



農銀國際

ABC INTERNATIONAL

ABCI SECURITIES COMPANY LIMITED



## China Ecommerce Sector

Long-term positive view unwavered



## China Ecommerce Sector

### Long-term positive view unwavered

- Intact long-term sector outlook as tightened regulatory environment is unlikely to deter consumers' growing desire to shop online
- Tightening regulatory environment would prompt major ecommerce platforms to fine-tune their business practices; Major ecommerce platforms' direct exposures to FinTech are overall manageable,
- We continue to like **JD (JD US/9618 HK)** for its supply chain prowess, and **Meituan (3690 HK)** for its leading position in consumer service ecommerce. For **Alibaba (BABA US/9988 HK)**, we are still positive on its prospects and see medium term value at current valuation

## Sector Report

### OVERWEIGHT

#### Feb 10, 2021

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**Navigating through regulatory headwinds.** The FinTech market is the key target of the recent regulatory actions, which could lead to significant changes in business model and growth outlook. On a positive note, major ecommerce platforms' direct exposures to FinTech are overall manageable and their core ecommerce business is likely to face more manageable regulatory impact such as fine-tuning their business practices in new business development, consumers' protection, relationship with online merchant, etc.

**Demand side remains intact.** Tightened regulatory environment is unlikely to deter consumers' growing desire to shop online. The ecommerce sector is experiencing a structural boost in the post-COVID-19 era driven by ongoing consumption shift from offline to online. E.g., the 4.2ppt increase in online shopping penetration rate in 2020 is significantly higher than the averaged 2.5ppt annual increment between 2016-2019.

**Divergent valuation trend.** We maintain our long-term positive view on China's ecommerce sector. Overall, the recent regulatory headwinds have led to divergent valuations among the major listed ecommerce platforms, with Alibaba lagging behind its peers. In our view, such divergent trend could potentially normalize in coming months should the markets see more clarity regarding the regulatory development. We continue to like JD for its supply chain process and Meituan for its leading position in consumer service ecommerce. For Alibaba, despite recent share price volatility, we are still positive on the medium-term prospects given its dominant position in the industry. The lower valuation after recent share price corrections only adds to its appeal, in our view.

#### Sector valuation summary

Company	Ticker	Rating	TP	2020E P/S(x)	2021E P/S(x)	2020E Core P/E(x)*	2021E Core P/E(x)*
Alibaba - ADR	BABA US	BUY	US\$351	6.8	5.3	28.0	22.1
Alibaba - SW	9988 HK	BUY	HK\$340	6.7	5.2	29.5	23.3
Meituan-W	3690 HK	BUY	HK\$480	17.1	11.6	347.1	118.8
Pinduoduo	PDD US	BUY	US\$230	28.5	16.1	NA	248.2
JD -ADR	JD US	BUY	US\$116	1.4	1.1	72.7	48.7
JD - SW	9618 HK	BUY	HK\$450	1.4	1.1	73.6	49.3
VIP SHOP	VIPS US	BUY	US\$40	1.5	1.3	22.9	17.9

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

Source(s): ABCI Securities estimates



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## Navigating the regulatory headwinds

Overall, there were various regulatory developments on online platforms in recent months, suggesting a tightened regulatory environment for the industry.

For examples, the State Council has issued antitrust guideline in Feb 2021 on online platforms, giving guidance on various aspects including monopoly agreement, abuse of dominance, etc. For example, the antitrust guideline prohibits various business practices including blocking merchants to co-operate with competitive platforms, using data and algorithms to manipulate the market, unfair product pricing, etc.

In addition, the “2020 Central Economic Work Conference” held in Dec 2020 has highlighted various policy goals on the internet sector:

- Support the innovation and development of platform enterprises and enhance global competitiveness;
- Improve the legal framework for platform enterprises in the area of antitrust, data collection, and consumer rights protection;
- Strengthen regulations, enhance supervision capabilities, and oppose monopoly and unfair competition;
- FinTech innovation must be carried out under close supervision;
- Optimize the income distribution structure and expand the middle class;
- Removal of certain administrative restrictions on consumption; fully unleash the consumption potential in rural regions.

The regulators have also recently announced various measures to regulate the online community group-purchase market, including prohibiting low-price dumping, price collusion, monopoly agreement, discriminatory pricing based on big data, illegally collecting and using consumer personal information, etc.

In addition, the regulators have conducted an antitrust investigation on Alibaba's business practice, such as requiring online merchants to set up exclusive online stores in its platform.

### FinTech platforms – drastic changes of existing business model

The Fintech market is the key target of the recent regulatory actions. The regulator has announced the regulatory requirements for the Ant Group, including

- Return to its origins in online payments and prohibit irregular competition
- Protect customers' privacy in operating its personal credit rating business
- Establish a financial holding company to manage its FinTech businesses
- Rectify any irregularities in its insurance, wealth management, and credit businesses in accordance with regulations

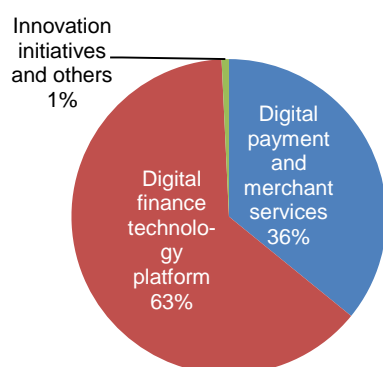
In addition, according to media reports, the regulators are reviewing Ant's various strategic investments.

In our view, the new regulatory framework might imply significant changes in the business models of the large-scale FinTech platforms, which may lower growth ahead. In the long run, however, overall business/financial risks could be reduced with more stringent regulatory requirements.

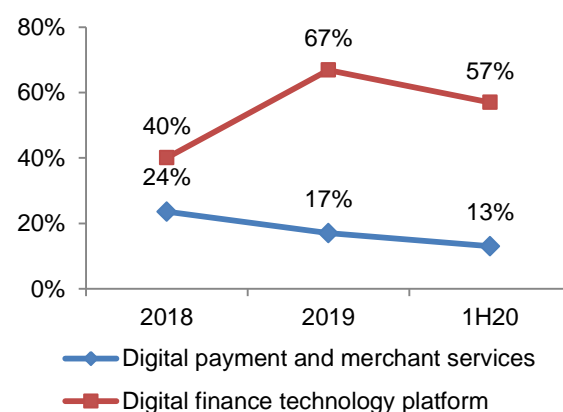
Taking Ant as an example, in addition to its online payment business, it leverages its massive user base and technological know-how to provide digital finance solutions to partner financial institutions, enabling them to provide services in consumer credit, SMB credit, investments and insurance. It is the largest online consumer credit and SMB credit services provider in China in terms of total outstanding credit balance originated (RMB 1.7tr for consumers and RMB422 bn for small businesses, as of June 30 2020), according to Oliver Wyman. Overall, its consumer and SMB credit balance has grown from RMB 647bn at end-2017 to RMB 2.2tr by June 2020.

Its existing business model does not use its own balance sheet or provide guarantees in order to minimize credit risk. Instead, it collaborates with ~100 partner banks through its technology platform. It originates loans, which are then independently underwritten by its partner financial institutions.

Its digital finance business collectively accounted for 63% of revenue in 1H20 and is the major growth driver for Ant. In 1H20, digital finance revenue was up 57% YoY while its digital payment business only reported a 13% YoY revenue growth.

**Exhibit 1: Ant's revenue mix (1H20)**


Source(s): Company, ABCI Securities

**Exhibit 2: Ant's segment revenue growth**


Source(s): Company, ABCI Securities

Although there are limited details available at the moment, the media reports that regulators might require Ant's digital finance business to comply with the existing regulatory framework for financial enterprises, which could potentially lead to additional capital or funding requirements for its online credit business.

At June 2020, Ant had RMB 105bn in cash and RMB 215bn in equity, accounting for about 5% and 10% of its outstanding loan balance. Should any capital or funding requirements be imposed, Ant might need to raise capitals or scale back its online lending portfolio.

On a positive note, we believe major ecommerce platforms' direct exposures to FinTech are overall manageable. For example, we estimate that Ant accounted for 8% of Alibaba's core net profit in 9M20, while JD Digits only accounted for 1.6% of JD's core net profit in 1H20.

**Ecommerce platforms – fine-tuning selected business practices**

On a positive note, we believe recent regulatory actions should lead to more manageable impact on the e-commerce market than the FinTech market, as many aspects of the regulatory concerns has already covered in the ecommerce law introduced in 2019.

Overall, the 2019 ecommerce law covers various areas including e-contracts and e-payments, guarantees for ecommerce transactions; data protection and promotion of consumer protection, fair competition, and mechanisms for dispute resolution; cross-border commerce, etc.

Under the ecommerce law, ecommerce platforms are prohibited from imposing unreasonable restrictions, conditions, or fees on merchants. In addition, the ecommerce law further fosters consumer protection and competition by requiring the ecommerce operator to disclose accurate product/service information and to avoid engaging in misleading and deceptive practices. Ecommerce platforms will also have to establish a system to post consumer comments and introduce other measures to ensure accurate information, such as prohibiting misleading promotions, fake reviews, and other attempts to manipulate the market.

We view the recent regulatory actions as an extension of the 2019 ecommerce law. Unlike FinTech platforms which should face drastic changes of their existing business model, e-commerce platforms might only need to fine-tune some of their existing business practices to meet the additional regulatory requirements.

For example, pricing transparency and effort to combat counterfeit products would need to be enhanced. In addition, online platforms might find it more difficult to acquire brands to set up exclusive online stores on their platforms.

**Rationalizing new businesses strategy**

In terms of new business development, major online platforms may turn more prudent in developing new business initiatives in areas such as grocery retail, community group purchase, etc., so as to reduce the potential negative impacts on traditional retailers.

While slower growth of these initiatives can be expected in the near term, losses may be reduced as many of these initiatives are loss-making in their nascent development stages.

Alibaba's core commerce initiatives, which include local consumer services, new retail, etc., collectively reported RMB5bn in negative EBITA in 3Q20. This dragged down its total EBITA by 11%.

For Meituan, its new business initiatives including grocery retail, community group-purchase, etc., collectively reported RMB 2bn in operating losses in 3Q20, dragging down its total operating profit by 23%.

In addition, major online platforms might adjust the business models of their new business initiatives to focus more on collaboration with offline retailers or creating more employments in lower-tier cities.



We believe ecommerce platforms with a direct-sales business model, such as JD.com, would encounter less regulatory risks than those with a marketplace business model, such as Alibaba and Pinduoduo, mostly because the former model generally entails better product quality control. In addition, unlike the marketplace business model, the direct-sales model is less exposed to potential regulatory risks related to business terms with online merchants.

Exhibit 3: Business model comparison

	Alibaba	JD.com	Pinduoduo	VIPSHOP
Direct sales	NA	Direct sales accounted for 89% of revenue in 2019	NA	Core apparel products
Online marketplace	Taobao and Tmall	Marketplace accounted for 7% of revenue in 2019	"team purchase" model to allow customers to purchase products at low prices	Low-margin product categories
Omni-channel initiatives	Freshippo –grocery retail chain  Partnership with various offline retailers including SunArt, Starbucks, Suning, Intime, Lianhua Supermarket, Red Star Macalline, etc., on omni-channel initiatives	Online-to-offline supermarket platform  7FRESH- 24/7 fresh food supermarket  SEVEN FUN- lifestyle space in Beijing to provide meal and leisure options  Partnership with Walmart	Strategic partnership with Gome Retail	Acquired ShanShan Outlet (杉杉奥特莱斯), a major outlet retail chain in China in 2019.
Logistic network	Cainiao Network	Self-owned logistics network (JD Logistics)	External logistic partners	External logistic partners
Fintech	Ant Group (33% stake)	JD Digits (36.8% stake)	NA	NA

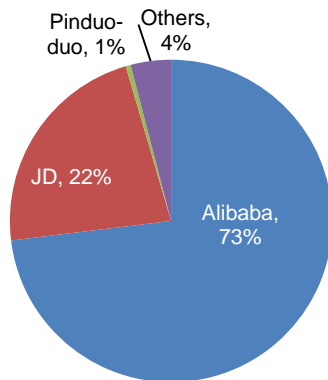
Source(s): Companies, ABCI Securities



### Market shares shows increasing diversity

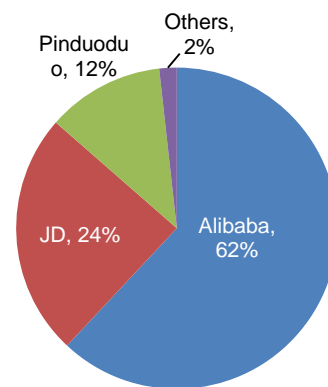
On a positive note, from a macro perspective, the market share distribution of major ecommerce platforms has been less concentrated in recent years. Alibaba's market share dropped from 73% in 2016 to 62% in 2019, based on NBS data and our estimates, while Pinduoduo's share increased from 1% to 12% during the same period. This indicates the industry has become less monopolistic over the past few years. In our view, this could potentially alleviate regulator's concern on industry-wide antitrust behavior in the sector.

Exhibit 4: Online shopping market share 2016



Source(s): Companies, NBS, ABCI Securities

Exhibit 5: Online shopping market share 2019



Source(s): Companies, NBS, ABCI Securities





## Demand side remains resilient

We believe the ecommerce sector is experiencing a structural boost in the post-COVID-19 era driven by ongoing consumption shift from offline to online. The tightened regulatory environment is unlikely to deter consumers' growing desire to shop online.

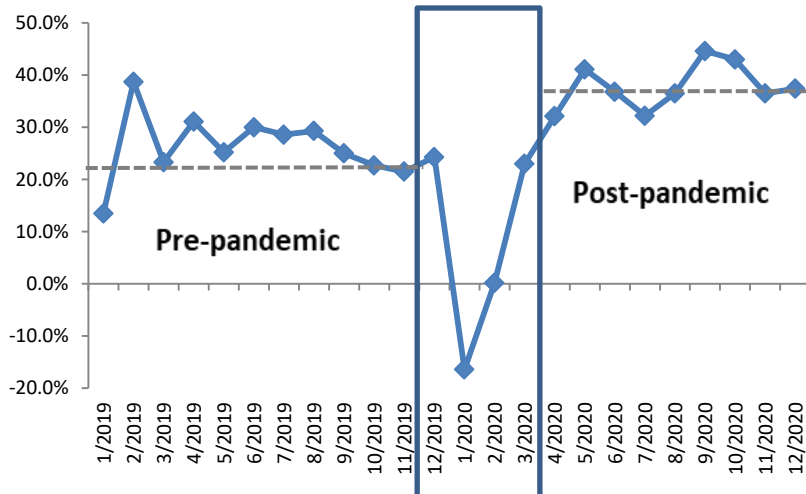
Our view is supported by the trend of volume growth of the express delivery industry (the downstream industry of the ecommerce sector). Volume change in the express delivery industry is often used as a proxy to indicate the general health of the ecommerce industry.

**Pre-pandemic (2019):** In 2019, the monthly volume growth in the express delivery industry averaged at 26% YoY.

**COVID-19 outbreak (1Q20):** The express delivery industry was heavily impacted in 1Q20 due to cut-off in local transportation.

**Post-pandemic (2Q20 onwards):** The express delivery industry experienced a speedy recovery along with the ecommerce industry. The average monthly volume growth accelerated to about 38% YoY in during Apr-Dec, 12ppt higher than the pre-pandemic growth rate. In our view, this represents a shift in consumer behavior to online shopping.

Exhibit 6: Volume growth in China's express delivery

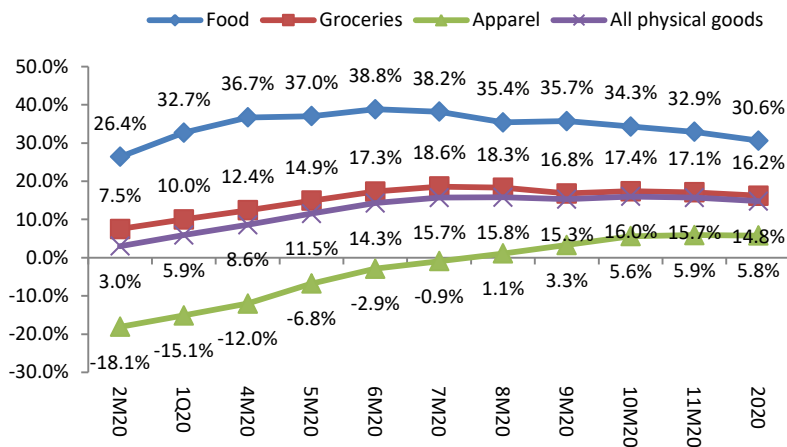


Source(s): State Post Bureau, ABCI Securities

Online sales of physical goods in China increased by 14.8% YoY in 2020. By product category, food product continued to be the outperformer, followed by groceries. In addition, growth in apparel online sales has returned to the positive territory since 8M20. Overall, the recovery is broad-based.



Exhibit 7: China online sales of physical goods by product

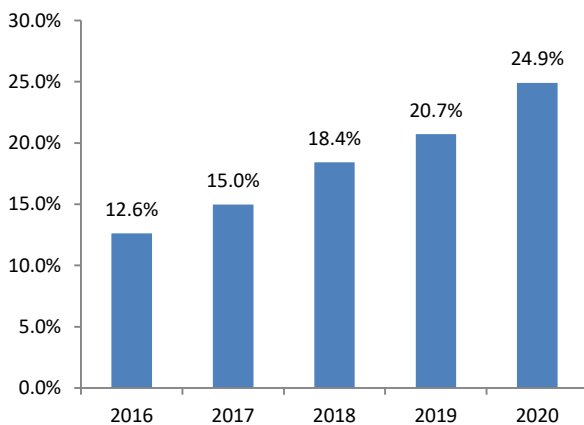


Source(s): NBS, ABCI Securities

In addition, the online shopping penetration rate (online sales of physical goods/total retail sales) has been rising rapidly. Penetration rate of online shopping increased by 3.5ppt YoY to 18.4% in 2018 and 2.3ppt YoY to 20.7% in 2019. In 2020, the penetration rate was up 4.2ppt to 24.9%, the most in recent years, indicating an accelerating shift to online consumption.

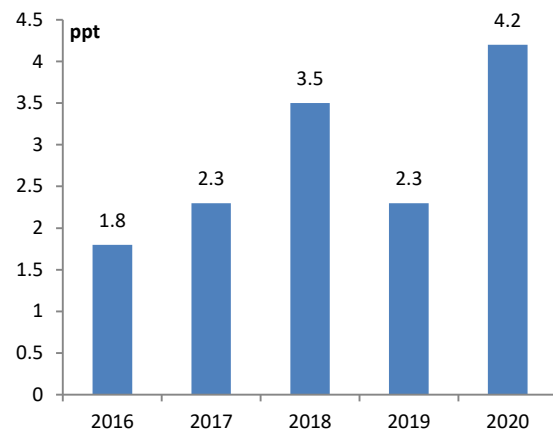
Looking forward, industry growth should remain resilient in 1Q21 due to low base (online sales of physical goods only grew by 5.9% YoY in 1Q20 amid pandemic.)

Exhibit 8: Online shopping penetration rate



Source(s): NBS, ABCI Securities

Exhibit 9: Online shopping penetration rate –increment



Source(s): NBS, ABCI Securities

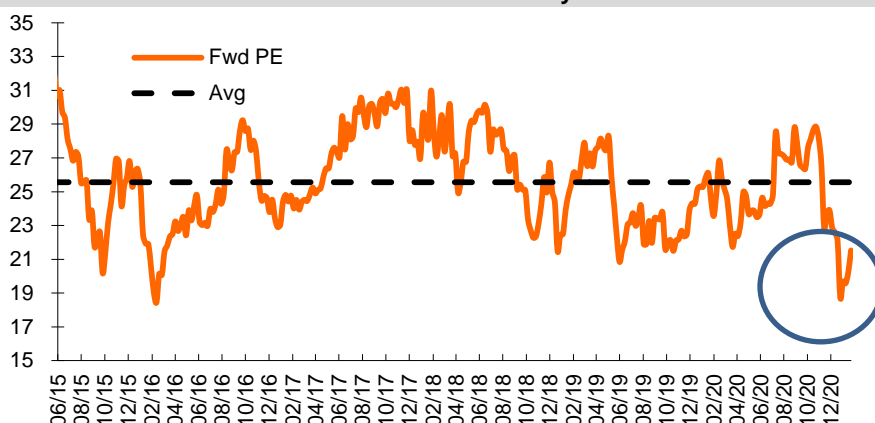


## Recommendation

We maintain our long-term positive view on China's ecommerce sector despite recent share price volatility amid regulatory concerns.

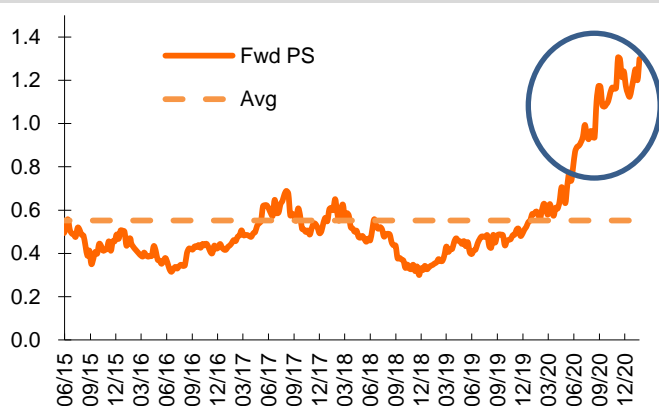
Overall, the tightening regulations have led to divergent valuations among the major listed ecommerce platforms, with Alibaba lagging behind its peers such as JD and Meituan. Alibaba's valuation is currently significantly below its long-term average. Valuation of JD.com and Meituan continues to trade at above their respective historical averages. In our view, such divergent trend could potentially normalize in coming months should the markets see more clarity regarding the regulatory development.

**Exhibit 10: Alibaba's fwd P/E – the lowest in recent years**



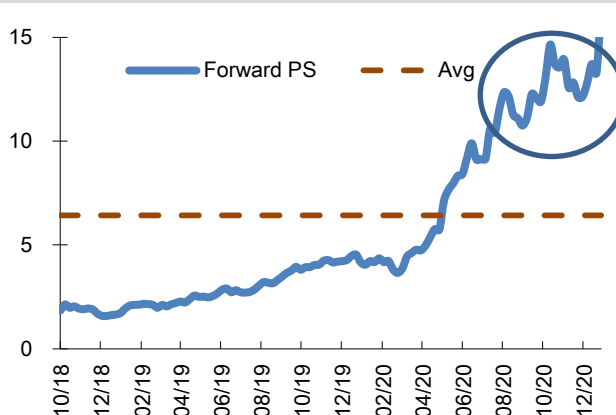
Source(s): Bloomberg, ABCI Securities

**Exhibit 11: JD – fwd P/S**



Source(s): Bloomberg, ABCI Securities estimates

**Exhibit 12: Meituan – fwd P/S**



Source(s): Bloomberg, ABCI Securities estimates

Among the listed ecommerce platforms, we continue to like JD for its supply chain process and Meituan for its leading position in consumer service ecommerce. For Alibaba, despite recent share price volatility, we are still positive on the medium-term prospects given its dominant position in the industry. The lower valuation after recent share price corrections only adds to its appeal, in our view.



## Alibaba (BABA US/9988 HK) Intact medium-term outlook

- Intact medium-term business outlook driven by structural industry uptrend despite ongoing regulatory headwinds
- Manageable direct exposure on Ant Group, which accounted for c. 8% of Alibaba's core net profit in 9M20
- Recent share price corrections support medium-term value

**Intact medium-term outlook.** Despite ongoing regulatory headwinds, which have hindered share price performance in recent weeks, we believe Alibaba's medium-term business outlook remained largely intact because of the structural uptrend in ecommerce industry supported by ongoing shift from offline to online consumption in the post-pandemic era. While its 33%-owned Ant Group may be more heavily affected under the regulatory framework, we believe the overall impact on Alibaba is manageable since Ant only accounts for about 8% of Alibaba's core net profit in 9M20.

**4Q20 review.** Alibaba's revenue grew by 37% YoY to RMB221bn in 4Q20 (3QFY3/21), indicating a sequential improvement versus the 30% YoY revenue growth in 3Q20. Core net profit grew by 25% YoY to RMB60.6bn. Core commerce revenue reported 38% YoY growth in 4Q20 versus 29% YoY growth in 3Q20 amid 19% YoY growth of Tmall physical goods GMV during the quarter. In addition, the cloud segment achieved positive adjusted EBITA during the quarter thanks to improving economy of scale.

**Business outlook.** For FY3/20-22E, we expect GMV to grow at 12% CAGR to RMB 8.2tr by FY3/22E, driven by the growing number of active users and higher user spending. Revenue would increase at 32% CAGR in FY3/20-22E while core net margin (excl. impacts of share-based compensation and other non-operating items) would be 24.9% for 2022E. We estimate FY3/20-22E core net profit CAGR to be 22%.

**Valuation and recommendation.** We maintain **BUY** on Alibaba. While ongoing regulatory headwind could continue to lead to share price volatility in the near term, we see the emergence in medium-term value given the lower valuation after recent share price corrections.

### Results and Valuation

FY end Mar 31	FY19A	FY20A	FY21E	FY22E
Revenue (RMB mn)	376,844	509,711	687,325	881,366
Chg (% YoY)	50.6	35.3	34.8	28.2
Net profit (RMB mn)	87,600	149,263	176,774	183,335
Chg (% YoY)	36.9	70.4	18.4	3.7
Core net profit (RMB mn)	100,731	141,344	165,994	210,883
Chg (% YoY)	17.4	40.3	17.4	27.0
Underlying EPS (RMB)	4.2	7.1	8.2	8.5
Chg (% YoY)	35.5	67.3	16.0	3.7
Core EPS (RMB)*	4.9	6.6	7.7	9.8
Chg (% YoY)	16.2	35.0	17.4	27.0
Core P/E (x) - ADR*	45.0	32.9	28.0	22.1
Core P/E (x) - SW share*	44.9	31.3	29.5	23.3
ROAE (%)	16.8	20.2	18.1	15.2
ROAA (%)	10.4	13.1	12.2	10.5

1 ADR = 8 ordinary shares

\*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\$ 340  
Rating (ADR): BUY  
TP (ADR): US\$ 351

Analyst : Steve Chow  
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Price (ADR/SW-share)	US\$266.5/ HK\$255.4
Est. share price return (ADR/SW-share)	31.7%/33.1%
Est. dividend yield (ADR/SW-share)	NA/NA
Est. total return (ADR/SW-share)	31.7%/33.1%
Last Rating & TP (ADR/SW-share)	BUY, US\$351/ BUY, HK\$340

Previous Report Date Oct 8, 2020

Source(s): Bloomberg, ABCI Securities estimates

### Key Data

52Wk H/L (HK\$) (SW-share)	292.0/167.6
52Wk H/L (US\$) (ADR)	299.0/161.7
Issued shares (mn)	21,645
Market cap (HK\$ mn) (all share)	5,528,133
3-mth avg daily turnover (HK\$ mn) (SW-share)	9,629
3-mth avg daily turnover (US\$ mn) (ADR)	6,846
Major shareholder(s) (%):	
Softbank	25.1%
Jack Ma	6.0%
Joseph Tsai	1.9%

Source(s): Bloomberg, HKEX, Company



## Financial outlook

For FY3/20-22E, we expect GMV to grow at 12% CAGR to RMB 8.2tr by FY3/22E, driven by the growing number of active users and increased user spending. We expect revenue to grow at 32% CAGR in FY3/20-22E. Among Alibaba's major business segments, core commerce would expand at 30% CAGR in FY3/20-22E; revenue from cloud computing and media/innovative initiatives would grow at 57% and 10% CAGRs in FY3/20-22E.

### Exhibit 13: Major assumptions

	FY19	FY20	FY21E	FY22E
Annual active buyers (mn)	654	726	820	886
Annual GMV per customer (RMB)	8,757	9,076	9,085	9,266
Total GMV (RMB bn)	5,727	6,589	7,453	8,210

Source(s): Company, ABCI Securities estimates

### Exhibit 14: Revenue forecasts

(RMB mn)	FY3/19	FY3/20	FY3/21E	FY3/22E
China retail revenue	247,615	332,750	449,213	561,516
China wholesale	9,988	12,427	14,291	17,149
International commerce	27,725	33,917	46,805	58,507
Cainiao logistics	14,885	22,233	35,573	53,359
Consumer service (Ele.me)	18,058	25,440	30,528	35,107
Others	5,129	9,337	12,605	15,756
<b>Core commerce</b>	<b>323,400</b>	<b>436,104</b>	<b>589,015</b>	<b>741,394</b>
Cloud computing	24,702	40,016	62,025	99,240
Digital media/ Innovation initiatives	28,742	33,591	36,286	40,732
<b>Total revenue</b>	<b>376,844</b>	<b>509,711</b>	<b>687,325</b>	<b>881,366</b>

Source(s): Company, ABCI Securities estimates

**Gross margin:** Gross margin declined to 44.6% in FY3/20 vs. 57.2% in FY3/18 mainly due to changes in business mix caused by the consolidation of Cainiao Network and Ele.me. Looking forward, we expect the trend to continue with gross margin reaching 42.9% by FY22E based on the ongoing changes in business contributions.

**Product development expense:** Non-GAAP product development expenses/sales ratio has remained largely stable at ~6% in recent years. We expect the ratio to be ~6.2% in FY3/21E and FY3/22E due to ongoing R&D investments in new services for merchants and consumers.



**Sales and marketing expenses:** Non-GAAP sales and marketing expenses/sales ratio was 9.2% in FY3/20. We expect the ratio to gradually improve to 8.5% by FY3/22E.

**General & admin expenses:** Non-GAAP general & admin expenses /sales ratio was 4.2% in FY3/20. We expect the ratio to improve to 3.5% by FY3/22E on economies of scale.

We expect core net margin (excl. impacts of share-based compensation and other non-operating items) to be 24.9% for FY3/22E. This would result in a core net profit CAGR of 22% for FY3/20-22E.

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

(FY end Mar 31)	FY3/19	FY3/20	FY3/21E	FY3/22E
Cost of revenue	198,014	275,045	378,029	484,751
Product development expenses	22,057	29,426	41,240	54,645
Sales & marketing expenses	35,369	46,843	63,921	74,916
General & admin expenses	16,102	21,261	26,118	30,848
Amortization of intangible assets	10,727	13,964	15,808	22,916
<b>Total</b>	<b>282,269</b>	<b>386,539</b>	<b>525,117</b>	<b>668,076</b>
<b>% of revenue</b>				
Cost of revenue	52.5%	54.0%	55.0%	55.0%
Product development expenses	5.9%	5.8%	6.0%	6.2%
Sales & marketing expenses	9.4%	9.2%	9.3%	8.5%
General & admin expenses	4.3%	4.2%	3.8%	3.5%
Amortization of intangible assets	2.8%	2.7%	2.3%	2.6%
<b>Total</b>	<b>74.9%</b>	<b>75.8%</b>	<b>76.4%</b>	<b>75.8%</b>

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

Source(s): Group, ABCI Securities estimates

**Exhibit 16: Forecast changes for FY3/21E**

(RMB mn)	old	new	Diff	Comment
Revenues	646,459	687,325	6%	Higher growth assumption
Core profit	162,090	165,994	2%	

Source(s): ABCI Securities estimates

**Exhibit 17: Forecast changes for FY3/22E**

(RMB mn)	old	new	Diff	Comment
Revenues	822,764	881,366	7%	Higher growth assumption
Core profit	204,955	210,883	3%	

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 25x-30x on its FY3/22E core profit. For its strategic investments, we refer to the latest book value and our estimation. The SOTP approach results in a valuation range of HK\$ 315-HK\$ 370 for Alibaba-SW (9988 HK).

**Alibaba-SW (9988 HK):** We set our TP at HK\$ 340

**Alibaba-ADR (BABA US):** Based on our TP of Alibaba-SW, we set the corresponding TP of Alibaba-ADR at US\$ 351 (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 18: SOTP valuation range for Alibaba-SW (9988 HK)

(HKD per share)	Low	High	Remarks
Core business	277	333	25-30x FY3/22E core profit
Strategic investments*	37	37	Latest book value, ABCI Securities estimates
<b>Total</b>	<b>315</b>	<b>370</b>	
Total (ex-Ant)	298	353	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

## Peer valuation analysis

Comparing with the major PRC ecommerce peers, Alibaba is currently trading at a lower P/E than that of JD (JD US/9618 HK) and Pinduoduo (PDD US). In addition to ongoing regulatory headwind, this could also be attributed to the fact that JD and Pinduoduo are still in the early stage of profitability. For JD and Pinduoduo, we believe investors tend to place more emphasis on overall sales momentum than near-term profits.

### Exhibit 19: Peer valuation

		Market cap# (USD mn)	Price (Lcy)	P/sales			Core P/E*		
				2019	2020E	2021E	2019	2020E	2021E
<b>Business model- platform based</b>									
BABA US	Alibaba	721,128	<b>US\$ 266.9</b>	9.1	6.8	5.3	32.9	28.0	22.1
3690 HK	Meituan-B	267,407	<b>HK\$ 402.8</b>	20.0	17.1	11.6	419.2	347.1	118.8
PDD US	Pinduoduo-A	126,972	<b>US\$ 197.2</b>	49.2	28.5	16.1	NA	NA	248.2
<b>Business model – direct sales</b>									
JD US	JD.com	149,746	<b>US\$ 94.6</b>	1.6	1.4	1.1	84.9	72.7	48.7
VIPS US	VIP Shop -A	19,913	<b>US\$ 33.5</b>	1.6	1.5	1.3	29.6	22.9	17.9

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

# All-share market cap for Alibaba and JD

Source(s): Bloomberg, ABCI Securities estimate



## Financial forecast

### Consolidated income statement (FY19A-FY22E)

FY Ended Mar 31 (RMB mn)	FY19A	FY20A	FY21E	FY22E
Core commerce	323,400	436,104	589,015	741,394
Cloud computing & Internet infrastructure	24,702	40,016	62,025	99,240
Others	28,742	33,591	36,286	40,732
<b>Total revenue</b>	<b>376,844</b>	<b>509,711</b>	<b>687,325</b>	<b>881,366</b>
Cost of sales	(206,929)	(282,367)	(389,127)	(503,049)
<b>Gross profit</b>	<b>169,915</b>	<b>227,344</b>	<b>298,198</b>	<b>378,317</b>
Product development expenses	(37,435)	(43,080)	(61,936)	(88,766)
Selling & marketing expenses	(39,780)	(50,673)	(69,727)	(84,487)
General & admin expenses	(24,889)	(28,197)	(36,632)	(48,181)
Amortization/Impairment	(10,727)	(13,964)	(15,808)	(22,916)
<b>Operating Profits</b>	<b>57,084</b>	<b>91,430</b>	<b>114,096</b>	<b>133,968</b>
Interest and investment income	44,106	72,956	75,000	75,000
Interest expenses	(5,190)	(5,180)	(5,700)	(5,700)
Other income	221	7,439	250	250
Share of results of equity investees	566	(5,733)	10,300	13,300
<b>Profit before tax</b>	<b>96,787</b>	<b>160,912</b>	<b>193,946</b>	<b>216,818</b>
Tax	(16,553)	(20,562)	(32,971)	(49,868)
<b>Profit after tax</b>	<b>80,234</b>	<b>140,350</b>	<b>160,975</b>	<b>166,950</b>
Minority interests	7,652	9,083	16,098	16,695
Accretion of mezzanine equity	(286)	(170)	(298)	(309)
<b>Profits attributable to ordinary shareholders</b>	<b>87,600</b>	<b>149,263</b>	<b>176,774</b>	<b>183,335</b>
Share-based compensation	37,491	31,742	48,113	79,323
Amortization and impairment	22,087	39,044	15,808	22,916
Gains on disposals/revaluation of investments	(47,525)	(4,764)	(75,000)	(75,000)
Other non-core items	1,078	(73,941)	298	309
<b>Non-GAAP profits attributable to ordinary shareholders (Core net profit)</b>	<b>100,731</b>	<b>141,344</b>	<b>165,994</b>	<b>210,883</b>
<b>Growth</b>				
Total revenue (%)	50.6	35.3	34.8	28.2
Gross Profits (%)	18.6	33.8	31.2	26.9
Operating Profits (%)	(17.6)	60.2	24.8	17.4
Net profit (%)	36.9	70.4	18.4	3.7
Core net profit (%)	17.4	40.3	17.4	27.0
<b>Operating performance</b>				
Operating margin (%)	15.1	17.9	16.6	15.2
Net margin (%)	23.2	29.3	25.7	20.8
Core net margin (%)	26.7	27.7	24.2	23.9

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

Source(s): Company, ABCI Securities estimates





**Consolidated balance sheet (FY19A-FY22E)**

As of Mar 31 (RMB mn)	FY19A	FY20A	FY21E	FY22E
Fixed assets	92,030	103,387	118,387	133,387
Investments	241,544	350,961	381,261	414,561
Other non-current assets	361,229	395,714	399,906	396,990
<b>Total non-current assets</b>	<b>694,803</b>	<b>850,062</b>	<b>899,554</b>	<b>944,938</b>
Cash & equivalents	189,976	330,503	547,266	820,720
Restricted cash and escrow receivables	8,518	15,479	15,479	15,479
Short-term investments and investment securities	13,189	32,712	32,712	32,712
Prepayments, deposits & other assets	58,590	84,229	84,229	84,229
<b>Total current assets</b>	<b>270,273</b>	<b>462,923</b>	<b>679,686</b>	<b>953,140</b>
<b>Total assets</b>	<b>965,076</b>	<b>1,312,985</b>	<b>1,579,240</b>	<b>1,898,078</b>
Accrued expenses, accounts payable and other liabilities	117,711	161,536	188,308	241,470
Other payables & accruals	25,935	23,204	23,204	23,204
Borrowings and notes	22,466	5,154	5,154	5,154
Deferred revenue	30,795	38,338	68,733	88,137
Merchants deposits	10,762	13,640	13,640	13,640
<b>Total current liabilities</b>	<b>207,669</b>	<b>241,872</b>	<b>299,039</b>	<b>371,605</b>
Borrowings and notes	111,834	120,276	120,276	120,276
Other non-current liabilities	30,171	71,186	71,186	71,186
<b>Total non-current liabilities</b>	<b>142,005</b>	<b>191,462</b>	<b>191,462</b>	<b>191,462</b>
<b>Total liabilities</b>	<b>349,674</b>	<b>433,334</b>	<b>490,501</b>	<b>563,067</b>
<b>Net current assets</b>	<b>62,604</b>	<b>221,051</b>	<b>380,647</b>	<b>581,536</b>
<b>Mezzanine equity</b>	<b>6,819</b>	<b>9,103</b>	<b>9,401</b>	<b>9,711</b>
Equity attributable to shareholders	492,257	755,401	980,288	1,242,946
Non-controlling interests	116,326	115,147	99,049	82,355
<b>Total equity</b>	<b>608,583</b>	<b>870,548</b>	<b>1,079,338</b>	<b>1,325,301</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

**Consolidated cash flow statement (FY19A-FY22E)**

As of Mar 31 (RMB mn)	FY19A	FY20A	FY21E	FY22E
<b>Operating cash flow</b>	<b>150,975</b>	<b>185,737</b>	<b>276,763</b>	<b>333,454</b>
<b>Investing cash flow</b>	<b>(151,060)</b>	<b>(60,000)</b>	<b>(60,000)</b>	<b>(60,000)</b>
<b>Financing cash flow</b>	<b>(7,392)</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Net cash flows</b>	<b>(7,477)</b>	<b>125,737</b>	<b>216,763</b>	<b>273,454</b>

Note. 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



## JD.com (JD US/9618 HK)

### Supply chain prowess

- More defensive against regulatory risk than Alibaba
- Thanks to 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** with a revised TP of US\$ 116 for JD-ADR (JD US) and HK\$ 450 for JD-SW (9618 HK)

**More defensive against regulatory risks.** We believe JD would be more defensive than Alibaba under the current regulatory environment given its less dominant market share of ~24% in 2019 versus 62% for Alibaba. In addition, its direct-sales business model could reduce potential regulatory risks related to business practice with online merchants.

**A premium online retailer with superior supply chain capabilities.** In our view, JD's direct-sales business model, superb quality control, and robust in-house logistic infrastructure form its core competitive edge, allowing it to enjoy a leading market position in online sales of consumer electronics and home appliance products.

**3Q20 review.** In 3Q20, revenue grew by 29% YoY to RMB 174bn. General merchandise products reported a 35% YoY revenue growth in 2Q20, higher than 23% YoY revenue growth for electronics and home appliances. In addition, core net profit grew by 80% YoY thanks to ongoing improvement in operation efficiency.

**Margin expansion underway.** JD's margin has been expanding in recent quarters, thanks to economies of scale and better utilization of logistic capacity. We believe JD's profitability has passed an inflection point, which implies a margin uptrend in the medium term. We expect core net margin to improve to 2.6% in 2021E from 1.9% in 2019.

**Maintain BUY.** We maintain **BUY** with a revised TP of US\$ 116 on **JD-ADR (JD US)** and HK\$ 450 on **JD-SW (9618 HK)** for its unique strength in consumer electronics and home appliances.

### Results and Valuation

FY end Dec 31	2018A	2019A	2020E	2021E
Revenue (RMB mn)	462,019	576,888	736,888	896,280
Chg (% YoY)	27.5	24.9	27.7	21.6
Net profit (RMB mn)	-2,492	12,184	15,724	21,817
Chg (% YoY)	NA	NA	29.1	38.8
Core net profit (RMB mn)	3,460	10,750	18,806	24,698
Chg (% YoY)	-30.4	210.7	74.9	31.3
Underlying EPS (RMB)	-1.7	8.2	10.6	14.7
Chg (% YoY)	NA	NA	29.0	38.8
Core EPS (RMB)	2.4	7.2	12.7	16.6
Chg (% YoY)	-30.4	204.9	74.9	31.3
Core P/E (x)- ADR	258.7	84.9	72.7	48.7
Core P/E (x)-SW share	261.7	85.8	73.6	49.3
ROAE (%)	-4.4	16.7	16.7	18.7
ROAA (%)	-1.3	5.2	5.4	6.3

\*1 ADR = 2 ordinary shares

Source (s): Bloomberg, ABCI Securities estimates

## Company Report

Rating (ADR): BUY  
TP (ADR): US\$ 116  
Rating (SW-share): BUY  
TP (SW-share): HK\$450

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

Price (ADR/SW-share)	US\$ 97.1/ HK\$367.0
Est. share price return ( ADR/SW-share )	19.6%/22.6%
Est. dividend yield ( ADR/SW-share )	NA/NA
Est. total return (ADR/SW-share )	19.6%/22.6%
Last Rating & TP (ADR/SW-share )	BUY, US\$ 93/ BUY, HK\$360

Previous Report Date Oct 8, 2020

Source(s): Bloomberg, ABCI Securities estimates

### Key Data

52Wk H/L (HK\$) (SW-share)	337.2/226.0
52Wk H/L (US\$ ) (ADR)	86.5/27.7
Issued shares (mn)	3,130
Market cap (HK\$ mn) (all share)	1,148,637
3-mth avg daily turnover (HK\$ mn) (SW-share)	2,058
3-mth avg daily turnover (US\$ mn) (ADR)	1,005
Major shareholder(s)	Voting right
Richard Liu	79.0%
Walmart	2.5%

Source(s): Bloomberg, HKEX, Company



## Financial analysis

For 2019-2021E, we expect GMV to grow by 20% CAGR to RMB 3.0tr by 2021E, driven by the growing number of active users and higher user spending.

Overall, we expect revenue to increase at 25% CAGR in 2019-2021E to RMB 896bn by 2021E, propelled by growing GMV and ongoing expansion of new businesses including the logistics. In particular, we expect logistic and other service revenue to grow at 47% CAGR in 2019-21E.

### Exhibit 20: Major assumptions

	2017	2018	2019	2020E	2021E
Annual active customer account (mn)	293	305	362	453	534
GMV (RMB bn)	1,295	1,677	2,085	2,603	2,979
Annual spending per active customer (RMB)	4,426	5,492	5,761	5,753	5,580

Source(s): the Group , ABCI Securities estimates

### Exhibit 21: Revenue forecasts (RMB mn)

	2017	2018	2019	2020E	2021E
<i>Electronics and home appliance</i>	236,269	280,059	328,703	394,444	453,611
<i>General merchandize</i>	95,555	136,050	182,031	254,843	331,296
<b>Net product revenue</b>	<b>331,824</b>	<b>416,109</b>	<b>510,734</b>	<b>649,287</b>	<b>784,906</b>
<i>Marketplace and advertising</i>	25,391	33,532	42,680	51,216	60,435
<i>Logistics and other service</i>	5,116	12,379	23,474	36,385	50,939
<b>Net service revenue</b>	<b>30,508</b>	<b>45,911</b>	<b>66,154</b>	<b>87,601</b>	<b>111,374</b>
<b>Total revenue</b>	<b>362,332</b>	<b>462,019</b>	<b>576,888</b>	<b>736,888</b>	<b>896,280</b>

Source(s): the Group , ABCI Securities estimates

We expect core net margin (excl. impacts of share-based compensation and other non-operating items) to rise to 2.8% by 2021E from 1.9% in 2019. Core net profit would increase at 52% CAGR for 2019-21E.



**Exhibit 22: Non-GAAP cost trend (RMB mn)**

	2017	2018	2019	2020E	2021E
COGS	311,490	395,994	492,385	623,407	758,253
Fulfillment expenses	25,275	31,423	36,363	46,424	54,673
Marketing expenses	13,560	17,815	21,338	25,791	31,370
Technology & content expenses	5,927	10,883	13,180	14,738	17,926
General & admin expenses	2,387	3,036	3,609	3,684	3,585
<b>Total</b>	<b>358,639</b>	<b>459,151</b>	<b>566,874</b>	<b>714,045</b>	<b>865,807</b>
<b>% of revenue</b>					
COGS	86.0%	85.7%	85.4%	84.6%	84.6%
Fulfillment expenses	7.0%	6.8%	6.3%	6.3%	6.1%
Marketing expenses	3.7%	3.9%	3.7%	3.5%	3.5%
Technology & content expenses	1.6%	2.4%	2.3%	2.0%	2.0%
General & admin expenses	0.7%	0.7%	0.6%	0.5%	0.4%
<b>Total</b>	<b>99.0%</b>	<b>99.4%</b>	<b>98.3%</b>	<b>96.9%</b>	<b>96.6%</b>

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

Source(s): the Group, ABCI Securities estimates

**Exhibit 23: Forecast changes for 2020E**

	2020E			Comment
(RMB mn)	old	new	Diff	
Revenues	710,178	736,888	4%	
Net income	13,222	15,724	19%	
Core profit	16,293	18,806	15%	Operational improvement

Source(s): ABCI Securities estimates

**Exhibit 24: Forecast changes for 2021E**

	2021E			Comment
(RMB mn)	old	new	Diff	
Revenues	846,703	896,280	6%	
Net income	19,048	21,817	15%	
Core profit	21,907	24,698	13%	Operational improvement

Source(s): ABCI Securities estimates



## Valuation and TP

We derive JD's valuation range based on the SOTP approach. For JD's core business, we apply the DCF method with a WACC of 10%-7%. For strategic investments, we refer to the latest the book/market value and our estimates. The SOTP approach yields a valuation range of HK\$ 415- 490 for JD-SW (9618 HK).

**JD-SW (9618 HK):** We set our TP at HK\$ 450

**JD-ADR (JD US):** Based on our TP of JD-ADR, we determine TP of JD-ADR to be US\$ 116 (1 ADR represents 2 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 technical factors such as supply/demand dynamics of shares.

### Exhibit 25: SOTP-based valuation range (US\$ per ADR)

Segment	Low	High	Comment
Core business	281	357	DCF –from 10% to 7% WACC
Investments*	133	133	Book/market value/ABCI Securities estimates
<b>Overall</b>	<b>414</b>	<b>490</b>	
<i>Overall (ex-JD Health)</i>	<i>323.8</i>	<i>399.8</i>	<i>For reference only</i>

\*Including HK\$ 90.2 per share for 67.5% stakes of JD Health (6618 HK) based on the latest market value with a 20% holding discount

Source(s): ABCI Securities estimates

### Exhibit 26: TP changes (HK\$ per share)

Old	New	Methodology -old	Methodology -new
<b>360</b>	<b>450</b>	DCF: 8.5% WACC for core business	DCF: 7.5% WACC for core business

Source(s): ABCI Securities estimates



## Peer valuation analysis

JD's comparables are major online ecommerce platforms – Alibaba (BABA US/ 9988 HK), Pinduoduo (PDD US), and VIP Shop (VIPS US). JD is trading at a higher 20E/21E P/E than Alibaba. In our view, this could be justified by its expanding margins and higher profit growth in coming years. JD's profit outlook is highly sensitive to its margins - meaningful upside would emerge if margins improve more than expected.

### Exhibit 27: Peer valuation

Exhibit 21.1 P/E Variation

		Market cap# (USD mn)	Price (Lcy)	P/sales			Core P/E*		
				<u>2019</u>	<u>2020E</u>	<u>2021E</u>	<u>2019</u>	<u>2020E</u>	<u>2021E</u>
Business model- platform based									
BABA US	Alibaba	721,128	US\$ 266.9	9.1	6.8	5.3	32.9	28.0	22.1
3690 HK	Meituan-B	267,407	HK\$ 402.8	20.0	17.1	11.6	419.2	347.1	118.8
PDD US	Pinduoduo-A	126,972	US\$ 197.2	49.2	28.5	16.1	NA	NA	248.2
Business model – direct sales									
JD US	JD.com	149,746	US\$ 94.6	1.6	1.4	1.1	84.9	72.7	48.7
VIPS US	VIP Shop -A	19,913	US\$ 33.5	1.6	1.5	1.3	29.6	22.9	17.9

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

# All-share market cap for Alibaba and JD

Source(s): Bloomberg, ABCI Securities estimates



## Financial forecast

### Consolidated income statement (2018A-2021E)

FY Ended Dec 31 (RMB mn)	2018A	2019A	2020E	2021E
Net product revenue	416,109	510,734	649,287	784,906
Net service revenue	45,911	66,154	87,601	111,374
<b>Total revenue</b>	<b>462,019</b>	<b>576,888</b>	<b>736,888</b>	<b>896,280</b>
Cost of sales	(396,066)	(492,467)	(623,429)	(758,272)
<b>Gross profit</b>	<b>65,953</b>	<b>84,421</b>	<b>113,459</b>	<b>138,008</b>
Fulfillment expenses	(32,010)	(36,968)	(46,895)	(55,131)
Marketing expenses	(19,237)	(22,234)	(26,911)	(32,695)
Technology & content expenses	(12,144)	(14,619)	(15,311)	(18,451)
General & admin expenses	(5,182)	(5,490)	(5,136)	(4,942)
Gains on disposal	0	3,885	0	0
<b>Operating Profits</b>	<b>(2,619)</b>	<b>8,995</b>	<b>19,207</b>	<b>26,788</b>
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
<b>PBT</b>	<b>(2,374)</b>	<b>13,693</b>	<b>18,457</b>	<b>26,038</b>
Tax	(427)	(1,802)	(2,983)	(4,471)
<b>PAT</b>	<b>(2,801)</b>	<b>11,890</b>	<b>15,474</b>	<b>21,567</b>
Minority interests	(309)	(293)	(250)	(250)
<b>Profits attributable to shareholders</b>	<b>(2,492)</b>	<b>12,184</b>	<b>15,724</b>	<b>21,817</b>
Share-based compensation	3,660	3,695	2,163	1,893
Amortization	1,806	885	1,474	1,793
Impairment/FV changes of investments	808	(745)	0	0
Other non-core items	(321)	(5,269)	(555)	(805)
<b>Non-GAAP profits attributable to shareholders</b>	<b>3,460</b>	<b>10,750</b>	<b>18,806</b>	<b>24,698</b>
<b>Growth</b>				
Total revenue (%)	27.5	24.9	27.7	21.6
Gross Profits (%)	29.8	28.0	34.4	21.6
Operating Profits (%)	213.8	NA	113.5	39.5
Net profit (%)	NA	NA	29.1	38.8
Non-GAAP net profit (%)	(30.4)	210.7	74.9	31.3
<b>Operating performance</b>				
Operating margin (%)	(0.6)	1.6	2.6	3.0
Net margin (%)	(0.5)	2.1	2.1	2.4
Core net margin (%)	0.7	1.9	2.6	2.8
ROAE (%)	(4.4)	16.7	16.7	18.7
ROAA (%)	(1.3)	5.2	5.4	6.3

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
<b>Total non-current assets</b>	<b>104,309</b>	<b>120,629</b>	<b>140,029</b>	<b>159,429</b>
Cash & equivalents	37,502	39,912	47,751	60,832
Short-term investments and investment securities	2,036	24,603	24,603	24,603
Inventories	44,030	57,932	70,654	85,936
Account receivables	11,110	6,191	28,264	34,378
Other current assets	10,178	10,457	10,457	10,457
<b>Total current assets</b>	<b>104,855</b>	<b>139,094</b>	<b>181,729</b>	<b>216,205</b>
<b>Total assets</b>	<b>209,164</b>	<b>259,723</b>	<b>321,758</b>	<b>375,634</b>
Account payables	93,003	106,507	149,305	178,121
Borrowings and notes	4,545	0	0	0
Other current liabilities	23,314	33,510	33,510	33,510
<b>Total current liabilities</b>	<b>120,862</b>	<b>140,017</b>	<b>182,815</b>	<b>211,630</b>
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
<b>Total non-current liabilities</b>	<b>11,474</b>	<b>19,082</b>	<b>19,082</b>	<b>19,082</b>
<b>Total liabilities</b>	<b>132,336</b>	<b>159,099</b>	<b>201,897</b>	<b>230,712</b>
<b>Mezzanine equity</b>	<b>15,961</b>	<b>15,964</b>	<b>15,961</b>	<b>15,961</b>
Equity attributable to shareholders	59,771	81,856	101,343	126,653
Non-controlling interests	1,096	2,804	2,554	2,304
<b>Total equity</b>	<b>60,866</b>	<b>84,660</b>	<b>103,896</b>	<b>128,957</b>

Note. 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
<b>Operating cash flow</b>	<b>20,881</b>	<b>24,782</b>	<b>32,839</b>	<b>38,080</b>
<b>Investing cash flow</b>	<b>(26,078)</b>	<b>(25,349)</b>	<b>(25,000)</b>	<b>(25,000)</b>
<b>Financing cash flow</b>	<b>11,220</b>	<b>2,573</b>	<b>0</b>	<b>0</b>
Effective of FX	1,681	405	0	0
<b>Net cash flows</b>	<b>7,704</b>	<b>2,410</b>	<b>7,839</b>	<b>13,080</b>

Note. 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



## Meituan Dianping-W (3690 HK)

### Leading consumer service ecommerce platform

- Intact medium-term outlook to benefit from the structural uptrend in consumer service ecommerce
- Improving business environment for food delivery services
- In-store, hotel and travel segment turned around in 3Q20.
- Maintain **BUY** with a revised TP of HK\$ 480

**Leading consumer service ecommerce platform.** We believe Meituan (MD) is well-positioned to benefit from the structural uptrend of consumer upgrade from physical goods to services given its leading position in the consumer service ecommerce market. As China's largest online food delivery platform, MD has become a household brand in the country with a substantial user base with 477mn annual transaction users in 3Q20. In 2019, the Group generated RMB 393bn, 39% YoY, in gross transaction value (GTV) from food delivery.

**3Q20 review.** Meituan's 3Q20 results illustrate an improving operating environment, especially for the food delivery business. In addition, the in-store, hotel and travel segment resumed revenue growth. 3Q20 revenue grew by 29% YoY to RMB 35.4bn, indicating a sequential improvement vs. the 8.9% YoY revenue growth in 2Q20. Core net profit grew by 5.8% YoY to RMB 2.1bn in 3Q20.

**Business outlook.** We expect food delivery GTV growth to slow to 27% YoY in 2020E due to the pandemic before rebounding by 51% in 2021E on low base and normalized business. Similarly, we expect revenue to slow to 18% YoY in 2020E before leaping by 47% YoY in 2021E.

**Maintain BUY.** We maintain our **BUY** call on the counter with a revised DCF-based TP of HK\$ 480.

#### Results and Valuation

FY end Dec 31	2018A	2019A	2020E	2021E
Revenue (RMB mn)	65,227	97,528	115,152	169,555
Chg (% YoY)	92.3	49.5	18.1	47.2
Net profit (RMB mn)	-115,477	2,239	3,122	12,600
Chg (% YoY)	NA	NA	NA	303.6
Core net profit (RMB mn)*	-8,346	4,657	5,672	16,568
Chg (% YoY)	NA	NA	21.8	192.1
Underlying EPS (RMB)	-42.41	0.39	0.54	2.17
Chg (% YoY)	NA	NA	38.3	303.6
Core EPS (RMB)*	-3.06	0.81	0.98	2.85
Chg (% YoY)	NA	NA	20.8	192.1
P/S (x)	14.1	20.0	17.1	11.6
Core P/E (x)*	NA	419.2	347.1	118.8
ROAE (%)	NA	2.5	3.3	12.4
ROAA (%)	NA	1.8	2.3	8.7

\*Excl. share-based compensation, amortization, impairment, etc.

Source(s): Bloomberg, ABCI Securities estimates

## Company Report

Rating: **BUY**  
TP: HK\$480

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

Share price (HK\$)	409
Est. share price return	17.4%
Est. dividend yield	NA
Est. total return	17.4%
Previous Rating & TP	BUY/HK\$330
Previous Report Date	Oct 8, 2020

Source(s): Bloomberg, ABCI Securities estimates

#### Key Data

52Wk H/L(HK\$)	280.0/70.1
Issued shares (mn)	5,881
of which:	
Listed B shares (mm)	5,145
Unlisted shares (mm)	736
B share market cap (HK\$ mn)	2,405,125
Avg daily turnover (HK\$ mn)	7,883
Major shareholder(s)	Voting right
Wang Xing	49.1%
Mu Rongjun	10.8%

Source(s): Bloomberg, HKEX, Company



## Financial analysis

We expect food delivery GTV growth to slow to 27% YoY in 2020E due to the COVID-19 outbreak, to be followed by a 51% growth in 2021E due to the low base expected for 2020E and normalized business situation in 2021E.

### Exhibit 28: Major assumptions

	2018	2019	2020E	2021E
Annual transacting users (mn)	400	451	496	535
No. of food delivery transactions (mn)	6,393	8,722	10,030	13,541
No. of domestic hotel room nights (mn)	284	392	354	503

Source(s): the Company, ABCI Securities estimates

We expect MD's revenue growth to slow to 18.1% YoY for 2020E before accelerating to 47.2% YoY for 2021E. Among major business segments, we expect food delivery revenue to increase by 27% YoY in 2020E, to be followed by a 51% YoY growth for 2021E. For the in-store, hotel and travel segment, we factor in a 10% revenue decline for 2020E, to be followed by a 49% growth for 2021E.

### Exhibit 29: GTV and revenue forecasts

	2018	2019	2020E	2021E
<b>Food delivery gross transaction volume (RMB bn)</b>	<b>283</b>	<b>393</b>	<b>497</b>	<b>751</b>
<b>Revenue (RMB mn)</b>	<b>65,227</b>	<b>97,528</b>	<b>115,152</b>	<b>169,555</b>
Food delivery	38,143	54,843	69,547	105,155
In-store, hotel and travel	15,840	22,275	20,092	29,958
New initiatives and others	11,244	20,410	25,512	34,442

Source(s): Company, ABCI Securities estimates

Overall gross margin improved to 33.1% in 2019 vs. 23.2% in 2018, mainly driven by improving profitability of the food delivery and the new initiatives segments. Looking forward, we expect gross margin to drop to 30.5% for 2020E amid weakened consumption sentiment before recovering to 31.0% for 2021E.

In terms of operating cost, we expect SG&A/revenue ratio to drop to 24.0% by 2021E vs. 32.4% in 2019 thanks to improving economy of scale and ongoing cost control.



**Exhibit 30: SG &A forecasts**

	2018	2019	2020E	2021E
Selling & marketing expenses	15,872	18,819	20,727	25,433
R&D	7,072	8,446	9,212	10,173
General & admin expenses	5,546	4,339	4,606	5,087
<b>Total SG&amp;A</b>	<b>28,490</b>	<b>31,604</b>	<b>34,546</b>	<b>40,693</b>
<b>% of revenue</b>				
Selling & marketing expenses	24.3%	19.3%	18.0%	15.0%
R&D	10.8%	8.7%	8.0%	6.0%
General & admin expenses	8.5%	4.4%	4.0%	3.0%
<b>Total SG&amp;A</b>	<b>43.7%</b>	<b>32.4%</b>	<b>30.0%</b>	<b>24.0%</b>

Source(s): Company, ABCI Securities estimates

Based on the above assumptions, we expect core net profit to reach RMB16.6bn in 2021E vs. RMB4.6bn in 2019, with core net margin improving to 9.8% in 2021E vs. 4.8% in 2019.

**Exhibit 31: Forecast changes in 2020E**

(RMB m)	2020E		Diff	Comment
	old	new		
Revenues	111,164	115,152	4%	
Net income	2,938	3,122	6%	
Core profit	4,647	5,672	22%	Economies of scale

Source(s): ABCI Securities estimates

**Exhibit 32: Forecast changes for 2021E**

(RMB m)	2021E		Diff.	Comment
	old	new		
Revenues	158,159	169,555	7%	Higher growth assumptions
Net income	13,721	12,600	(8%)	
Core profit	16,547	16,568	0%	

Source(s): ABCI Securities estimates



## Valuation and TP

We derive MD's valuation range based on the DCF approach with a WACC of 7%-10%. The DCF approach results in a valuation range of HK\$ 249-HK\$ 553. We set our TP at HK\$ 480, which warrants a **BUY** rating.

Overall, our valuation range implies a wide trading range. Any major new business development or initiatives could lead to a higher valuation (higher risk appetites among investors). Our TP indicates a medium-term target but we notice that short-term share price might deviate from it due to technical factors such as share supply/demand dynamics.

## Peer valuation analysis

Comparing with other major ecommerce platforms including Alibaba (BABA US/9988 HK) and JD (JD US/9618 HK), MD is trading at a higher valuation in terms of core P/E. In our view, this could be due to the fact that MD is still in early stage of profitability and investors tend to focus on its longer-term outlook.

Exhibit 33: Peer valuation

		Market cap# (USD mn)	Price (Lcy)	P/sales			Core P/E*			
				<u>2019</u>	<u>2020E</u>	<u>2021E</u>	<u>2019</u>	<u>2020E</u>	<u>2021E</u>	
Business model- platform based										
BABA US	Alibaba	721,128	US\$ 266.9	9.1	6.8	5.3	32.9	28.0	22.1	
3690 HK	Meituan-B	267,407	HK\$ 402.8	20.0	17.1	11.6	419.2	347.1	118.8	
PDD US	Pinduoduo-A	126,972	US\$ 197.2	49.2	28.5	16.1	NA	NA	248.2	
Business model – direct sales										
JD US	JD.com	149,746	US\$ 94.6	1.6	1.4	1.1	84.9	72.7	48.7	
VIPS US	VIP Shop -A	19,913	US\$ 33.5	1.6	1.5	1.3	29.6	22.9	17.9	

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

# All-share market cap for Alibaba and JD

Source(s): Bloomberg, ABCI Securities estimates

Exhibit 34: TP changes (HK\$ per share)

Segment	Old	New	Methodology -old	Methodology - new
Overall	330	480	DCF with a 9% WACC	DCF with a 7.5% WACC

Source(s): ABCI Securities estimates



農銀國際

ABC INTERNATIONAL

ABCI SECURITIES COMPANY LIMITED

Meituan Dianping-W (3690 HK) - BUY

China Ecommerce Sector

Feb 10, 2021

## Financial forecast

### Consolidated income statement (FY18A-FY21E)

FY Ended Dec 31 (RMB mn)	FY18A	FY19A	FY20E	FY21E
<b>Total revenue</b>	<b>65,227</b>	<b>97,528</b>	<b>115,152</b>	<b>169,555</b>
Cost of sales	(50,122)	(65,208)	(80,031)	(116,993)
<b>Gross profit</b>	<b>15,105</b>	<b>32,320</b>	<b>35,121</b>	<b>52,562</b>
Other gains/losses	2,585	2,609	2,850	2,850
Selling & marketing expenses	(15,872)	(18,819)	(20,727)	(25,433)
R&D expenses	(7,072)	(8,446)	(9,212)	(10,173)
General & admin expenses	(5,546)	(4,339)	(4,606)	(5,087)
Impairment	(286)	(646)	0	0
<b>Operating Profits</b>	<b>(11,086)</b>	<b>2,680</b>	<b>3,426</b>	<b>14,719</b>
Finance income, net	249	(25)	(50)	(20)
Other cost	(104,654)	107	90	110
<b>Profit before tax</b>	<b>(115,491)</b>	<b>2,762</b>	<b>3,466</b>	<b>14,809</b>
Tax	2	526	347	2,221
<b>Profit after tax</b>	<b>(115,493)</b>	<b>2,236</b>	<b>3,119</b>	<b>12,588</b>
Minority interests	(16)	(3)	(3)	(13)
<b>Profits attributable to shareholders</b>	<b>(115,477)</b>	<b>2,239</b>	<b>3,122</b>	<b>12,600</b>
Share-based compensation	1,865	2,191	2,303	3,730
Amortization and impairment	2,367	751	600	600
Adjustments on disposals/revaluation	102,743	(547)	(350)	(350)
Other adjustments	157	23	(3)	(13)
<b>Core profits</b>	<b>(8,346)</b>	<b>4,657</b>	<b>5,672</b>	<b>16,568</b>
<b>Growth</b>				
Total revenue (%)	92.3	49.5	18.1	47.2
Gross Profits (%)	23.6	114.0	8.7	49.7
Operating Profits (%)	189.7	NA	27.8	329.7
Net profit (%)	510.5	NA	39.5	303.6
Core profit (%)	192.6	NA	21.8	192.1
<b>Operating performance</b>				
Operating margin (%)	NA	2.7	3.0	8.7
Net margin (%)	NA	2.3	2.7	7.4
Core net margin (%)	NA	4.8	4.9	9.8
ROAE (%)	NA	2.5	3.3	12.4
ROAA (%)	NA	1.8	2.3	8.7

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

Source(s): Company, ABCI Securities estimates



**Consolidated balance sheet (FY18A-FY21E)**

As of Dec 31 (RMB mn)	FY18A	FY19A	FY20E	FY21E
Fixed assets	3,979	5,376	4,262	10,196
Intangible assets	33,876	32,700	32,700	32,700
Investment in associates and JV	2,103	2,284	2,284	2,284
Financial assets	6,242	7,166	7,166	7,166
Other non-current assets	1,312	2,352	2,352	2,352
<b>Total non-current assets</b>	<b>47,512</b>	<b>49,877</b>	<b>48,763</b>	<b>54,697</b>
Cash & equivalents	17,044	13,396	17,528	26,416
Restricted cash	4,256	8,760	8,760	8,760
Account receivables	466	677	2,414	4,020
Deposit, prepayments and other assets	9,065	9,591	9,591	9,591
Inventories	400	275	707	1,040
Short term investment	41,918	49,436	49,436	49,436
<b>Total current assets</b>	<b>73,149</b>	<b>82,135</b>	<b>88,436</b>	<b>99,262</b>
<b>Total assets</b>	<b>120,661</b>	<b>132,012</b>	<b>137,198</b>	<b>153,959</b>
Accounts payable	5,341	6,766	8,834	13,007
Borrowings and notes	1,800	3,553	3,553	3,553
Deferred revenue	3,103	4,567	4,567	4,567
Other current liabilities	21,581	21,706	21,706	21,706
<b>Total current liabilities</b>	<b>31,825</b>	<b>36,592</b>	<b>38,659</b>	<b>42,833</b>
Deferred revenue	625	389	389	389
Borrowings	470	467	467	467
Other non-current liabilities	1,232	2,510	2,510	2,510
<b>Total non-current liabilities</b>	<b>2,326</b>	<b>3,366</b>	<b>3,366</b>	<b>3,366</b>
<b>Total liabilities</b>	<b>34,151</b>	<b>39,958</b>	<b>42,025</b>	<b>46,199</b>
<b>Net current assets</b>	<b>41,324</b>	<b>45,542</b>	<b>49,776</b>	<b>56,429</b>
Equity attributable to shareholders	86,504	92,113	95,235	107,835
Non-controlling interests	5	(58)	(61)	(74)
<b>Total equity</b>	<b>86,510</b>	<b>92,055</b>	<b>95,174</b>	<b>107,761</b>

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

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

Source(s): Company, ABCI Securities estimates

**Consolidated Cash flows statement (FY18A-FY21E)**

As of Dec 31 (RMB mn)	FY18A	FY19A	FY20E	FY21E
Operating cash flow	(9,180)	7,112	8,162	14,822
Investing cash flow	(23,439)	(3,506)	(4,030)	(5,934)
Financing cash flow	29,295	-	-	-
<b>Net cash flows</b>	<b>(3,323)</b>	<b>3,606</b>	<b>4,132</b>	<b>8,887</b>

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

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

Source(s): Company, ABCI Securities estimates

## Pinduoduo (PDD US)

### Inflection point insight

- Emerging ecommerce platform with rapid growth on innovative social ecommerce features; 731mn users in 3Q20 vs. Alibaba's 757m
- Rationalizing marketing expenses leading to RMB466m core net profit in 3Q20, paving the way for a breakeven by 2021E
- Maintain **BUY** on emerging potential in lower-tier cities

**A rising star in lower-tier cities.** Pinduoduo is an emerging player with rapid growth in the ecommerce sector despite its relatively short operating history (since 2015). In our view, its rising popularity is driven by its innovative business model, which provides buyers with value-for-money products and interactive shopping experiences. Strong user growth was seen, with its active users reaching 731mn in 3Q20, nearing Alibaba's 757mn.

**Long-term investment on user loyalty.** Pinduoduo has been suffering from core net losses in recent years, mainly dragged by sales and marketing expenses that accounted for 2.7% of GMV in 2019 vs. 0.7% for Alibaba and 1.0% for JD. We view such expenses as a long-term investment on user loyalty and stickiness, and expect a breakeven to occur by 2021E based on the ongoing sales growth and improving margins enabled by better economies of scale and cost control.

**3Q20 review.** In 3Q20, revenue grew by 89% YoY (2Q20 growth: 67% YoY) to RMB14.2bn, indicating a significant sequential improvement amid improving macro environment. In addition, the company reported a net core profit of RMB 466m in 3Q20 driven by lower marketing expenses, paving the way for a breakeven by 2021E.

**Maintain BUY on potential in lower-tier regions.** We maintain **BUY** with a DCF-based TP of US\$ 230. We believe the Group is well-positioned to ride on the consumption growth in China's lower-tier cities.

#### Results and Valuation

FY end Dec 31	2018A	2019A	2020E	2021E
Revenue (RMB mn)	13,120	30,142	52,364	92,782
Chg (% YoY)	652.5	129.7	73.7	77.2
Net profit (RMB mn)	-10,297	-6,968	-6,341	-956
Chg (% YoY)	NA	NA	NA	NA
Core net profit (RMB mn)	-3,456	-4,266	-2,675	6,003
Chg (% YoY)	NA	NA	NA	NA
Earnings per ADS (RMB)	-13.9	-6.0	-5.5	-0.8
Chg (% YoY)	NA	NA	NA	NA
Core earnings per ADS (RMB)	-4.7	-3.7	-2.3	5.2
Chg (% YoY)	NA	NA	NA	NA
Core P/E (x)	NA	NA	NA	248.2
P/S (x)	72.5	49.2	28.5	16.1
ROAE (%)	NA	NA	NA	-3.8
ROAA (%)	NA	NA	NA	-1.0

1 ADS = 4 common shares

Source(s): Bloomberg, ABCI Securities estimates

## Company Report

Rating: **BUY**  
TP: US\$ 230

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

ADS price (US\$ )	189.7
Est. share price return	21.2%
Est. dividend yield	NA
Est. total return	21.2%
Previous Rating & TP	BUY/US\$113
Previous Report Date	Oct 8, 2020

Source(s): Bloomberg, ABCI Securities estimates

#### Key Data

52Wk H/L(US\$ )	99.0/30.2
Issued shares (mn)	4,650
of which:	
Listed A shares (mn)	2,576
Unlisted B shares (mn)	2,074
A share market cap (US\$ mn)	126,972
Avg daily turnover (US\$ mn)	1,560
Major shareholder(s)	Voting right
Zheng Huang	88.9%
Banyan Partners	1.7%

Source(s): Bloomberg, Company

## Financial analysis

For 2019-2021E, we expect GMV to grow by 62% CAGR to RMB 2.9tr by 2021E, driven by the growing number of active users and spending.

### Exhibit 35: Major assumptions

	2018	2019	2020E	2021E
Annual active customer account (mn)	419	585	761	913
GMV (RMB bn)	472	1,007	1,636	2,651
Annual spending per active customer (RMB)	1,127	1,721	2,151	2,904
Monetization rate	2.8%	3.0%	3.2%	3.5%

Source(s): the Group, ABCI Securities estimates

Overall, we expect revenue to increase at 75% CAGR in 2019-21E to RMB 92.8bn by 2021E, propelled by growing GMV and an improving monetization rate from 3.0% in 2019 to 3.5% in 2021E on value-added services provided to merchants.

### Exhibit 36: Revenue forecasts (RMB mn)

	2018	2019	2020E	2021E
Online marketplace services	11,516	26,814	47,128	84,432
Transaction services	1,604	3,328	5,236	8,350
<b>Total revenue</b>	<b>13,120</b>	<b>30,142</b>	<b>52,364</b>	<b>92,782</b>

Source(s): the Group, ABCI Securities estimates

Gross margin trended up to 79.0% in 2019 vs. 58.5% in 2017, driven by economies of scale and improving efficiency of online marketplace. We expect such improvement to continue with gross margin reaching 81.9% by 2021E.

**Sales and marketing expenses:** Non-GAAP sales and marketing expenses have been the biggest cost item, accounting for 87.3% of revenue in 2019. Such ratio has been declining from the peak of 99.4% in 2018 because less promotion and subsidies are required as customer loyalty increases; also, bargaining power over merchants improves as the Group's operation scale grows. We expect non-GAAP sales and marketing expenses/revenue ratio to improve to 68.0% by 2021E.

**General & admin expenses:** We expect non-GAAP G&A expense/sales ratio to improve to 1.0% for 2021E vs. 1.7% in 2019, driven by improving economies of scale.

**R&D expenses:** Non-GAAP R&D expenses /sales ratio was 9.9% in 2019. We expect this ratio to improve in 2020E-21E on economies of scale and reach 7.5% in 2021E.





**Exhibit 37: Non-GAAP cost trend (RMB mn)**

	2018	2019	2020E	2021E
Cost of revenue	2,902	6,315	9,687	16,701
Sales and marketing	13,036	26,313	40,844	63,092
General and admin	160	510	785	928
R&D	980	2,984	4,713	6,959
<b>Total</b>	<b>17,078</b>	<b>36,123</b>	<b>56,029</b>	<b>87,679</b>
<b>% of revenue</b>				
Cost of revenue	22.1%	21.0%	18.5%	18.0%
Sales and marketing	99.4%	87.3%	78.0%	68.0%
General and admin	1.2%	1.7%	1.5%	1.0%
R&D	7.5%	9.9%	9.0%	7.5%
<b>Total</b>	<b>130.2%</b>	<b>119.8%</b>	<b>107.0%</b>	<b>94.5%</b>

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 declining cost trends, we estimate the Group would reach the breakeven point by 2021E with a core net profit of RMB 6.0bn, implying a core net margin of 6.5% in 2021E vs. -14.2% in 2019. Nonetheless, our forecasts are subject to revision with reference to quarterly earnings.

**Exhibit 38: Forecast changes in 2020E**

(RMB m)	2020E		Diff	Comment
	old	new		
Revenues	46,403	52,364	13%	Higher growth assumptions
Core profit	(3,654)	(2,675)	NA	

Source(s): ABCI Securities estimates

**Exhibit 39: Forecast changes for 2021E**

(RMB m)	2021E		Diff	Comment
	old	new		
Revenues	75,368	92,782	23%	Higher growth assumptions
Core profit	5,872	6,003	2%	

Source(s): ABCI Securities estimates

## Maintain BUY

Our DCF-based valuation range is US\$ 142- US\$ 311 per share based on a WACC of 10%-7%. We set our TP to US\$ 230.

Overall, our valuation range implies a wide trading range. Any major new business development or initiatives could lead to a higher valuation (higher risk appetites among investors). Our TP indicates a medium-term target but we notice that short-term share price might deviate from it due to technical factors such as share supply/demand dynamics.

## Peer valuation analysis

Pinduoduo's peers are China's major online ecommerce platforms, including Alibaba (BABA US/9988 HK) and JD (JD US/HK).

Pinduoduo is currently trading at a higher P/E than Alibaba and JD; however, P/E is not the best valuation metric for the Group since it is still in the early stage of profitability. Pinduoduo is trading at a higher P/S than Alibaba, reflecting the higher GMV growth expected for the Group.

### Exhibit 40: Peer valuation

Exhibit 46: Peer valuation

		Market cap# (USD mn)	Price (Lcy)	P/sales			Core P/E*		
				<u>2019</u>	<u>2020E</u>	<u>2021E</u>	<u>2019</u>	<u>2020E</u>	<u>2021E</u>
Business model- platform based									
BABA US	Alibaba	721,128	US\$ 266.9	9.1	6.8	5.3	32.9	28.0	22.1
3690 HK	Meituan-B	267,407	HK\$ 402.8	20.0	17.1	11.6	419.2	347.1	118.8
PDD US	Pinduoduo-A	126,972	US\$ 197.2	49.2	28.5	16.1	NA	NA	248.2
Business model – direct sales									
JD US	JD.com	149,746	US\$ 94.6	1.6	1.4	1.1	84.9	72.7	48.7
VIPS US	VIP Shop -A	19,913	US\$ 33.5	1.6	1.5	1.3	29.6	22.9	17.9

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

# All-share market cap for Alibaba and JD

Source(s): Bloomberg, ABCI Securities estimates

### Exhibit 41: TP changes (US\$ per share)

Old	New	Methodology- old	Methodology -new
113	230	DCF	DCF with revised revenue growth assumptions

Source(s): ABCI Securities estimates



農銀國際

ABC INTERNATIONAL

ABCI SECURITIES COMPANY LIMITED

Pinduoduo (PDD US) - BUY

China Ecommerce Sector

Feb 10, 2021

## Financial forecast

### Consolidated income statement (2018A-2021E)

FY Ended Dec 31 (RMB mn)	2018A	2019A	2020E	2021E
<b>Total revenue</b>	<b>13,120</b>	<b>30,142</b>	<b>52,364</b>	<b>92,782</b>
Cost of sales	(2,905)	(6,339)	(9,721)	(16,766)
<b>Gross profit</b>	<b>10,215</b>	<b>23,803</b>	<b>42,643</b>	<b>76,017</b>
Sales and marketing	(13,442)	(27,174)	(42,078)	(65,434)
General and admin	(6,456)	(1,297)	(1,913)	(3,068)
R&D	(1,116)	(3,870)	(5,983)	(9,370)
<b>Operating Profits</b>	<b>(10,799)</b>	<b>(8,538)</b>	<b>(7,331)</b>	<b>(1,856)</b>
Interest income	585	1,542	1,450	1,350
Interest expenses	0	(146)	(600)	(600)
Fx gain	10	63	100	100
Others, net	(12)	83	0	0
Share of results of investee	0	29	40	50
<b>PBT</b>	<b>(10,217)</b>	<b>(6,968)</b>	<b>(6,341)</b>	<b>(956)</b>
Tax	0	0	0	0
<b>PAT</b>	<b>(10,217)</b>	<b>(6,968)</b>	<b>(6,341)</b>	<b>(956)</b>
Minority interests/distribution to convertible preferred shareholders	(81)	0	0	0
<b>Profits attributable to shareholders</b>	<b>(10,297)</b>	<b>(6,968)</b>	<b>(6,341)</b>	<b>(956)</b>
Share-based compensation	6,841	2,558	3,665	6,959
Interest related to CB amortization	0	144	0	0
Other non-core items	0	0	0	0
<b>Non-GAAP profits attributable to shareholders</b>	<b>(3,456)</b>	<b>(4,266)</b>	<b>(2,675)</b>	<b>6,003</b>
<b>Growth</b>				
Total revenue (%)	652.5	129.7	73.7	77.2
Gross Profits (%)	900.8	133.0	79.1	78.3
Operating Profits (%)	NA	NA	NA	NA
Net profit (%)	NA	NA	NA	NA
Non-GAAP net profit (%)	NA	NA	NA	NA
<b>Operating performance</b>				
Operating margin (%)	(82.3)	(28.3)	(14.0)	(2.0)
Net margin (%)	(78.5)	(23.1)	(12.1)	(1.0)
Core net margin (%)	(26.3)	(14.2)	(5.1)	6.5
ROAE (%)	NA	NA	NA	(3.8)
ROAA (%)	NA	NA	NA	(1.0)

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	29	41	91	141
Intangible asset	2,579	1,994	1,994	1,994
Other non-current assets	183	1,020	1,045	1,072
<b>Total non-current assets</b>	<b>2,791</b>	<b>3,056</b>	<b>3,131</b>	<b>3,207</b>
Cash & equivalents	14,160	5,768	21,772	37,321
Restricted cash	16,379	27,578	30,335	33,369
Short-term investments and investment securities	7,631	35,289	29,996	26,996
Account receivables	248	1,051	1,104	1,159
Other current assets	1,973	3,315	3,363	3,413
<b>Total current assets</b>	<b>40,391</b>	<b>73,001</b>	<b>86,570</b>	<b>102,257</b>
<b>Total assets</b>	<b>43,182</b>	<b>76,057</b>	<b>89,700</b>	<b>105,465</b>
Account payables	670	2,109	2,184	2,263
Payable to merchants	17,276	29,927	41,805	45,349
Merchant deposit	4,188	7,841	11,706	17,345
Borrowings and notes	0	899	1,399	1,899
Other current liabilities	2,225	4,993	4,993	4,993
<b>Total current liabilities</b>	<b>24,359</b>	<b>45,768</b>	<b>62,087</b>	<b>71,848</b>
Convertible bonds	-	5,207	5,207	5,207
Other non-current liabilities	-	436	436	436
<b>Total non-current liabilities</b>	<b>-</b>	<b>5,642</b>	<b>5,642</b>	<b>5,642</b>
<b>Total liabilities</b>	<b>24,359</b>	<b>51,410</b>	<b>67,729</b>	<b>77,490</b>
Equity attributable to shareholders	18,823	24,647	21,971	27,974
Non-controlling interests	-	-	-	-
<b>Total equity</b>	<b>18,823</b>	<b>24,647</b>	<b>21,971</b>	<b>27,974</b>

Note. 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
<b>Operating cash flow</b>	<b>7,768</b>	<b>14,821</b>	<b>16,104</b>	<b>15,699</b>
<b>Investing cash flow</b>	<b>(7,549)</b>	<b>(28,320)</b>	<b>(600)</b>	<b>(650)</b>
<b>Financing cash flow</b>	<b>17,344</b>	<b>15,855</b>	<b>500</b>	<b>500</b>
Effective of FX	547	450	-	-
<b>Net cash flows</b>	<b>18,111</b>	<b>2,806</b>	<b>16,004</b>	<b>15,549</b>

Note. 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

## VIPSHOP (VIPS US)

### Niche player in discount online retailing

- A niche online ecommerce platform in China focusing on discount online retailing
- Strategic move to refocus on the core discount retailing market and operating improvement resulted in better margins
- Maintain **BUY** with revised TP of US\$ 40 on potential margin improvement

**A niche player focusing on discounted online retailing.** VIPSHOP (VIPS) is a niche online ecommerce platform in China focusing on discount online retailing. Unlike other online retail platforms offering a wide range of merchandises to customers, VIPS specializes in flash sales of discounted branded products, resembling the outlet format in traditional offline retailing. The Group has earned a strong reputation in this niche segment with 69mn active customers at end-2019.

**Counter-cyclical nature.** In our view, the Group's business model offers some degree of counter cyclicity. During the economic downturn, brand owners typically choose to clear its inventories via heavy discounts to VIPS. This allows VIPS to lower purchase cost and offers a deeper discount to customers, which enhances overall customer engagement and loyalty.

**3Q20 results review.** In 3Q20, revenue growth accelerated to 18% YoY vs. 6% YoY in 2Q20, driven by 36% YoY growth in active customers. In addition, core net profit grew by 15% YoY with core net margin improving to 6.0% in 3Q20 vs. 5.5% in 2Q10. In addition, gross margin improved to 21.1% in 3Q20 vs. 20.5% in 2Q20.

**Maintain BUY.** We maintain **BUY** with a revised DCF-based TP of US\$ 40 to reflect its solid market position in the discount online retailing market and ongoing margin improvement.

#### Results and Valuation

FY end Dec 31	2018A	2019A	2020E	2021E
Revenue (RMB mn)	84,524	92,994	96,186	116,144
Chg (% YoY)	15.9	10.0	3.4	20.8
Net profit (RMB mn)	2,129	4,017	5,509	7,111
Chg (% YoY)	9.2	88.7	37.2	29.1
Core net profit (RMB mn)	2,719	5,013	6,471	8,273
Chg (% YoY)	(6.9)	84.4	29.1	27.8
Earnings per ADS (RMB)	3.1	5.9	8.1	10.5
Chg (% YoY)	11.3	90.5	37.2	29.1
Core earnings per ADS (RMB)	3.9	7.4	9.5	12.2
Chg (% YoY)	(6.9)	89.8	29.1	27.8
Core P/E (x)	56.2	29.6	22.9	17.9
ROAE (%)	24.7	20.4	21.6	21.6
ROAA (%)	9.8	8.7	10.8	11.6

1 common shares = 5 ADS

Source(s): Bloomberg, ABCI Securities estimates

## Company Report

Rating: **BUY**  
TP: US\$40

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

ADS price (US\$ )	33.8
Est. share price return	18.3%
Est. dividend yield	NA
Est. total return	18.3%
Previous Rating & TP	BUY, US\$ 22
Previous Report Date	Oct 8, 2020

Source(s): Bloomberg, ABCI Securities estimates

#### Key Data

52Wk H/L(US\$ )	24.5/8.6
Issued shares (mn)	135.1
of which:	
Listed A shares (mn)	118.6
Unlisted B shares(mn)	16.5
A share market cap (US\$ mn)	19,913
Avg daily turnover (US\$ mn)	235
Major shareholder(s)	
Eric Ya Shen	12.7%

Source(s): Bloomberg, Company



## Financial analysis

For 2019-21E, we expect GMV to grow by 12% CAGR to RMB 184bn by 2021E, driven by the growing number of active users.

**Annual active customer:** the Company had 69mn annual active customers at end-2019, up 14% YoY. Looking forward, we expect the figure to reach 81mn by 2021E.

**Annual spending per active customer:** Annual spending per active customer has been largely stable at about RMB 2.1K in recent years. We expect this trend to continue going forward.

Based on the above assumptions, we expect revenue to increase by 3%/21% YoY growth in 2020E/21E. With improving gross margins and cost trends, we expect core net profit to reach RMB8.3bn by 2021E vs. RMB5.0bn for 2019.

### Exhibit 42: Major assumptions

	2018	2019	2020E	2021E
Active customer (mn)	61	69	70	81
GMV (RMB bn)	131	148	153	184
Annual spending per active customer (RMB)	2,165	2,148	2,169	2,278

Source(s): the Company, ABCI Securities estimates

### Exhibit 43: Revenue forecasts (RMB mn)

	2018	2019	2020E	2021E
Product revenue	81,510	88,721	91,766	110,807
Other revenue	3,014	4,273	4,420	5,337
Total revenue	84,524	92,994	96,186	116,144

Source(s): The Company, ABCI Securities estimates

### Exhibit 44: Non-GAAP cost trend (RMB mn)

	2018	2019	2020E	2021E
Fulfillment	7,416	7,205	6,925	8,246
Marketing	3,200	3,289	2,982	3,484
Technology and content	1,798	1,388	1,154	1,394
General and admin	2,321	3,704	3,366	3,484
Total	14,734	15,586	14,428	16,609
<b>% of revenue</b>				
Fulfillment	8.8%	7.7%	7.2%	7.1%
Marketing	3.8%	3.5%	3.1%	3.0%
Technology and content	2.1%	1.5%	1.2%	1.2%
General and admin	2.7%	4.0%	3.5%	3.0%
Total	17.4%	16.8%	15.0%	14.3%

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

Source(s): The Company, ABCI Securities estimates



## Maintain BUY

We maintain **BUY** on the counter with a revised DCF-based TP of US\$ 40.

Our DCF-based valuation range is US\$ 29- US\$ 49 per ADS, based on a WACC of 14%-10% WACC. We set our TP at US\$ 40.

Overall, our valuation range implies a wide trading range. Any major new business development or initiatives could lead to a higher valuation (higher risk appetites among investors). Our TP indicates a medium-term target but we notice that short-term share price might deviate from it due to technical factors such as share supply/demand dynamics.

## Peer valuation analysis

VIPS's peers are major online ecommerce platforms, including Alibaba (BABA US, 9988 HK) and Pinduoduo (PDD US). Overall, it is trading at discounts to peers on a core P/E basis. We believe this is due to its smaller operation and narrower product selection. Nonetheless, its undemanding valuation could imply potential re-rating in the medium term given the Group's ongoing margin expansion.

### Exhibit 45: Peer valuation

Exhibit 10.1 CCF Validation

		Market cap# (USD mn)	Price (Lcy)	P/sales			Core P/E*		
				<u>2019</u>	<u>2020E</u>	<u>2021E</u>	<u>2019</u>	<u>2020E</u>	<u>2021E</u>
Business model- platform based									
BABA US	Alibaba	721,128	US\$ 266.9	9.1	6.8	5.3	32.9	28.0	22.1
3690 HK	Meituan-B	267,407	HK\$ 402.8	20.0	17.1	11.6	419.2	347.1	118.8
PDD US	Pinduoduo-A	126,972	US\$ 197.2	49.2	28.5	16.1	NA	NA	248.2
Business model – direct sales									
JD US	JD.com	149,746	US\$ 94.6	1.6	1.4	1.1	84.9	72.7	48.7
VIPS US	VIP Shop -A	19,913	US\$ 33.5	1.6	1.5	1.3	29.6	22.9	17.9

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

# All-share market cap for Alibaba and JD

Source(s): Bloomberg, ABCI Securities estimates

### Exhibit 46: TP changes (US\$ per share)

Old	New	Methodology -old	Methodology -new
22	40	DCF: 13% WACC	DCF: 10.5% WACC

Source(s): ABCI Securities estimates



## Financial forecast

### Consolidated income statement (2018A-2021E)

FY Ended Dec 31 (RMB mn)	2018A	2019A	2020E	2021E
<b>Total revenue</b>	<b>84,524</b>	<b>92,994</b>	<b>96,186</b>	<b>116,144</b>
Cost of sales	(67,455)	(72,314)	(75,025)	(90,592)
<b>Gross profit</b>	<b>17,069</b>	<b>20,680</b>	<b>21,161</b>	<b>25,552</b>
Fulfillment	(7,489)	(7,318)	(7,083)	(8,436)
Marketing	(3,241)	(3,324)	(3,031)	(3,543)
R&D	(2,001)	(1,568)	(1,407)	(1,698)
General and admin	(2,674)	(4,064)	(3,870)	(4,092)
Others, net	757	367	667	805
<b>Operating Profits</b>	<b>2,421</b>	<b>4,773</b>	<b>6,438</b>	<b>8,587</b>
Interest income	243	217	220	230
Interest expenses	(160)	(86)	(70)	(75)
Investment and FX gain	243	38	50	50
Share of results of investee	(47)	27	30	30
<b>PBT</b>	<b>2,700</b>	<b>4,970</b>	<b>6,668</b>	<b>8,822</b>
Tax	(566)	(984)	(1,200)	(1,764)
<b>PAT</b>	<b>2,133</b>	<b>3,986</b>	<b>5,468</b>	<b>7,057</b>
Minority interests	(5)	30	42	54
<b>Net income</b>	<b>2,129</b>	<b>4,017</b>	<b>5,509</b>	<b>7,111</b>
Share-based compensation	671	688	962	1,161
Other non-core items	(81)	308	0	0
<b>Core net income</b>	<b>2,719</b>	<b>5,013</b>	<b>6,471</b>	<b>8,273</b>
<b>Growth</b>				
Total revenue (%)	15.9	10.0	3.4	20.8
Gross Profits (%)	4.8	21.2	2.3	20.8
Operating Profits (%)	(10.0)	97.1	34.9	33.4
Net profit (%)	9.2	88.7	37.2	29.1
Core net profit (%)	(6.9)	84.4	29.1	27.8
<b>Operating performance</b>				
Operating margin (%)	2.9	5.1	6.7	7.4
Net margin (%)	2.5	4.3	5.7	6.1
Core net margin (%)	3.2	5.4	6.7	7.1
ROAE (%)	24.7	20.4	21.6	21.6
ROAA (%)	9.8	8.7	10.8	11.6

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

Source(s): The Company, ABCI Securities estimates





Consolidated balance sheet (2018A-2021E)

As of Dec 31 (RMB mn)	2018A	2019A	2020E	2021E
Fixed assets	12,593	16,899	20,999	25,099
Investments	2,139	5,116	5,116	5,116
Other non-current assets	1,505	3,539	3,539	3,539
<b>Total non-current assets</b>	<b>16,237</b>	<b>25,554</b>	<b>29,654</b>	<b>33,754</b>
Cash & equivalents	9,540	6,574	9,496	15,757
Restricted cash	498	1,146	1,146	1,146
Short-term investments	2,321	3,053	3,053	3,053
Account receivables	5,675	1,296	1,296	1,296
Inventories	5,368	7,708	5,763	10,503
Other current assets	3,923	3,252	3,252	3,252
<b>Total current assets</b>	<b>27,325</b>	<b>23,029</b>	<b>24,006</b>	<b>35,007</b>
<b>Total assets</b>	<b>43,562</b>	<b>48,583</b>	<b>53,660</b>	<b>68,761</b>
Advance from customer	1,473	1,233	1,233	1,233
Account payables	11,630	13,792	12,398	19,226
Borrowings and notes	6,639	1,094	1,094	1,094
Other current liabilities	6,203	7,807	7,807	7,807
<b>Total current liabilities</b>	<b>25,945</b>	<b>23,926</b>	<b>22,532</b>	<b>29,360</b>
Long term debt	-	65	65	65
Other non-current liabilities	406	2,343	2,343	2,343
<b>Total non-current liabilities</b>	<b>406</b>	<b>2,407</b>	<b>2,407</b>	<b>2,407</b>
<b>Total liabilities</b>	<b>26,351</b>	<b>26,333</b>	<b>24,939</b>	<b>31,767</b>
Equity attributable to shareholders	17,262	21,827	28,257	36,475
Non-controlling interests	(51)	423	464	518
<b>Total equity</b>	<b>17,211</b>	<b>22,250</b>	<b>28,721</b>	<b>36,993</b>

Note. 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 Company, ABCI Securities estimates

Consolidated cash flow statement (2018A-2021E)

As of Dec 31 (RMB mn)	2018A	2019A	2020E	2021E
<b>Operating cash flow</b>	<b>5,746</b>	<b>12,290</b>	<b>7,922</b>	<b>11,261</b>
<b>Investing cash flow</b>	<b>(6,694)</b>	<b>(8,240)</b>	<b>(5,000)</b>	<b>(5,000)</b>
<b>Financing cash flow</b>	<b>587</b>	<b>(6,257)</b>	<b>-</b>	<b>-</b>
FX effect	178	(112)	-	-
<b>Net cash flows</b>	<b>(184)</b>	<b>(2,319)</b>	<b>2,922</b>	<b>6,261</b>

Note. 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 Company, ABCI Securities estimates



## Risk factors

### Loss-making business

Selected ecommerce platform such as Pinduoduo reported net losses in recent years. The current business model may not be sustainable in the long run without a turnaround in coming years. In such case, our forecast and valuation method cannot be justified. The counter may not be suitable to prudent investors who prefer companies with a proven profitable record.

### Market competition

The ecommerce industry is a competitive one. 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 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

### Analyst Certification

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.

### Disclosures of Interests

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

### Definition of equity rating

Rating	Definition
Buy	Stock return rate $\geq$ Market return rate (10%)
Hold	- Market return rate (-10%) $\leq$ 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(For reference: HSI total return index 2008-20CAGR 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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