could leverage on Tencent's massive user base.

Other strategic partnerships/business initiatives

In addition to above, JD also has various strategic partnerships/business initiatives. These serve as part of JD's ecosystem with various synergies. Please refer to the following table for more details.

Exhibit 7: JD's cooperation with other companies

Partners	Detail
Partnership with Walmart (WMT US)	In June 2016, JD entered into strategic partnership with Walmart. As of Feb 28, 2019, Walmart held Class A ordinary shares representing ~9.9% stakes. As part of the strategic alliance with Walmart, JD acquired ownership of the Yihaodian online marketplace platform. JD has collaborated with Walmart on e-commerce, including launching Sam's Club Flagship Store and Walmart China Flagship Store on JD.com, as well as Sam's Club Global Flagship Store, Walmart Global Flagship Store, and ASDA Flagship Store on JD Worldwide. JD also provides a one-hour delivery service from Walmart Stores in select cities through the JD Daojia app. The two companies also leverage one another's supply chain to increase product selection for customers across China.
Partnership with Google (GOOGL US)	In June 2018, Google invested USD550 m in JD and the two companies will work together to explore a broad range of possibilities, leveraging JD's supply chain and logistics expertise and Google's technology strengths. In early 2019, JD joined Google Shopping to offer a selection of high-quality products to consumers in the US
Bitauto (BITA US)	JD held about 26% stakes in Bitauto, a US-listed online platform for automotive industry
Yixin (2858 HK)	JD held about 11% stakes in Yinxin, a HK-listed subsidiary of Bitauto primarily engaged in ecommerce-related automotive financing platform business
Tuniu (TOUR US)	JD held about 20.4% stakes in Tuniu, a US-listed online travel platform. JD's leisure travel channel is currently operated by Tuniu
Yonghui (601933 CH)	JD held about 12% stakes in Yonghui, a major supermarket chain in China. The two companies have formed a strategic partnership to strengthen supply chain management capability primarily through joint procurement, and explore development opportunities in online-to-offline initiatives
Dada	JD held about 47.5% stakes in Dada, China's largest crowdsourcing delivery company As of Dec 31, 2018, its joint venture, Dada-JD Daojia, had partnered with more than 100,000 stores from leading supermarket brands, including Walmart, Yonghui, Carrefour and CR Vanguard, by leveraging Dada's crowd-sourcing delivery network Dada-JD Daojia is China's leading on-demand logistics and omni-channel e-commerce platform
China Unicom (600050 CH)	In Aug 2017, JD entered into a conditional share subscription agreement with China Unicom, a Chinese telecommunications operator in relation to its investment of ~RMB 5bn. Concurrently, JD also entered into a strategic business cooperation agreement with China Unicom
VIP shop (VIPS US)	JD held about 7.2% stakes in VIP shop, an online discount retailer in China
Wanda Commercial Properties	JD held about 2% stakes in Wanda, a leading developer, owner and operator of commercial properties in China

Source(s): Companies, ABCI Securities

Financial analysis

For 2019-2021E, we expect GMV to grow by 18% CAGR to RMB 2.9tr by 2021E, driven by the growing number of active users and their spending.

Annual active customer: the Group had 387mn of annual active customers at end-Mar 2010, much lower than 711mn for Alibaba (end-2019) and 585mn for Pinduoduo (end- 2019). The Group has seen good progress in penetrating into lower-tier cities, as illustrated by the 25% YoY user growth in 1Q20 vs. 3%/2% growth in 1Q19/2Q19. Looking forward, we expect the no. of active customers to reach 458mn by 2021E.

Annual spending per active customer: Annual spending per active customer has seen a growing trend in recent years, reaching RMB 5.8K in 2019. Having said that, it is still lower than RMB 9.2K for Alibaba. We expect the figure to increase further to RMB 6.4K in 2021E, driven by ongoing improvement in product selection and user experience.

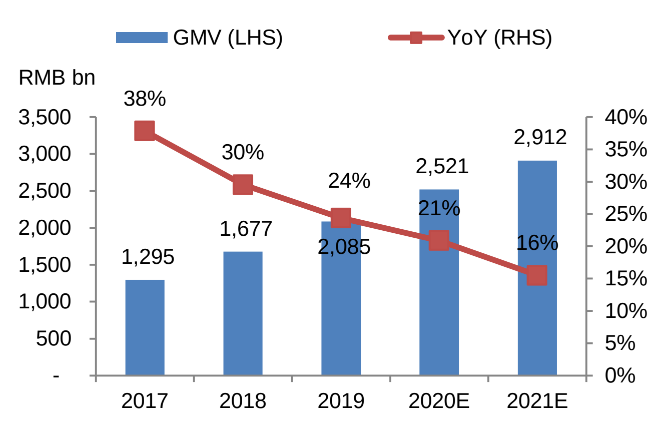
Exhibit 8: Major assumptions

	2017	2018	2019	2020E	2021E
Annual active customer account (mn)	293	305	362	416	458
GMV (RMB bn)	1,295	1,677	2,085	2,521	2,912
Annual spending per active customer (RMB)	4,426	5,492	5,761	6,055	6,358

Source(s): the Group , ABCI Securities estimates

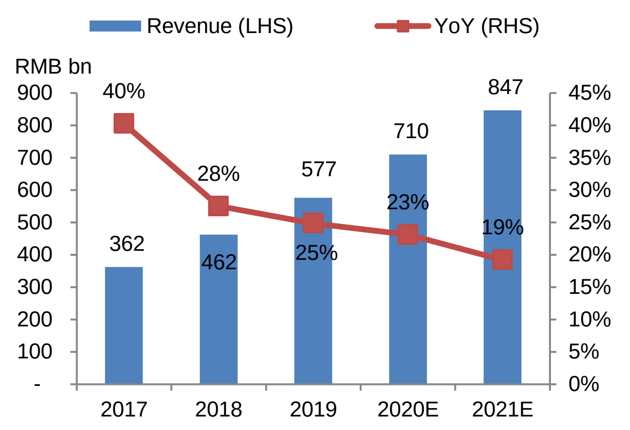
Overall, we expect revenue to increase at 21% CAGR in 2019-2021E to RMB 847bn by 2021E, propelled by growing GMV and ongoing expansion of new businesses including the logistics. In particular, we expect logistics and other service revenue to grow at 45% CAGR in 2019-21E.

Exhibit 9: GMV outlook



Source(s): the Group , ABCI Securities estimates

Exhibit 10: Revenue outlook



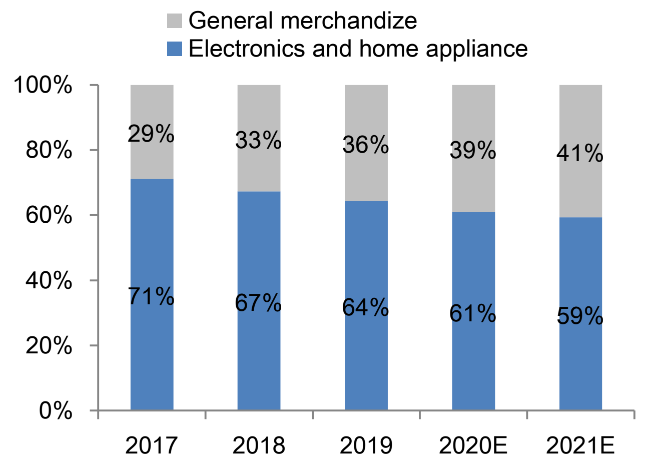
Source(s): the Group , ABCI Securities estimates

In terms of business mix, product revenue (direct sales revenue) accounted for 89% of total in 2019, while service revenue accounted for the remaining 11%. We expect share of service revenue to increase to 13% by 2021E.

Net product revenue (direct sales): We expect direct sales revenue to be RMB 737bn in 2021E vs. RMB 511bn in 2019, implying a CAGR over 20% in 2019-2021E. In our view, this is mainly driven by general merchandize products given the Group's ongoing product expansion effort in this category, as illustrated by the increasing sales mix of general merchandize products (as a percentage of net product revenue) in recent years.

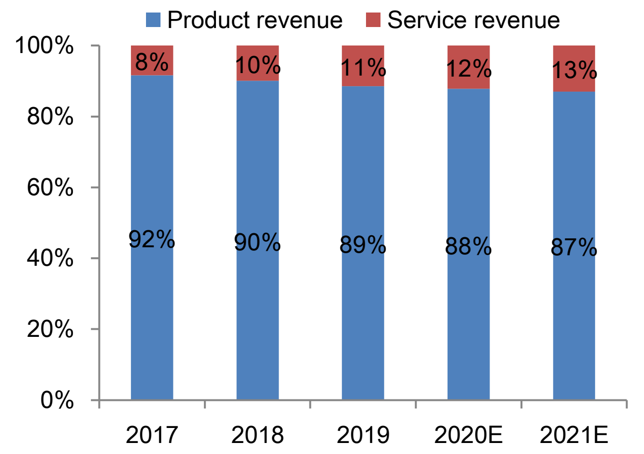
Net service revenue (marketplace, advertising, logistics, other services): We expect net service revenue to grow at 29% CAGR in 2019-2021E. In particular, we expect logistics and other services revenue to increase at 45% CAGR during the period, as JD Logistics continues to launch new services such as cold-chain and acquire external customers. As a result, we expect service revenue to account for 13% of total revenue in 2021E vs. 11% in 2019.

Exhibit 11: Direct sales- revenue mix



Source(s): the Group , ABCI Securities estimates

Exhibit 12: Revenue mix outlook



Source(s): the Group , ABCI Securities estimates

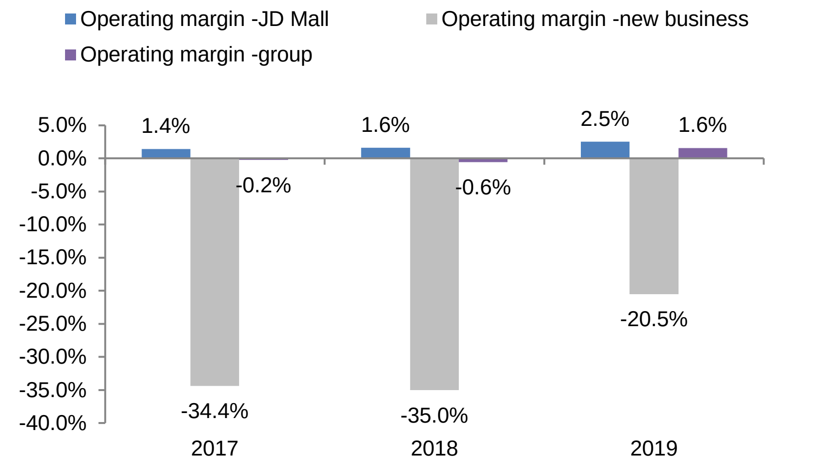
Exhibit 13: Revenue forecasts (RMB mn)

	2017	2018	2019	2020E	2021E
Electronics and home appliance	*236,269*	*280,059*	*328,703*	*378,009*	*434,710*
General merchandize	*95,555*	*136,050*	*182,031*	*245,741*	*302,262*
Net product revenue	**331,824**	**416,109**	**510,734**	**623,750**	**736,972**
Marketplace and advertising	*25,391*	*33,532*	*42,680*	*51,216*	*60,435*
Logistics and other service	*5,116*	*12,379*	*23,474*	*35,211*	*49,295*
Net service revenue	**30,508**	**45,911**	**66,154**	**86,427**	**109,731**
Total revenue	**362,332**	**462,019**	**576,888**	**710,178**	**846,703**

Source(s): the Group , ABCI Securities estimates

The Group's margins have been increasing in recent years, with improvement seen in both the core JD Mall business and new businesses such as logistics, technology, etc. Operating margins of JD Mall and new businesses improved to 2.5% and -20.5% in 2019 vs. 1.4% and -34.4% in 2017 respectively. The improved profitability is driven by ongoing cost control, economies of scale in new businesses, enhanced logistic capacity utilization, and higher staff productivity.

Exhibit 14: Operating margin by segment



Source(s): the Group , ABCI Securities

Looking forward, we expect the margins to improve further.

Gross margin: Gross margin improved to 14.6% in 2019 vs. 14.0% in 2017. Looking forward, we expect it to improve further to 15.1% by 2021E, driven by 1) product expansion into general merchandise products, which has a higher gross margin than consumer electronics products; 2) improving contribution from service revenue, which has a higher gross margin than direct sales business.

Fulfillment expanse: Non-GAAP fulfillment expenses/sales ratio improved to 6.3% in 2019 vs. 7.0% in 2017, driven by economies of scale and higher operation efficiency. We expect the ratio to improve further to 6.1% by 2021E as JD Logistics' scale continues to expand.

Marketing expenses: Non-GAAP marketing expenses/sales ratio was 3.7% in 2019 vs. 3.9% in 2018. We expect this ratio to stay flat in 2020-2021E.

Technology & content expenses: Non-GAAP Technology & content expenses /sales ratio was 2.3% in 2019 vs. 2.4% in 2018. We expect the ratio to improve slightly in 2020-2021E on economies of scale. Having said that, we notice that JD's R&D/revenue ratio is significantly lower than those of Alibaba and Pinduoduo ranging from 8.5-10% in recent years.

Other general & admin expenses: We expect non-GAAP G&A expense/sales ratio to improve to 0.4% in 2021E vs. 0.6% in 2019, driven by improving economies of scale.

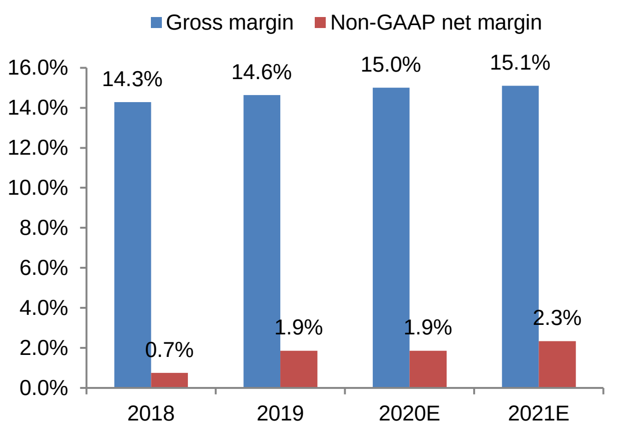
Exhibit 15: Non-GAAP cost trend (RMB mn)

	2017	2018	2019	2020E	2021E
COGS	311,490	395,994	492,385	603,651	718,851
Fulfillment expenses	25,275	31,423	36,363	44,741	51,649
Marketing expenses	13,560	17,815	21,338	26,277	30,481
Technology & content expenses	5,927	10,883	13,180	15,624	17,781
General & admin expenses	2,387	3,036	3,609	3,551	3,387
Total	**358,639**	**459,151**	**566,874**	**693,844**	**822,148**
% of revenue					
COGS	*86.0%*	*85.7%*	*85.4%*	*85.0%*	*84.9%*
Fulfillment expenses	*7.0%*	*6.8%*	*6.3%*	*6.3%*	*6.1%*
Marketing expenses	*3.7%*	*3.9%*	*3.7%*	*3.7%*	*3.6%*
Technology & content expenses	*1.6%*	*2.4%*	*2.3%*	*2.2%*	*2.1%*
General & admin expenses	*0.7%*	*0.7%*	*0.6%*	*0.5%*	*0.4%*
Total	***99.0%***	***99.4%***	***98.3%***	***97.7%***	***97.1%***

Note: Excl. impacts of share-based compensation and other non-operating items
Source(s): the Group , ABCI Securities estimates

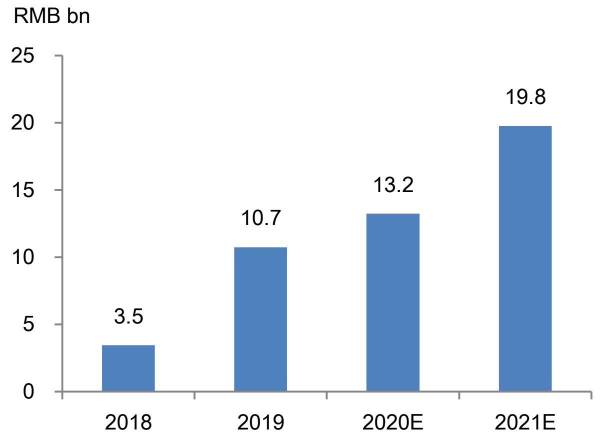
Based on improving gross margins and cost trends, we expect core net margin (excl. impacts of share-based compensation and other non-operating items) to rise to 2.3% by 2021E from 1.9% in 2019. This would result in a 36% CAGR in core net profit for 2019-21E.

Exhibit 16: Margin outlook



Source(s): the Group, ABCI Securities estimates

Exhibit 17: Core net profit outlook



Source(s): the Group, ABCI Securities estimates

Exhibit 18: Changes in forecast (RMB mn)

	2020			2021			
	old	new	Diff	old	new	Diff	Comment
Revenues	668,965	710,178	6%	797,852	846,703	6%	Higher GMV growth outlook
EBIT	12,554	12,751	2%	19,649	20,968	7%	
Net income	9,996	10,163	2%	15,789	16,900	7%	
Core profit	13,049	13,234	1%	18,627	19,760	6%	

Source(s): ABCI Securities estimates

Earnings sensitivity

Overall, JD's profit outlook is highly sensitive to its future core net margin, which is still thin at 1.9% in 2019. A 50bp improvement in core net margin will increase its 2020E and 2021E core net profits by 27% and 21%.

Exhibit 19: Earnings sensitivity analysis

Changes in core net margin (bps)	Changes in 2020E core net profit	Changes in 2021E core net profit
50	27%	21%
40	21%	17%
30	16%	13%
20	11%	9%
10	5%	4%
-10	-5%	-4%
-20	-11%	-9%
-30	-16%	-13%
-40	-21%	-17%
-50	-27%	-21%

Source(s): ABCI Securities estimates

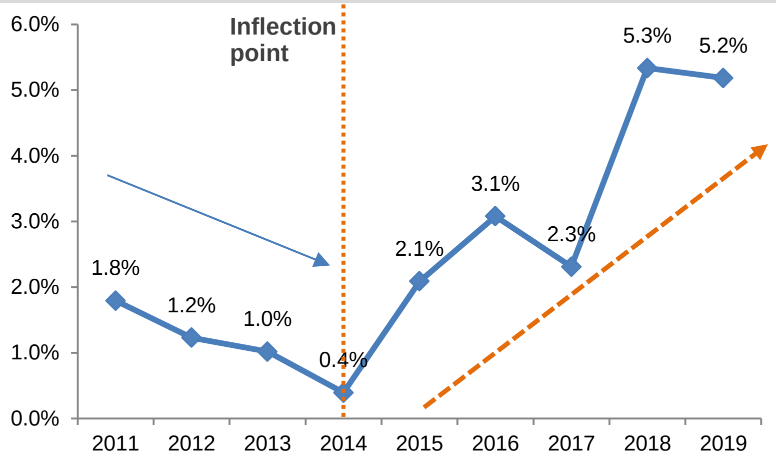
Lesson learnt from Amazon (AMZN US)

By analyzing Amazon's historical margin trend, we believe room for margin improvement for JD is still ample.

Amazon adopts a similar asset-heavy business model as JD with direct sales and in-house logistics facilities. It suffered from declining EBIT margin during 2012-14 due to ongoing investments in infrastructure. However, the situation has started to improve since 2015, with significant margin growth seen in subsequent years driven by economies of scale and ongoing business expansion into the service area. In 2019, its EBIT margin was 5.2% vs. 0.4% in 2014. Amazon's case suggests that margin could improve significantly once a company passes through the turnaround inflection point.

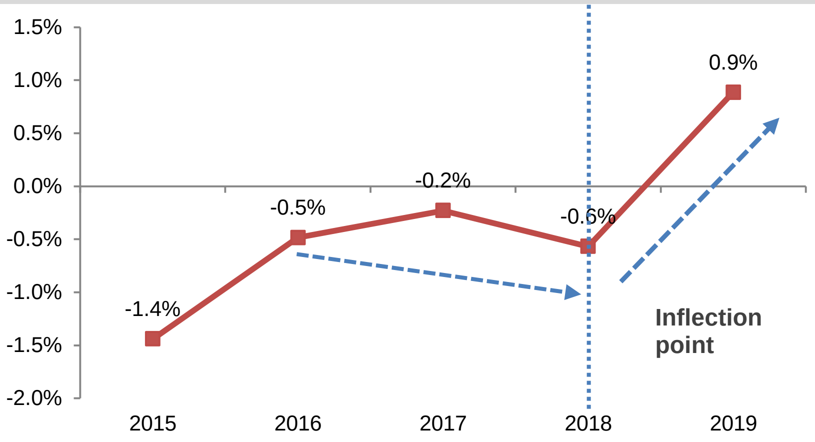
For JD, its EBIT margin has been in the range of -1.4% to -0.2% between 2015 and 2018. In 2019, it has begun to pass the turnaround inflection point with a positive EBIT margin of 0.9%, which resembles Amazon's situation in 2014. This implies significant margin potential over the next 3-5 years if JD follows in Amazon's footsteps with ongoing improvement in operating efficiency, economies of scale, and expansion into the service area.

Exhibit 20: EBIT margin – Amazon



Source(s): the Group, ABCI Securities

Exhibit 21: EBIT margin – JD



Source(s): the Group, ABCI Securities

Exhibit 22: Quarterly financials (RMB mn)

	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19	1Q20
Net product	*91,498*	*110,489*	*93,890*	*120,232*	*108,652*	*133,516*	*118,854*	*149,712*	*130,093*
Net service	*8,630*	*11,802*	*10,878*	*14,601*	*12,430*	*16,764*	*15,988*	*20,972*	*16,112*
Net revenues	**100,128**	**122,291**	**104,768**	**134,833**	**121,081**	**150,280**	**134,842**	**170,684**	**146,205**
Cost of revenue	-85,970	-105,777	-88,659	-115,661	-102,897	-128,156	-114,729	-146,686	-123,670
Gross profit	**14,159**	**16,514**	**16,109**	**19,172**	**18,184**	**22,125**	**20,113**	**23,998**	**22,535**
Fulfillment expenses	-7,173	-8,215	-7,761	-8,861	-8,064	-9,155	-8,755	-10,995	-10,400
Marketing expenses	-3,492	-5,261	-4,132	-6,352	-3,940	-5,621	-4,447	-8,226	-4,468
Technology & content expenses	-2,413	-2,781	-3,449	-3,502	-3,717	-3,726	-3,585	-3,592	-3,935
General & admin expenses	-1,076	-1,291	-1,397	-1,396	-1,321	-1,356	-1,341	-1,472	-1,412
Impairment of goodwill and intangible asset			-22						
Gain on disposal					83		2,987	815	
Non-GAAP operating profit	**1,084**	**353**	**878**	**551**	**2,204**	**3,435**	**3,157**	**1,029**	**3,443**
Profit from operations	**4**	**-1034**	**-652**	**-939**	**1,226**	**2,266**	**4,973**	**529**	**2,320**
Share of result of equity investees	-497	-260	-185	-171	-717	-304	-199	-518	-1,120
Interest income	546	606	576	390	313	376	503	594	523
Interest expenses	-229	-240	-241	-145	-187	-155	-163	-220	-207
Others, net	1,803	-1,186	3,429	-3,951	6,886	-1,199	-3,958	3,647	-133
PBT	**1,628**	**-2,114**	**2,927**	**-4,816**	**7,519**	**984**	**1,156**	**4,032**	**1,383**
Income tax expenses	-151	-163	-52	-61	-280	-439	-605	-479	-326
PAT	**1,477**	**-2,277**	**2,876**	**-4,877**	**7,240**	**545**	**551**	**3,553**	**1,057**
Minority interest	-48	-65	-124	-73	-80	-74	-62	-81	-16
Minority interest - mezzanine		1	1	1	1		1	1	1
Net income	**1,525**	**-2,212**	**3,000**	**-4,805**	**7,319**	**619**	**612**	**3,634**	**1,073**
Non-GAAP net profit	**1,047**	**478**	**1,184**	**750**	**3,294**	**3,559**	**3,086**	**811**	**2,972**
YoY									
Net product	31%	29%	23%	20%	19%	21%	27%	25%	20%
Net service	60%	51%	49%	46%	44%	42%	47%	44%	30%
Group revenue growth (%)	**33%**	**31%**	**25%**	**22%**	**21%**	**23%**	**29%**	**27%**	**21%**
EBIT growth (%)	-99%	157%	-230%	-41%	26541%	-433%	-863%	-156%	89%
Net profit growth (%)	539%	345%	196%	429%	380%	-133%	-80%	-176%	-85%
Core profit growth (%)	**-21%**	**-51%**	**-47%**	**67%**	**215%**	**645%**	**161%**	**8%**	**-10%**
Margin									
Gross profit margin (%)	14.1%	13.5%	15.4%	14.2%	15.0%	14.7%	14.9%	14.1%	15.4%
EBIT margin (%)	0.0%	-0.8%	-0.6%	-0.7%	1.0%	1.5%	3.7%	0.3%	1.6%
Net margin (%)	1.5%	-1.8%	2.9%	-3.6%	6.0%	0.4%	0.5%	2.1%	0.7%
Core net margin (%)	1.0%	0.4%	1.1%	0.6%	2.7%	2.4%	2.3%	0.5%	2.0%

Source(s): the Group, ABCI Securities

Maintain BUY with TP of US$ 60.0

We maintain **BUY** on the counter with a SOTP-based TP of US$ 60. We view JD as a quality play in the ecommerce sector given its direct-sales business model and in-house logistic network.

For JD's core ecommerce business, we assess the value through the DCF approach to capture JD's long-term value since the Group is still in the process of improving its profitability.

Our DCF approach is based on the following assumptions:

- 10% WACC
- 3% terminal growth rate
- EBIT margin normalized to 7% by 2029E

The following table shows the sensitivity analysis.

Exhibit 23: DCF sensitivity

		WACC				
		8%	**9%**	**10%**	**11%**	**12%**
Terminal growth	**2.0%**	53.0	49.2	45.7	42.6	39.7
	2.5%	55.0	51.0	47.4	44.1	41.1
	3.0%	57.3	53.1	49.3	45.8	42.7
	3.5%	59.9	55.4	51.4	47.8	44.4
	4.0%	62.8	58.1	53.9	50.0	46.5

Source: ABCI Securities estimates

For JD Logistics, we refer to its implied valuation in its latest refinancing round. For strategic investment, we refer to its latest book value.

Our SOTP-based valuation range is US$ 55.4-US$ 65.8 per share. We set our TP to US$ 60, approximating the mid-point of the range.

Exhibit 24: SOTP-based valuation range (USD per share)

Segment	Low	Base	High	Comment
Core business	45.7	49.3	53.9	DCF –from 2% to 4% terminal growth rate
JD Logistics	6.8	7.5	8.3	From 10% discount to 10% premium of its 81% stake
Investments	2.9	3.2	3.6	Book value with 0-20% discount
Overall	**55.4**	**60.0**	**65.8**	

Source(s): ABCI Securities estimates

Exhibit 25: Valuation range (mid-point) changes (USD per share)

Segment	Old	New	Methodology -old	Methodology -new
Core business	38.9	49.3	DCF –11% WACC	DCF -10% WACC
JD Logistics	7.5	7.5	Implied valuation in the latest refinancing round	Implied valuation in the latest refinancing round
Investments	3.2	3.2	Book value with 10% discount	Book value with 10% discount
Overall	**49.6**	**60.0**		

Source(s): ABCI Securities estimates

Peer valuation analysis

JD's comparable peers are major online e-commerce platforms, Alibaba and Pinduoduo. Among the three, the market leader Alibaba is currently trading at 19.6x 2021E P/E. On the other hand, Pinduoduo, an emerging player, is currently trading at 83.1x 2021E P/E.

JD is trading at a higher P/E than Alibaba. In our view, this could be justified by its margin expansion, which could lead to higher profit growth in coming years. In addition, as discussed above, as JD's profit outlook is highly sensitive to its margin trend; meaningful upside would emerge if margin improves more than expected.

Exhibit 26: Peer valuation

		Market cap (Lcy)	Price (Lcy)	P/sales			P/E			PEG*
				2019E	2020E	2021E	2019E	2020E	2021E	20-21E
BABA US Equity	ALIBABA	546,417	**203.7**	7.6	5.8	4.6	28.9	24.5	19.6	0.9
JD US Equity	JD.COM	74,680	**50.9**	0.9	0.7	0.6	42.6	39.7	25.5	0.9
PDD US Equity	PINDUODUO	73,414	**61.3**	16.9	11.2	7.4	NA	NA	83.1	NA
	Average			**8.5**	**5.9**	**4.2**	**35.8**	**32.1**	**42.7**	**0.9**

*PEG=2021E PE/core profit CAGR 2019-21E

Source(s): Bloomberg, ABCI Securities estimates

Appendix: Peer comparison

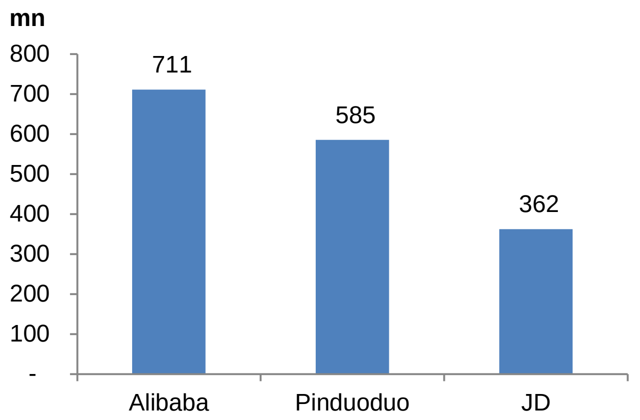
Comparing with major peers including Alibaba and Pinduoduo, we estimate that JD's annual spending per customer was ~RMB 5.8K in 2019, lower than ~RMB9.2K for Alibaba but significantly higher than ~RMB 1.7K for Pinduoduo.

In our view, JD's lower annual spending per customer than Alibaba could be due to its narrower product range constrained by the direct sales business model. On this front, we believe JD's ongoing expansion of its marketplace business and C2M initiatives could gradually alleviate such weakness.

On the other hand, its annual spending per customer is significantly higher than that of Pinduoduo, implying that its customers are ones with higher purchasing power and stronger loyalty.

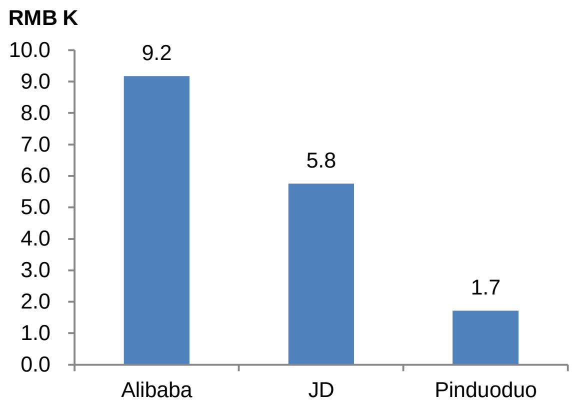
In terms of customer size, JD is lagging behind its competitors but we believe it could be partly due to the fact that Group has been focusing more on quality growth in the past. Having said that, we believe its recent new business initiative, Jingxi, could help expand its customer base, especially in lower-tier cities.

Exhibit 27: Annual active customers (2019)



Source(s): Companies, ABCI Securities

Exhibit 28: Annual spending per customer (2019)



Source(s): ABCI Securities estimates

At first glance, JD generated RMB 577bn in revenue in 2019, higher than that of Alibaba and Pinduoduo - but this fails to reflect the true picture as JD adopts a direct-sales business model, meaning that it recognizes direct-sales GMV as revenue while Alibaba and Pinduoduo only recognize sales commission as revenue with their marketplace model.

Hence, core net profit sizes would be a better benchmark for comparison. In 2019, JD generated RMB 10.8bn in core net profit vs. RMB 138.7bn for Alibaba and RMB 4.3bn of core net losses for Pinduoduo. In our view, although JD's profit size is still significantly lower than Alibaba's, its business operation is more sustainable than Pinduoduo, which is still suffering from meaningful losses at the moment.

In terms of margin, JD's core net margin was 2.3% in 2019, significantly lower than Alibaba's. In our view, this could be attributed to JD's direct sales business model and in-house logistics facilities, which bear both the inventory and logistic costs. On the other hand, Alibaba adopts an asset-light business model conducive to a higher core net margin

Exhibit 29: Business comparison

	JD.com	Alibaba	Pinduoduo
Direct sales	Direct sales business sourced products from over 19K supplies at end-2018	NA	NA
Online marketplace	Over 270,000 merchants at end-2019,	Taobao and Tmall had over 2bn product and service listings at Mar, 2019. As of Mar 31, 2019, there were over 190,000 brands and merchants on Tmall, including 77% of the consumer brands ranked in the Forbes Top 100 World's Most Valuable Brands for 2019.	3.6mn active merchants in 2018 "team purchase" model to allow customers to purchase products at low prices
Omni-channel initiatives	JD Daojia –Online-to-offline supermarket platform 7FRESH- 24/7 fresh food supermarket SEVEN FUN- lifestyle space in Beijing to provide meal and leisure options JD E-SPACE – a 50K sqm experience store in Chongqing with innovative electronics and smart products Partnership with Walmart	Freshippo –grocery retail chain Partnership with various offline retailers including SunArt, Starbuck, Suning, Intime, Lianhua Supermarket, Red Staf Macalline, etc on omni-channel initiatives	NA
Logistics network	Self-owned logistics network –JD Logistics At end-2019, JD Logistics operated over 700 warehouses, covering GFA of approximately 16.9m sqm	In FY3/19, Cainiao Network's 15 strategic logistic partners employed over 1.6 mn delivery personnel in more than 700 cities and 31 provinces in China. Collectively, these partners operate more than 190,000 hubs and sorting stations and delivered 25.1 bn packages in FY3/19.	External logistic partners
FinTech	JD Digit (formerly JD Finance). Potential conversion into 40% of JD Digit's equity interest in the future, subject to regulatory approval	Ant Financial (33% stake)	NA

Source(s): Companies, ABCI Securities

Exhibit 30: Financial comparison (2019)

	Alibaba			JD			Pinduoduo		
	2018	2019	YoY	2018	2019	YoY	2018	2019	YoY
Annual active user (mn) (period end)	636	711	11.8%	305	362	18.6%	419	585	39.7%
Revenue (RMB mn)	345,278	488,895	41.6%	462,019	576,888	24.9%	13,120	30,142	129.7%
Gross profit (RMB mn)	161,455	223,420	38.4%	65,953	84,421	28.0%	10,215	23,803	133.0%
Operating profit (RMB mn)	57,540	93,064	61.7%	-2,619	8,994	NA	-10,799	-8,538	-20.9%
Core net profit (RMB mn)	93,243	138,740	48.8%	3,460	10,750	211.0%	-3,456	-4,266	23.4%
Gross margin	46.8%	45.7%		14.3%	14.6%		77.9%	79.0%	
Operating margin	16.7%	19.0%		-0.6%	1.6%		-82.3%	-28.3%	
Core net margin	27.0%	28.4%		0.7%	1.9%		-26.3%	-14.2%	

Source(s): Companies, ABCI Securities

Exhibit 31: Financial comparison (2018)

	Alibaba			JD			Pinduoduo		
	FY3/18	FY3/19	YoY	2017	2018	YoY	2017	2018	YoY
Annual active user (mn)	552	654	18.5%	293	305	4.4%	245	419	71.0%
GMV (RMB bn)	4820	5727	18.6%	1,295	1,677	29.5%	141	472	234.0%
Annual spending per user (RMB)	8,732	8,742	0.1%	4,426	5,492	24.1%	576	1,126	95.3%
Revenue (RMB mn)	250,266	376,844	50.6%	362332	462,019	27.5%	1744	13,120	652.3%
Gross profit (RMB mn)	143,222	169,915	18.6%	50,815	65,953	29.8%	1021	10,215	900.5%
Operating profit (RMB mn)	69,314	57,084	-17.6%	-835	-2,619	213.8%	-596	-10,799	1711.9%
Core net profit (RMB mn)	85,766	100,731	17.4%	4,968	3,460	-30.4%	-373	-3,456	826.5%
Gross margin	57.2%	45.1%		14.0%	14.3%		58.5%	77.9%	
Operating margin	27.7%	15.1%		-0.2%	-0.6%		-34.2%	-82.3%	
Core net margin	34.3%	26.7%		1.4%	0.7%		-21.4%	-26.3%	

Source(s): Companies, ABCI Securities

Business model comparison

Overall, there are two major business models for online e-commerce platforms – in-house and co-op. In our view, each business model has its pros and cons. The decision to adopt which model is dependent on one's business strategies.

Co-op business model: Alibaba and Pinduoduo operate online marketplaces and charge commission on merchants' sales. They also rely on third-party logistics companies for product delivery.

In theory, this model requires less fixed-asset investments and working capital. In addition, product and geographical expansion are also easier as platforms can leverage merchants' product sourcing capabilities and logistic partners' network. However, quality control is more difficult due to multiple parties involved in the supply chain, which can affect customer loyalty.

In-house business model: JD, with its own product inventories and logistic network, is the only major online ecommerce platform adopting an in-house business model.

In theory, this business model, with more control on product quality and supply chain, could potentially lead to better quality assurance and customer loyalty. The drawback is that this model usually requires hefty early-stage investments, which could impact a company's profitability in the beginning years.

Exhibit 32: In-house vs. Co-op –theoretical pros and cons

	In-house	Co-op
Examples	JD	Alibaba, Pinduoduo
Business model	Direct sales	Marketplace
Inventories	Self-owned inventories	Inventories owned by merchants
Logistics network	Self-built logistic network	Third party logistics partners
Product expansion	Harder as platforms need to source new product by itself	Easier as platforms can leverage on merchants' product sourcing capabilities
Geographical expansion	Harder due to the need to establish logistic infrastructure	Generally easier, as platform can leverage on logistic partners' network
Quality assurance	Easier	More difficult due to more parties involved and less control on external parties
Margins	Potentially lower due to higher fixed cost and product cost	Potentially higher as platforms mainly charge sales commission with no inventory cost.
Working capital requirement	Higher	Lower

Source(s): ABCI Securities

DuPont analysis

We conduct a DuPont analysis to study the ROA composition among the three major online ecommerce platforms, Alibaba, JD, and Pinduoduo.

To recap, under the DuPont model:

Return on average asset (ROA) = Core net margin (i.e. core net profit/revenue) x Asset turnover (i.e. revenue/Average total asset).

Having said that, under JD's direct sales business model, it recognizes the direct-sale GMV as revenue, while Alibaba and Pinduoduo only recognizes sales commission as revenue (which is only a small % of GMV) under their marketplace model. As a result, the conventional DuPont formula might not be entirely applicable in this case, in our view.

To account for their accounting treatment difference, we adjust the DuPont formula by replacing revenue with GMV in the equation. So, the revised formula becomes:

Return on average asset (ROA) = (Core net profit/GMV) x (GMV/average total asset)

Alibaba: Alibaba's ROA is the highest among its major peers. In our view, this is mainly driven by its high core net profit/GMV ratio, which could be partly attributed to its co-op business model that does not bear inventory and logistic cost. This is despite the fact that its GMV-to-average total asset ratio is the lowest among the three.

JD: JD's ROA was ranked second (4.6% in 2019). In our view, the main drag is its low core net profit/GMV ratio of 0.5%, which is related to its inventory and logistic cost. Its GMV-to-average total asset ratio is higher than that of Alibaba, implying a more effective use of assets to generate GMV.

Pinduoduo: Pinduoduo is still loss-making with a negative ROA. Its negative core net margin/GMV ratio is mainly due to its high marketing and selling expenses equivalent to 90% of revenue and 114% of gross profit in 2019. Such high expenses are partially caused by the support given to merchants' price promotion. In our view, this subsidy-driven price promotion strategy has led to superior GMV-to-average total asset ratio (16.9x in 2019) but at the expense of overall profitability.

Exhibit 33: ROA analysis (2019)*

	Core net profit/GMV (A)	GMV/average total asset (B)	ROA (AxB)
Alibaba	2.3%	5.0	11.6%
JD	0.5%	8.9	4.6%
Pinduoduo	-0.4%	16.9	-7.2%

*FY3/20E for Alibaba

Source(s): Companies, ABCI Securities

Appendix: Industry trends

China's retail sales dropped by 19.0% YoY in 1Q20, according to National Bureau of Statistics (NBS). Among the product categories, jewelry, automobiles, furniture, apparel, construction materials, and consumer electronics were the hardest hits.

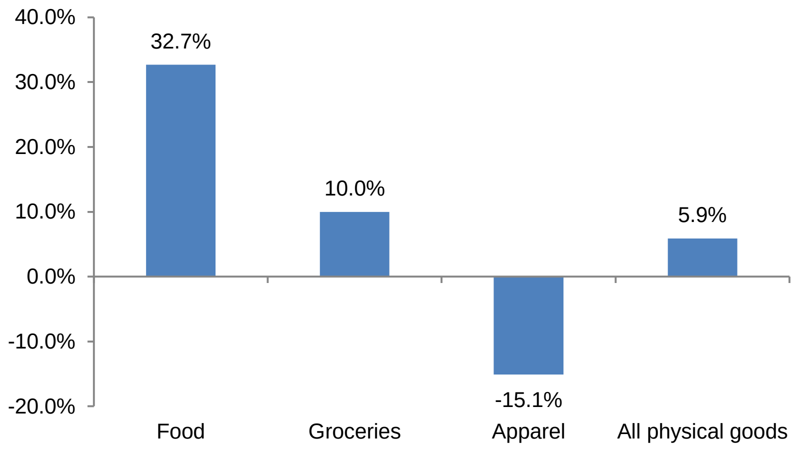
Under the weakening macro backdrop, online sales of physical goods grew by 5.9% in 1Q20, down from 19.5% YoY in 2019. In our view, this would inevitably impact the performance of major online sales platforms. The 5.9% YoY growth in 1Q20 implies sequential improvement in Mar 2020 vs. the 3.0% growth in 2M20.

The recent virus outbreak has prompted more consumers to utilize online shopping, especially for groceries and food products due to the closure of physical shops and cut-off in local transportation. In our view, such changes in consumer behavior could benefit the ecommerce industry as a whole in the long run.

In recent years, we have seen emerging trends in the ecommerce sector benefiting players with strengths in specific areas.

Food products: Overall, food products achieved an online sales growth of 30.9% YoY in 2019, higher than 15.4% and 19.8% YoY for apparel and grocery products, according to NBS. In 1Q20, online sales of food grew by 32.7% YoY, outperforming other major categories. In our view, this is partly driven by ongoing improvement in logistic supply chain, especially the same-day delivery and cold-chain service.

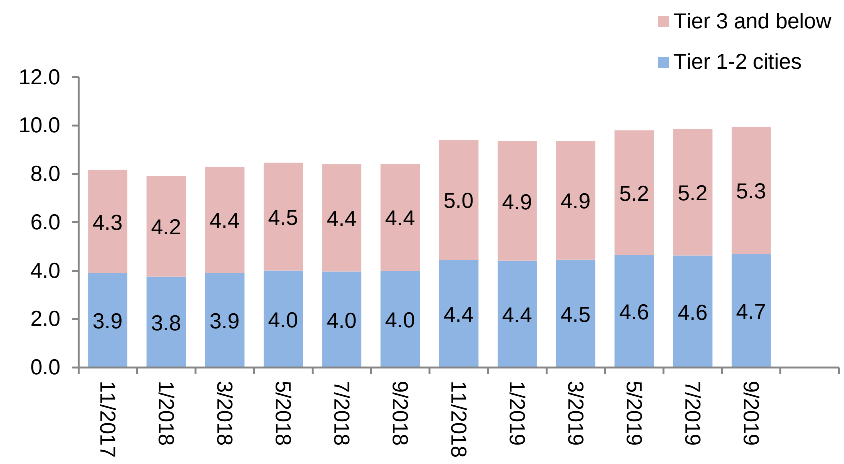
Exhibit 34: China's online sales growth by category (1Q20)



Source(s): NBS, ABCI Securities

Lower-tier cities: Overall, major ecommerce platform have been focusing on lower-tier cities in recent years. About 70% of new customers of Alibaba and JD are from lower tier cities. There were about 1bn mobile shopping users in Sep 2019, according to Questmoibile, in which about 53% of users were from lower-tier cities (tier-3 and below).

Exhibit 35: Number of mobile shoppers by city tier (100m)



Source(s): Questmobile, ABCI Securities

Social ecommerce: Social ecommerce, which leverages social network such as WeChat to allow users to share product information with friends, has become increasingly popular. Consumers could enjoy steep discounts when they share an item to their friends, or by joining an ongoing group-buying deals on the app.

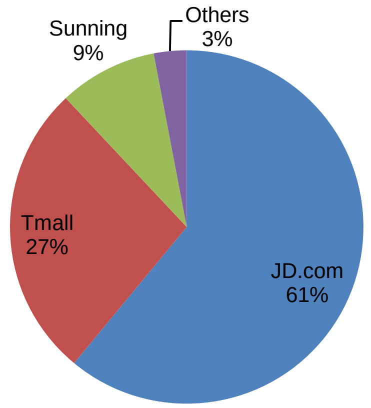
Also, more online brands/online platforms partners with celebrities or internet KOLs (Key Opinion Leader) to offer live videos or short videos to introduce products. E.g., Austin Li (李佳琦), a male KOL famous for selling lipsticks and other cosmetic products in his live program, has over 50mn fans. Another ecommerce KOL, Viya (薇娅), had over 30mn customer views for her live programs in the recent Nov 11 festival. She has also once achieved a record over RMB 300mn daily sales during the Nov 11 festival in 2018.

Market share trend

JD's forte is in the online sales of electronics and home appliance products, which accounted for 64% of its direct sales revenue in 2019. In our view, customers are more willing to purchase high-ticket price items like consumer electronics in an online platform with better quality and assurance such as JD.

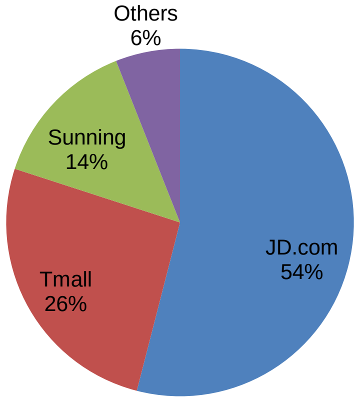
According to CAMIR, JD enjoys a market share of 54% in online sales of mobile phone, doubling that of Tmall in 3Q19. In addition, JD has a dominant market share in the online sales of notebook PC (75%), desktop PC (88%), digital camera (62%), and home appliance (61%) in 3Q19.

Exhibit 36: Market share in China's online sales of home appliance (3Q19)



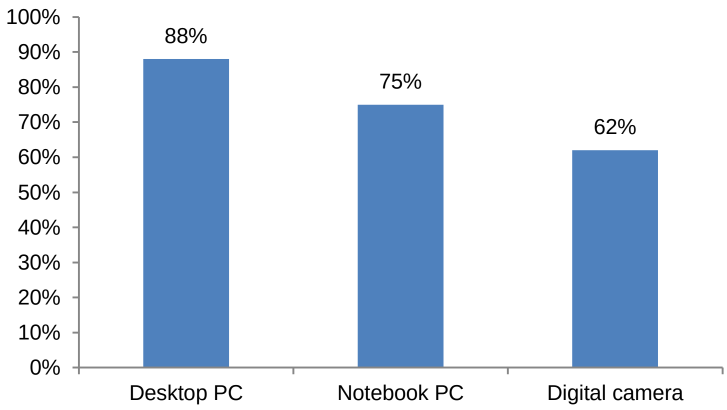
Source(s): CAMIR, ABCI Securities

Exhibit 37: Market share in China's online sales of mobile phone (3Q19)



Source(s): CAMIR,ABCI Securities

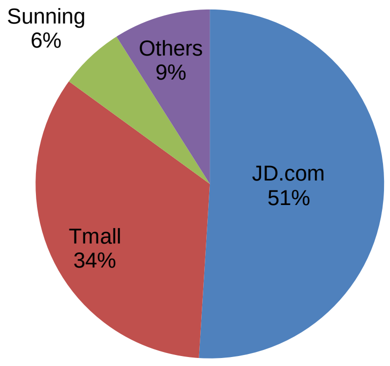
Exhibit 38: JD's online market share in other consumer electronic products (3Q19)



Source(s): CAMIR,ABCI Securities

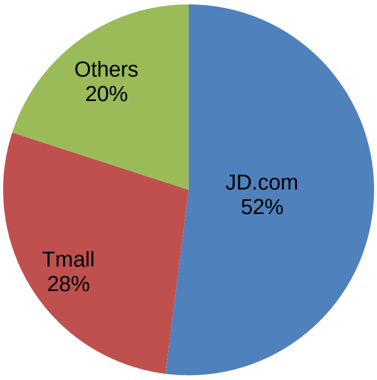
In recent years, JD has been leveraging its premium brand image for other product categories. This strategy has achieved success in some categories. JD's market shares of online sales of infant formula milk powder, cooking oil, and Chinese white wine in 3Q19 were 58%/51%/52%, according to CAMIR.

Exhibit 39: JD's market share in China's online sales of home cooking oil (3Q19)



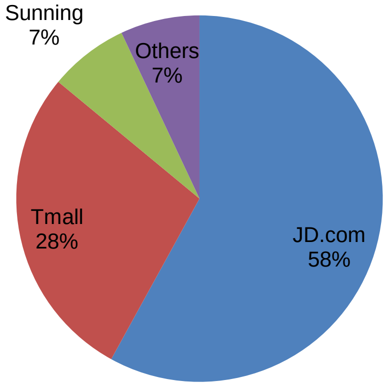
Source(s): CAMIR, ABCI Securities

Exhibit 40: JD's market share in China's the online sales of Chinese white wine (3Q19)



Source(s): CAMIR, ABCI Securities

Exhibit 41: JD's market share in China's online sales of infant formula milk powder (3Q19)



Source(s): CAMIR, ABCI Securities

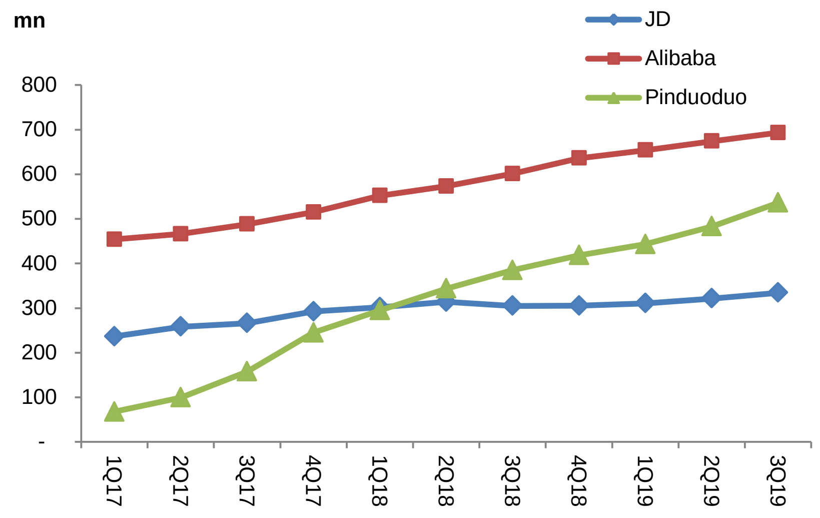
Risk factors

Market competition

The Group competes with other online ecommerce platforms including Alibaba and Pinduoduo. The competition will be on commission rate, promotion discount, brand advertising, technological investment, and more.

Pinduoduo has been experiencing rapid growth in recent years, with its active users reaching 536mn in Sep 2019 vs. 68mn in 1Q17. Its number of active users has exceeded that of JD since 2Q18. Overall, Pinduoduo has been particularly popular in lower-tier cities due to heavy promotion discounts.

Exhibit 42: User comparison



Source(s): Companies, ABCI Securities

Slowing ecommerce consumption

As the Group is exposed to consumer spending on services, any significant slowdown of consumption in China would impact financial performance. In the long term, we believe domestic market growth would converge with income growth, which is usually in line with GDP growth.

No dividend record to ordinary shareholders

The Group has omitted dividend to ordinary shareholders since listing. In our view, this could due to its weak profitability over the past few years. Having said that, the situation might changes in the medium term should its profitability continue to improve over the next few years driven by ongoing margin expansion.

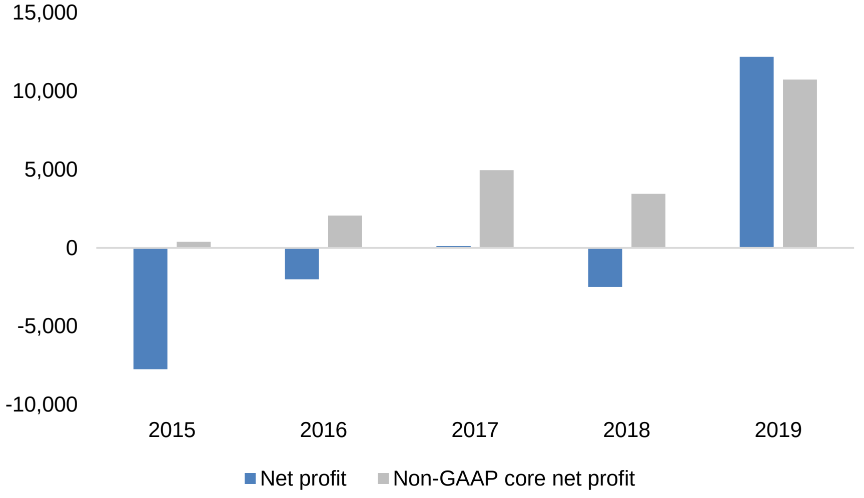
Non-GAAP financials

The Group has disclosed the non-GAAP financial metrics, such as the non-GAAP net profit, to supplement its GAAP financial measures. Historically, there were significant differences between its GAAP net profit and non-GAAP net profit due to inclusion of items such as share-based compensation, impairment, fair valuation changes of investment, and disposal gains of asset 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. JD's share-based compensation expenses have been trending up over the past few years, rising from RMB 1.1bn in 2015 to RMB 3.7bn in 2019.

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 reference.

Exhibit 43: Net profit vs. Non-GAAP core net profit (RMB m)



Source(s): the Group, ABCI Securities

Financial Statements

Consolidated income statement (2018A-2021E)

FY Ended Dec 31 (RMB mn)	2018A	2019A	2020E	2021E
Net product revenue	416,109	510,734	623,750	736,972
Net service revenue	45,911	66,154	86,427	109,731
Total revenue	**462,019**	**576,888**	**710,178**	**846,703**
Cost of sales	-396,066	-492,467	-603,673	-718,870
Gross profit	**65,953**	**84,421**	**106,505**	**127,833**
Fulfillment expenses	-32,010	-36,968	-45,207	-52,098
Marketing expenses	-19,237	-22,234	-27,360	-31,739
Technology & content expenses	-12,144	-14,619	-16,195	-18,302
General & admin expenses	-5,182	-5,490	-4,993	-4,727
Gains on disposal	0	3,885	0	0
Operating Profits	**-2,619**	**8,995**	**12,751**	**20,968**
Interest income	-1,113	-1,738	-1,600	-1,600
Interest expenses	2,118	1,786	1,600	1,650
Share of results of equity investees	-855	-725	-850	-900
Others, net	95	5,375	100	100
PBT	**-2,374**	**13,693**	**12,001**	**20,218**
Tax	-427	-1,802	-2,087	-3,568
PAT	**-2,801**	**11,890**	**9,913**	**16,650**
Minority interests	-309	-293	-250	-250
Profits attributable to shareholders	**-2,492**	**12,184**	**10,163**	**16,900**
Share-based compensation	3,660	3,695	2,163	1,893
Amortization	1,806	885	1,420	1,693
Impairment/FV changes of investments	808	-745	0	0
Other non-core items	-321	-5,269	-513	-727
Non-GAAP profits attributable to shareholders	**3,460**	**10,750**	**13,234**	**19,760**
Growth				
Total revenue (%)	27.5	24.9	23.1	19.2
Gross Profits (%)	29.8	28.0	26.2	20.0
Operating Profits (%)	213.8	-443.4	41.7	64.4
Net profit (%)	-2,239.3	-588.8	-16.6	66.3
Non-GAAP net profit (%)	-30.4	210.7	23.1	49.3
Operating performance				
Operating margin (%)	-0.6	1.6	1.8	2.5
Net margin (%)	-0.5	2.1	1.4	2.0
Core net margin (%)	0.7	1.9	1.9	2.3
ROAE (%)	-4.4	16.7	11.1	15.6
ROAA (%)	-1.3	5.2	3.6	5.1

Note: Individual items may not sum to total due to rounding
Source(s): the Group, ABCI Securities estimates

Consolidated balance sheet (2018A-2021E)

As of Dec 31 (RMB mn)	2018A	2019A	2020E	2021E
Fixed assets	38,112	37,352	53,852	70,352
Investments	47,258	56,993	56,993	56,993
Other non-current assets	18,939	26,284	29,184	32,084
Total non-current assets	**104,309**	**120,629**	**140,028**	**159,428**
Cash & equivalents	37,502	39,912	41,233	48,302
Short-term investments and investment securities	2,036	24,603	24,603	24,603
Inventories	44,030	57,932	68,415	81,470
Account receivables	11,110	6,191	27,240	32,476
Other current assets	10,178	10,457	10,457	10,457
Total current assets	**104,855**	**139,094**	**171,946**	**197,307**
Total assets	**209,164**	**259,723**	**311,975**	**356,736**
Account payables	93,003	106,507	145,083	169,700
Borrowings and notes	4,545	0	0	0
Other current liabilities	23,314	33,510	33,510	33,510
Total current liabilities	**120,862**	**140,017**	**178,592**	**203,210**
Payables & accruals	309	226	226	226
Borrowings and notes	9,874	10,052	10,052	10,052
Other non-current liabilities	1,291	8,805	8,805	8,805
Total non-current liabilities	**11,474**	**19,082**	**19,082**	**19,082**
Total liabilities	**132,336**	**159,099**	**197,674**	**222,292**
Mezzanine equity	**15,961**	**15,964**	**15,961**	**15,961**
Equity attributable to shareholders	59,771	81,856	95,782	116,176
Non-controlling interests	1,096	2,804	2,554	2,304
Total equity	**60,866**	**84,660**	**98,336**	**118,479**

Notes: Individual items may not sum to total due to rounding
Individual items may vary from reported figures due to rounding /definition differences
Source(s): the Group, ABCI Securities estimates

Consolidated cash flow statement (2018A-2021E)

As of Dec 31 (RMB mn)	2018A	2019A	2020E	2021E
Operating cash flow	**20,881**	**24,782**	**26,321**	**32,069**
Investing cash flow	**-26,078**	**-25,349**	**-25,000**	**-25,000**
Financing cash flow	**11,220**	**2,573**	**-**	**-**
Effective of FX	1,681	405	-	-
Net cash flows	**7,704**	**2,410**	**1,321**	**7,069**

Notes: Individual items may not sum to total due to rounding
Individual items may vary from reported figures due to rounding /definition differences
Source(s): the Group, ABCI Securities estimates

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Definition of equity rating

Rating	Definition
Buy	Stock return rate≥ Market return rate (10%)
Hold	- Market return rate (-10%) ≤ Stock return rate < Market return rate (+10%)
Sell	Stock return < - Market return (-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 2008-19 CAGR at 10%)

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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