農銀國際
ABC INTERNATIONAL
ABCI SECURITIES COMPANY LIMITED

China Internet Sector

The Art of Cherry Picking

Mar 7, 2024

China Internet Sector

The Art of Cherry Picking

Sector Report

Mar 7, 2024

- We see a divergent operating environment within sub-segments in the internet space
- Wide valuation range and diversified sub-segment outlook has led us to adopt a valuation-based stock selection strategy
- In our view, sector valuations have turned reasonable. Our sector preferred picks include Pinduoduo (PDD US), Alibaba (9988 HK/ BABA US), NetEase (9999 HK/NTES US), and Kuaishou (1024 HK)

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Divergent outlook among sub-segments: 1) Live-streaming and cross-border e-commerce are the area of growth in the e-commerce space, while soft consumer sentiment has prompted major e-commerce platforms to increase user incentives and price subsidies, which intensifies industry competition. 2) Major short video platforms are leveraging their online traffic to live-streaming e-commerce with success. 3) Competition in the online gaming market has been less than that in the e-commerce market, and major players have been largely maintaining their respective market positions. 4) In the local service market, we are seeing competition in the in-store segment, which could lead to margin pressure from increased user subsidies/incentives. Competition in the food delivery market is less intense due to higher entry barrier on local on-demand delivery network. 5) Increasing competition in the AI space with over 540 AI models/algorithms being successfully registered with the Chinese regulators so far.

The art of cherry picking. China internet stocks are trading at a wide valuation range with distinct risk-reward profiles, which requires a different stock selection strategy based on each valuation category. Specially, we prefer 1) Valuation play (high-single-digit PE) with shareholders' return enhancement potential supported by strong balance sheet; 2) Counters with above-peer growth momentum driven by ongoing market share gains with reasonable valuation (high-teens P/E); 3) For counters with mid-range valuation (low-to-mid teens P/E), we prefer those with online gaming and live-streaming e-commerce exposure.

Pinduoduo, Alibaba, NetEase, and Kuaishou. Based on the above criteria, our preferred picks in the internet space include Pinduoduo, Alibaba, NetEase, and Kuaishou. In our view, sector valuations have turned reasonable with the moderating economic outlook being priced in, leading to improved risk-reward profile.

Valuation summary

Company	Ticker	Rating	Price	TP	2024E P/S(x)	2025E P/S(x)	2024E Core P/E*(x)	2025E Core P/E*(x)
Alibaba - ADR	BABA US	BUY	US$72.00	US$113	1.3	1.2	7.7	7.0
Alibaba - SW	9988 HK	BUY	HK$70.8	HK$110	1.3	1.2	7.7	7.0
Kuaishou	1024 HK	BUY	HK$44.3	HK$65	1.3	1.2	14.3	10.3
Meituan-W	3690 HK	BUY	HK$87.8	HK$110	1.6	1.3	18.4	14.1
NetEase -S	9999 HK	BUY	HK$166.9	HK$200	4.4	4.0	14.0	12.9
NetEase -ADR	NTES US	BUY	US$105.90	US$128	4.4	4.0	15.3	13.9
Pinduoduo	PDD US	BUY	US$121.30	US$180	4.2	3.2	17.8	14.0

Source(s): Bloomberg, ABCI Securities Estimates

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

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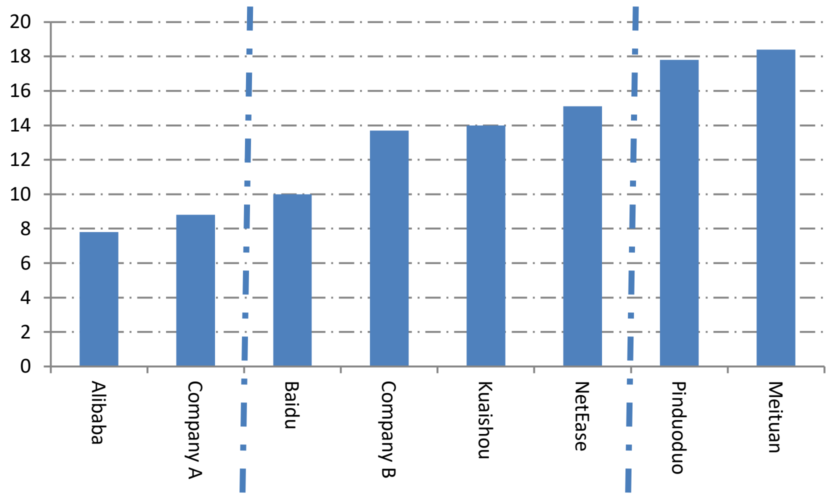
Cherry picking the China internet stocks

China's internet stocks have been de-rated over the past few quarters amid the softening economic environment and lackluster market sentiment. Looking forward, the sector represents both opportunities and risks for investors. After significant share price corrections, valuations have turned reasonable with the moderating economic outlook being priced in; consequently, the risk-reward profile have improved for most counters. However, the less-than-sanguine economic environment will limit industry growth in the near future and affect business performance of companies.

To compare the risk-reward profile of major internet stocks, we start by accessing their relative valuations.

Exhibit 1: Forward core P/E* of major internet platforms



Source(s): Bloomberg, ABCI Securities estimates

Note: Company A: A major e-commerce platform; Company B: A major online social network and gaming platform

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

As seen, China internet stocks are trading at a wide valuation range that can be classified into three categories.

Valuation play: Look for shareholders' return enhancement potential. Alibaba and another e-commerce platform (Company A) are trading towards the low-end of the sector valuation range at ~8x forward P/E amid intensified competition and soft consumer sentiment. While fundamental headwinds are likely to persist in the near term, we believe their low valuations have priced in the moderating growth outlook. In particular, Alibaba has a strong balance sheet with the potential of increasing shareholders' return. In our view, near-term valuation recovery for these bargain counters would depend on their shareholders' return initiatives.

Mid-range valuation: Be selective: Kuaishou, NetEase, Baidu (9888 HK), and a major online gaming platform (Company B) are currently trading at low-to-mid-teens forward P/E. These companies cover various sub-segments such as local service e-commerce, live-streaming/short video, online gaming, etc. In our view, investors should select those with better near-term fundamentals. Among these sub-segments, we prefer online gaming and live-streaming/short video platforms with a more favorable operating environment compared to those focusing on local service e-commerce. As a result, we prefer Kuaishou and NetEase in the mid-range category.

Above-peer valuation: Growth momentum is key. Despite the soft macro environment, selected companies such as Pinduoduo are able to achieve robust growth by increasing market share among peers and new business expansion, thus commanding a higher valuation than peers. Currently, Pinduoduo is trading at the high-teens forward P/E but we believe its superior growth can justify its valuation.

Based on the above analysis, our preferred picks in the internet space are as below.

- **Pinduoduo (PDD US):** Pinduoduo has been achieving strong revenue growth in recent quarters, implying market share gains against peers. In our view, this can be attributed to 1) solid position in the industry as a "value-for-money" platform when shoppers are turning more frugal amid a slowing economy; 2) enhanced monetization capabilities driven by operational improvement; 3) optimized product portfolio enabled by deepened cooperation with brands and continuous investments in agriculture and other areas; 4) increased contribution of emerging businesses, including Duoduo Grocery and Temu. We believe Pinduoduo commanded a mid-20s market share in China’s e-commerce market as of Dec 2023, challenging incumbents such as Alibaba (9988 HK, BABA/US).

- **NetEase (9999 HK/NTES US):** NetEase is the second-largest player in China’s online gaming market with a strong track record in self-developed games. We estimate its online gaming revenue is around 40% of that of the largest online gaming platform in China. Its flagship game “Fantasy Westward Journey” (FWJ), maintained a top 10 position in the revenue ranking in recent months. In addition, its recently launched games “Justice Mobile” and “Egg Party”, entered the top 10 position in 2023.

- **Kuaishou (1024 HK):** Kuaishou has successfully leveraged its user traffic to live-streaming e-commerce in recent years. It is now one of the three major live-streaming platforms in China (Alibaba, Douyin, and Kuaishou) with an estimated mid-single digit market share in the e-commerce market. We estimate its revenue contribution related to e-commerce activities (online advertising spending, service charges, etc. by e-commerce merchants) are broadly in the 30s range.

- **Alibaba (9988 HK/ BABA US):** Alibaba is still the largest e-commerce platform in China with an estimated market share in the mid-40s despite lackluster consumption. Its recent decisions not to proceed with the full spin-off of Cloud Intelligence Group and to suspend the IPO of Freshippo have raised concerns over near-term shareholders’ return. After recent share price corrections, the counter’s valuation is undemanding and implies room for recovery in the medium term, in our view.

Exhibit 2: Valuation summary

Company	Ticker	Rating	Price	TP	2024E P/S(x)	2025E P/S(x)	2024E Core P/E(x)*	2025E Core P/E(x)*
Alibaba - ADR	BABA US	BUY	US$72.00	US$113	1.3	1.2	7.7	7.0
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Source(s): Bloomberg, ABCI Securities estimates

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

HKD/CNY =0.92; USD/CNY = 7.20

Risks and opportunities among sub-segments

On the macro front, we see a divergent operating environment among sub-segments within the internet sector.

Online shopping: Live-streaming and cross-border e-commerce are rising stars. Online shopping has slowed in recent months amid softening economy and we expect such trend to persist in the near term. In addition, we believe online shoppers have turned price-sensitive and increased their "wallet-share" towards value-to-money e-commerce platforms such as Pinduoduo. This trend has prompted major e-commerce platforms to increase their sales and marketing effort by raising user incentives and price subsidies, which intensifies industry competition.

On a positive note, live-streaming and cross-border e-commerce is emerging. Selected platforms such as Pinduoduo and Shein are actively developing cross-border e-commerce and growing traction have been observed in various overseas markets.

Short video and live-streaming: Leveraging traffic to e-commerce. Major short video platforms such as Douyin and Kuaishou are leveraging their online traffic to live-streaming e-commerce with success. In 9M23, live-streaming e-commerce sales rose 60.6% YoY and accounted for 18.3% of total online sales, according to the Ministry of Commerce. We attribute its rising popularity to 1) the products offered, which are generally of low prices; 2) the more interactive features than the traditional search-based e-commerce format. Short-video platforms such as Douyin and Kuaishou are major players in this emerging segment. Meanwhile, Alibaba (9988 HK/ BABA US): has been actively developing live-streaming business to defend its market position.

Online gaming: Stable competition amid a changing regulatory environment. In our view, competition in the online gaming market has been less than that in the e-commerce market, and major players have been maintaining their respective market position. In our view, regulatory hurdle on new game approvals and long development cycles of blockbuster games discourage new entrants, such as short-video platforms, to expand into the gaming realm. Nonetheless, regulatory requirements on user time for youngsters, gaming content, monetization method, among others, have tightened over time and online gaming platforms need to be flexible in adjusting its business model to the continuous changes.

Local service: A mixed outlook. Within the local service market, we are seeing competition in the in-store segment from Douyin, which could lead to margin pressure arising from increased user subsidies/incentives. Competition in the food delivery market is less intense due to higher entry barrier on local on-demand delivery network. In addition, the increased supply of food delivery riders amid economic downturn could alleviate some of the cost pressure resulted from raising user subsidies/incentives needed to stimulate slowing demand.

In addition, the food and grocery space is consolidating, with Missfresh (MF US) and Dingdong Maicai (DDL US) scaling down their businesses in recent quarters. In addition, community group purchase platforms have seen tightened regulatory control over user subsidies due to potential impact on traditional grocery store/wet market. Community group purchase platforms benefited immensely during the pandemic period due to surge in demand for food and grocery e-commerce; however, as consumer demand has ebbed post-pandemic, community group purchase platforms are now rationalizing their expansion plans with less aggressive targets.

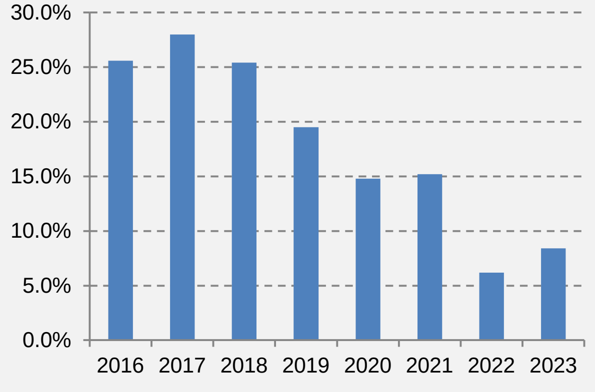
Generative AI: Increasing competition. Since June 2023, there are over 540 AI models/algorithms being successfully registered with the Chinese regulators so far. Currently, various internet companies, including Alibaba, Xiaomi (1810 HK), Baidu, Ant Group, NetEase, Meituan, Huawei, Douyin, among others, have developed their respective large language models. In our view, many internet platforms have been actively developing their generative AI models, and competition in this emerging segment is intensifying. These generative AI models generally offer interactive features such as interactive dialogue and content (text and graphic) generation. Platforms can utilize these features to improve overall user experience and stickiness and explore monetization opportunities. However, US's export control of high-end AI chips could hinder industry development in the long run due to the intensive computing power (CPU) required for training and running these AI models.

For a more detailed evaluation of each sub-segment, please refer to "Segment Profile" in the next section.

Segment profile: Online shopping

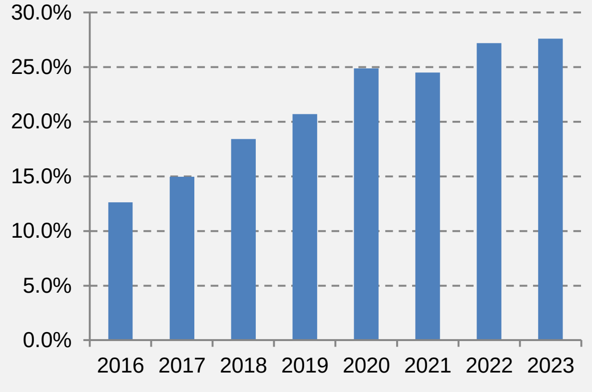
- **China's online sales growth has turned steadier** after years of development. According to NBS, online sales of physical goods grew 8.4% YoY in 2023. In particular, the 8.4% industry growth in 2023 was lower than the 10.8% industry growth in 1H23, indicating a slowdown in 2H23
- By product category, online sales of food products, groceries, and apparel rose 11.2%, 7.1%, and 10.8% in 2023
- **Online shopping penetration rate was generally in an uptrend** in recent months, indicating an ongoing consumption shift from offline to online
- **Live-streaming e-commerce** has been fast growing in recent years. In 9M23, live-streaming e-commerce sales rose by 60.6% YoY and accounted for 18.3% of total online sales, according to Ministry of Commerce. Short video platforms such as Douyin and Kuaishou (1024 HK) are major players in this emerging segment, leading to competitive pressure to traditional e-commerce platforms. On the other hand, Alibaba has been actively developing live-streaming business to defend its market position
- Major e-commerce platforms are **increasing their sales and marketing effort** by raising user incentives and price subsidies. In our view, **online shoppers have turned more price-sensitive** in past years due to the pandemic and moderating economic development, prompting e-commerce platforms to enhance price competitiveness
- In terms of market share, we estimate that Alibaba is still the largest e-commerce platform with mid-40s market share, vs. Pinduoduo (mid-20s), Platform A (low-20s), Douyin (high-single-digit), and Kuaishou (mid-single-digit)
- Over the past few years, **Pinduoduo and short-video platforms (Douyin and Kuaishou) are gaining market shares.** Common features of these platforms: 1) Product offers have low prices; 2) More interactive features (social e-commerce, live streaming, etc.) than traditional search-based e-commerce format
- Selected platforms such as Pinduoduo and Shein are actively developing **cross-border e-commerce** and gained growing traction in various overseas markets

Exhibit 3: Online sales growth of physical goods (YoY)



Source(s): NBS, ABCI Securities

Exhibit 4: Online shopping penetration rate



Source(s): NBS, ABCI Securities

Segment profile: Short video and live-streaming

- China's short-video market is primarily **dominated by Douyin and Kuaishou**. According to Questmobile, Douyin had 743mn MAUs vs. 457mn for Kuaishou in Sep 2023.

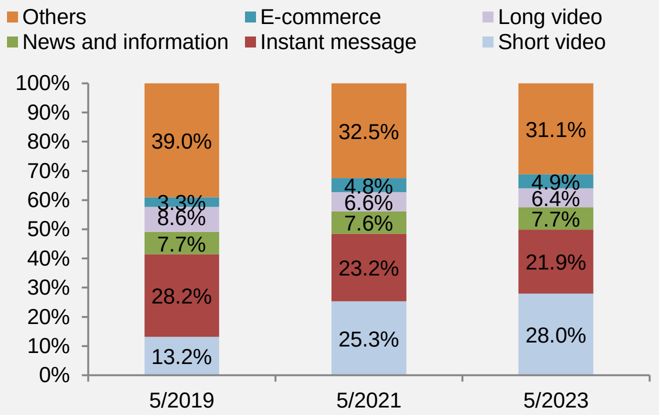
- **Short-video platforms have been gaining popularity** in recent years and has the highest market share in terms of time spent among internet users. According to Questmobile, time spent market share of short videos increased from 13.2% in May 2019 to 28.0% in May 2023.

- **Monetization:** Online advertising has been the major form of monetization for short-video platforms. In addition, short video platforms have been actively leveraging its traffic to other monetization scenarios such as e-commerce, local service, etc. Short-video advertising accounted for about 17.3% of China's online advertising market in 1H23, according to Questmobile.

- **Live–streaming e-commerce:** Short-video platforms have been successfully developing live-streaming e-commerce businesses in recent years, challenging traditional search-based e-commerce platforms. In 9M23, live-streaming e-commerce sales rose by 60.6% YoY and accounted for 18.3% of total online sales, according to Ministry of Commerce.

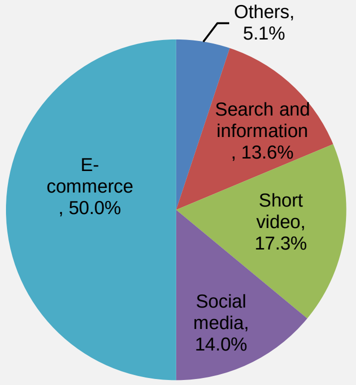
- **Local service:** Douyin has been actively developing in-store business in recent quarters, posing an increasingly significant competitive pressure on Meituan.

Exhibit 5: Market share in terms of user time spent



Source(s): Questmobile, ABCI Securities

Exhibit 6: China's online advertising market share (1H23)



Source(s): Questmobile, ABCI Securities

Segment profile: Local service

Food delivery

- Meituan and Ele.me are the two major players in this segment. Based on our estimates, **Meituan's food delivery market share at ~60% is roughly twice of Ele.me.** Meituan has been able to maintain its leading market position despite Douyin's entry attempts

- The requirement of nationwide on-demand delivery network and short delivery time presents a major entry barrier, in our view. Nonetheless, Douyin is addressing the barrier by partnering with third-party delivery platforms such as Ele.me and Dada

- Regulators are requesting food delivery platforms to **take up the social insurances payment of delivery riders**

On-demand delivery

- **Business model:** Platforms with no inventories. Local on-demand delivery networks connect local retailers such as supermarkets/grocery stores with consumers. Delivery time is usually within hours

- In contrast with the community group purchase model which targets price-sensitive consumers, this segment **targets those willing to pay for convenience**

- **Meituan, Dada, and Ele.me are major players.** Food delivery platforms such as Meituan and Ele.me are leveraging their existing delivery network for this segment

- Popular product categories include FMCG products and fresh products

- The segment is still in the early stage of development with **low penetration. Most players are still in losses**

- On-demand delivery enjoys a **more supportive regulatory environment than community group purchase** since the former helps SMEs extend their geographical coverage, whereas the community group purchase business usually take market shares away from SMEs

Community group purchase

- **Community group purchase** (pre-order via community leader and next-day delivery) is a popular business model in the local service segment as local residents can enjoy low prices via grouping orders with neighboring residents. Community group purchase is particularly popular in lower-tier cities. Major players include Pinduoduo, Meituan, and Alibaba

- Major community group purchase platforms generally provided substantial **user subsidies** to maintain price advantages and attract customers in the initial stage of development. The situation has changed recently due to **tightened regulatory control over price competition** and platforms' cost-control initiatives. As a result, platforms' profitability has generally improved in recent quarters. Less aggressive industry subsidies, however, could reduce the price advantages of community group purchase over the traditional grocery store/wet market

- The food and grocery e-commerce space is consolidating due to intensified competition. For example, Missfresh (MF US) and Dingdong Maicai (DDL US) have significantly scaled down their businesses in recent quarters. While Missfresh and Dingdong Maicai do not follow the community group purchase model, they are essentially competing with community group purchase platforms in the food and grocery e-commerce space

- On the macro front, there was a surging demand for food and grocery e-commerce during pandemic due to lockdowns, which benefited the community group purchase platforms immensely. However, **After the epidemic, consumer demand for food and grocery e-commerce has normalized**

In-store

- In contrast to the above “To-home” segments (food delivery/on-demand delivery/community group purchase), in-store business directs online traffic to offline store (To-store) via group purchase deals, store review articles, short videos, etc. Overall, an increasing number of offline retailers are developing online marketing channels to support growth in the in-store segment

- Short-video and live-streaming platforms, including Douyin, are capitalizing on their traffic in the in-store segment by providing online marketing channels to retailers. Competition in the in-store segment has been increasing as a result. .

- Compared with food delivery, this segment has a lower entry barrier because an on-demand delivery network is not required. Since pricing and customer incentives are the major competing criteria, as such, margin pressure on local service platforms will increase

- By our broad estimates, Douyin’s in-store GMV size is 30-50% of that of Meituan’s

Segment profile: Online gaming

- China's online gaming market is **dominated by a handful of major players**. We estimate the top three players collectively accounted for over 50% of the market share, while the rest is more fragmented with numerous smaller game developers. The top player (Company A) is a distant leader with a revenue size 1.8x-2x of that of the second-largest player, NetEase. The third-largest player MiYoHo, due to its much smaller gaming portfolio than NetEase's, presents no major challenges to the latter in our view

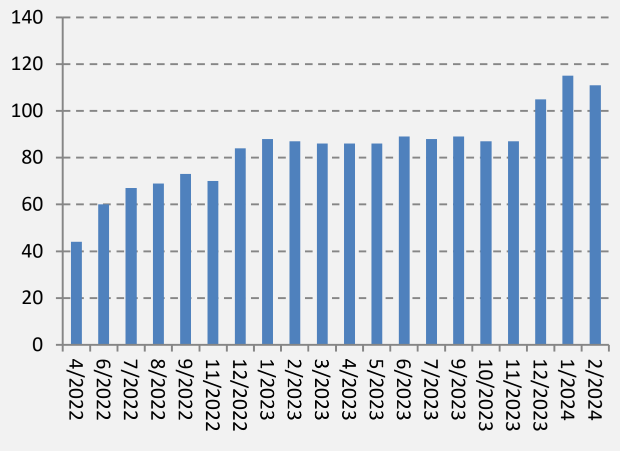
- In our view, **regulatory hurdle on new game approvals and long development cycles of blockbuster games discourage potential new entrants**, including the short-video platforms. This results in a **more stable competitive environment than other sub-segments,** such as e-commerce and local service, in recent years

- One of new entrants, **Douyin, has decided to exit the online gaming market** after brief attempts

- **New game approval** was resumed since Apr 2022 after suspending for eight months. The regulator has granted new game approvals in most months since then. The average number of approved new games per month has been gradually increasing. In addition, the majority of games approved were from smaller game developers in the initial months after resumption though clearance has gradually extended to games on the larger online gaming platforms later on

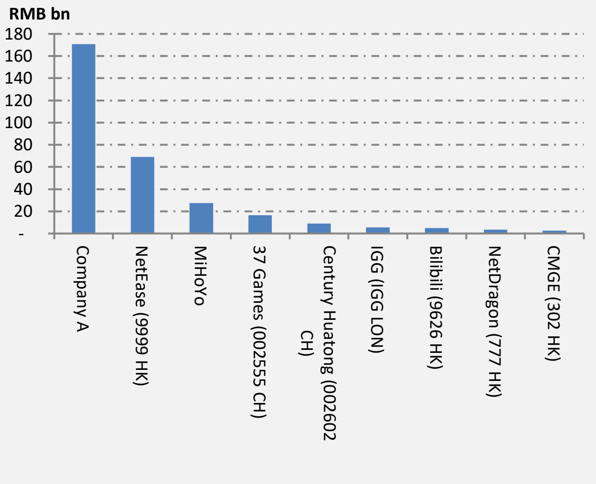
- **Tighten regulatory requirements** on user time for youngsters, gaming content, monetization method, etc. in recent years. In Dec 2023, the regulator proposed potential new online gaming rules that would tighten various user incentive mechanisms such as daily login reward, first-time spending reward, and tighter requirements for sales of virtual items, although implementation detail is still uncertain at the moment

Exhibit 7: No. of new online game approval



Source(s): Sapprft, ABCI Securities

Exhibit 8: Online gaming revenue – major gaming platforms (2022)



Source(s): Companies, Guangming Daily, ABCI Securities
Note: Company A is a major social network and online gaming platform in China

Segment profile: Generative AI

- The **regulatory environment of generative AI is an evolving one**, given the industry is still in its early stage. Recently announced generative AI measures include prohibiting generative AI services to generate inappropriate contents, leveraging algorithms, data and other information to engage in monopoly and unfair competition, etc. In addition, it required generative AI service providers to conduct security review and register their AI models/algorithms with regulators before product launch. Looking forward, regulators might fine-tune existing measures or introduce rules in accordance with the development of the industry

- Since Jun 2023, there are over **540 AI models/algorithms being successfully registered** so far. Currently, **various internet companies including Alibaba, Xiaomi, Baidu, Ant Group, NetEase, Meituan, Huawei, Douyin, etc have developed their respective large language models.** In our view, many internet platforms have been actively developing generative AI models, and **competition** in this emerging segment has been growing. Among these models, Alibaba's Tongyi Qianwen, Baidu's ERNIE Bot, Hunyuan, and 360's Smart Brain have become the first batch of models that pass the official "Large Model Standard Compliance Evaluation" by China Electronics Standardization Institute

- Generative AI models offer interactive features such as interactive dialogue, content (text and graphic) generation, etc. Platforms can utilize these features to **improve overall user experience and stickiness and explore monetization opportunities**

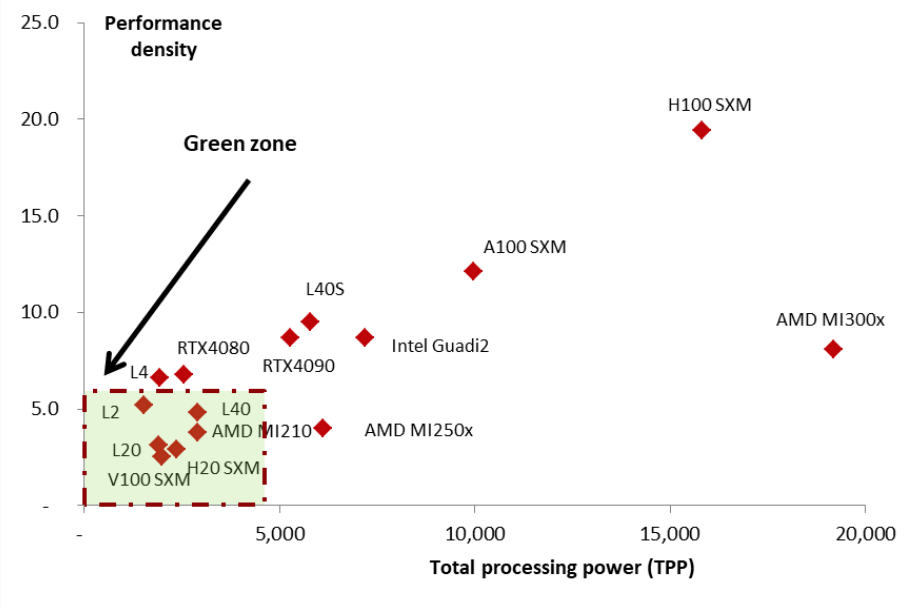
- Selected platforms have adopted an **open-source AI strategy** which allows other enterprises to develop their own AI models based on the open-sourced model. E.g., Alibaba has built one of the largest open-source AI developer communities in China. Its developer community, ModelScope, has gathered over 2,300 AI models, attracting 2.8mn AI developers and over 100mn cumulative model downloads. It has also launched the open-source version of its Tongyi Qianwen models. In our view, this could **lower the entry barrier of AI model development especially for smaller enterprises**

- **US's export control of high-end AI chips** could hinder industry development in the long run given the intensive computing power (GPU) required for training and running AI models. Currently, the thresholds for export control include total processing performance of 4,800 (TOPS x bit length) and performance density (performance power per die area) of 5.92. As a result, various server-grade GPU models of Nvidia such as A100, A800, H100, H800, L40, L4, etc have been restricted from exporting to China. In our view, **these thresholds are strict**- even the high-end consumer-grade GPU RTX4090 falls within these thresholds

- On a positive note, **Nvidia has developed various models such as H20, L20, and L2 within these regulatory thresholds for the China market,** which help reduce some of the restriction impacts. Having said that, **the processing powers of these customized chips are inferior compared with their official models.** The following chart compares the performance metrics of various GPUs. Note that only those in the left lower corner belong to the "green zone" under the current US regulatory environment, meaning that the items can be exported without regulatory control

- In response, the **Chinese companies are developing its own AI chips.** For example, Huawei has launched Ascend 910B, a 7nm-based GPU which ranges between A100 and H100 in terms of performance. Having said that, its production volume could be constrained by SMIC's "(N+2) 7nm" production capability

Exhibit 9: Performance comparison of major AI chips



Source(s): Companies, Semianalysis, ABCI Securities

Alibaba (9988 HK/BABA US)
In transition

- Taobao/Tmall is undergoing business revitalization; cross-border e-commerce may become a near-term growth driver
- Mixed development in shareholders' return initiatives
- Undemanding valuation after recent share price corrections

Company Report

Rating (SW-share): BUY
TP (SW-share): HK$ 110
Rating (ADR): BUY
TP (ADR): US$ 113

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E-commerce platforms in transition. We believe Taobao and Tmall are likely to face soft growth in the near term, while the company's revitalization plan to enhance the platform's price competitiveness and user experience will take time to be completed. International digital commerce should see higher near-term growth driven by ongoing development in cross-border e-commerce business, though short-term margin will be pressured as the business is still in the development stage. We expect overall revenue to grow at 8% CAGR in FY3/24-26E, in which Taobao and Tmall would grow at 4% CAGR during the period.

Mixed development in the shareholders' return initiatives. The company targets to repurchase c. 3% outstanding share per year over the next three years via its upsized share repurchase program. In addition, non-core retail asset disposal is under consideration. Given the dismal state of the market, the company is not in a rush to pursue IPO or spin-off of its business units. This could, in our opinion, lead to some market disappointments.

A value play. Maintain **BUY** with SOTP-based TP at HK$ 110 for Alibaba-SW (9988 HK) and US$ 113 for Alibaba-ADR (BABA US). After recent share price corrections, the counter is currently trading at an undemanding valuation. In our view, extent and pace for valuation recovery in coming months would depend on 1) overall market sentiment; 2) near-term business outlook; 3) development of shareholders' return initiatives.

Price (ADR/SW-share)	US$72.0/ HK$70.8
Est. share price return (ADR/SW-share)	56.7%/55.4%
Est. dividend yield (ADR/SW-share)	1.6%/1.5%
Est. total return (ADR/SW-share)	58.3%/56.9%
Last Rating &TP (ADR/SW-share)	BUY/US$113 BUY/HK$110
Previous Report Date	Feb 9, 2024

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L (HK$) (SW-share)	108.5/64.6
52Wk H/L (US$) (ADR)	109.8/66.6
Issued shares (bn)	20.0
Market cap (HK$ bn) (all share)	1,416
3-mth avg daily turnover (HK$ mn) (SW-share)	3,993
3-mth avg daily turnover (US$ mn) (ADR)	1,749
Major shareholder(s) (%):	
Joseph Tsai	1.4%

Source(s): Bloomberg, HKEx, Company

Results and Valuation

FY end Mar 31	FY23A	FY24E	FY25E	FY26E
Revenue (RMB mn)	868,687	942,779	1,009,352	1,093,782
Chg (%,YoY)	*1.8*	*8.5*	*7.1*	*8.4*
Net profit (RMB mn)	72,509	101,316	122,419	130,372
Chg (%,YoY)	*17.0*	*39.7*	*20.8*	*6.5*
Core net profit (RMB mn)	143,991	161,248	167,462	178,968
Chg (%,YoY)	*0.3*	*12.0*	*3.9*	*6.9*
Underlying EPS (RMB)	3.5	5.0	6.2	6.8
Chg (%,YoY)	*20.3*	*44.3*	*24.6*	*9.8*
Core EPS (RMB)*	6.8	7.9	8.4	9.3
Chg (%,YoY)	*3.5*	*15.4*	*7.1*	*10.2*
Core P/E (x)- ADR*	9.5	8.2	7.7	7.0
Core P/E (x)-SW share*	9.6	8.3	7.7	7.0
ROAE (%)	6.6	8.9	10.4	10.5
ROAA (%)	4.2	5.7	6.6	6.6

1 ADR = 8 ordinary shares
*Excluding share-based compensation, impairments, fair value changes of investment, etc.
Source (s): Bloomberg, ABCI Securities estimates

Financial Outlook

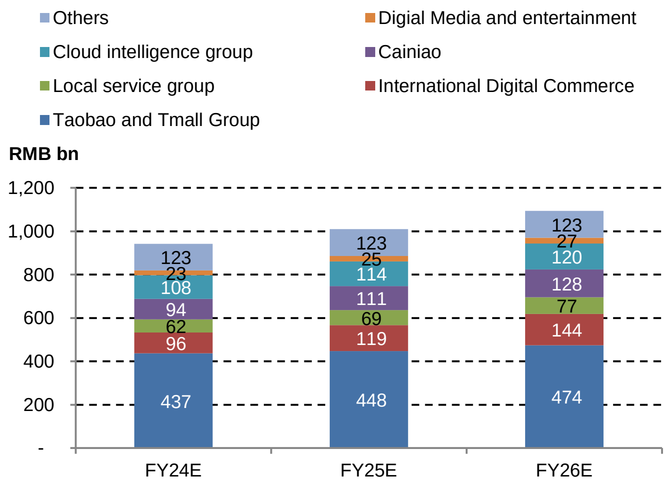
We expect revenue to grow at 8% CAGR in FY3/24E-26E.

Taobao and Tmall revenue would expand at 4% CAGR in FY3/24E-26E. In our view, near-term challenges include take rate pressure as GMV shifts towards Taobao merchants amid moderating consumer sentiment; competition from Pinduoduo and other live-streaming e-commerce platforms can also affect revenue. The company is revitalizing its platform to enhance price competitiveness and user experience with a new management team, but we believe a revamp will take time.

We expect Cloud intelligence's revenue to grow at 5% CAGR in FY3/24E-26E due to continuous business adjustment and rivalry from telco cloud operators. In our view, more focus will be on propping up profitability instead of driving revenue growth for this segment in the near term.

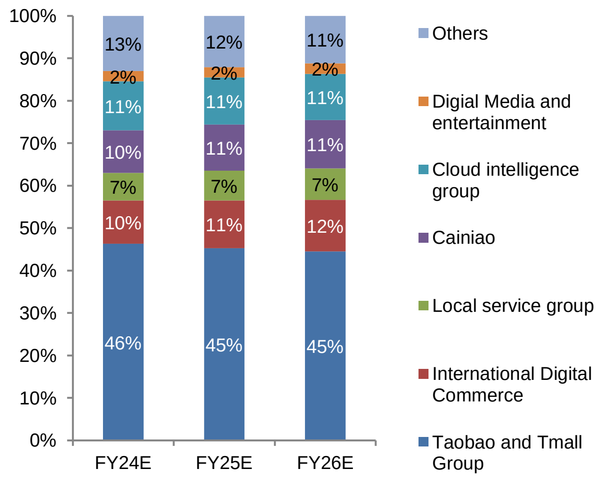
For other businesses, we expect International Digital Commerce to grow at 23% CAGR in FY3/24E-26E, driven by expansion of cross-border e-commerce initiatives such as AliExpress Choice. In addition, we expect Cainiao and Local consumer services to expand at 16% and 12% CAGRs in FY3/24E-26E amid ongoing business expansion. For DME (Digital Media and Entertainment), we expect it to grow at 8% CAGRs in FY3/24E-26E driven by offline entertainment business.

Exhibit 10: Revenue outlook



Source(s): Company, ABCI Securities estimates

Exhibit 11: Revenue mix outlook

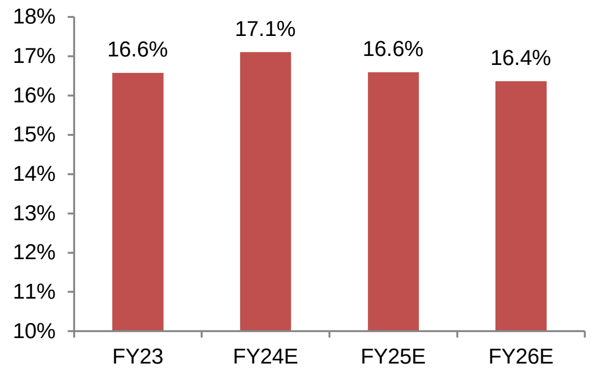


Source(s): Company, ABCI Securities estimates

In terms of segment profitability, we estimate adjusted EBITA margin of Taobao and Tmall to moderate to 43.6% in FY26E due to increased customer incentives and promotions to boost sales. Adjusted EBITA margin of other businesses (International commerce/Local service/Cainiao/Cloud/DME) would remain largely stable, in which International commerce is likely to see some margin pressure amid ongoing business expansion, while Cloud margins would continue to improve.

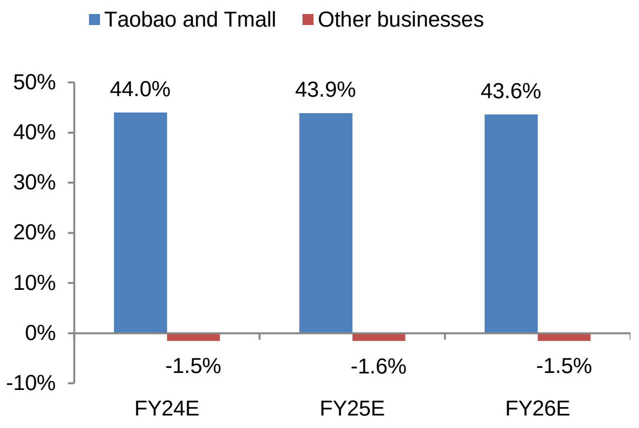
We expect core net margin (excl. impacts of share-based compensation and other non-operating items) to be 16.4% for FY26E. Our financial forecast remains unchanged.

Exhibit 12: Core net margin



Source(s): Company, ABCI Securities estimates

Exhibit 13: Segment adjusted EBITA margin



Source(s): Company, ABCI Securities estimates

Recommendation

We maintain our SOTP-based TPs to HK$ 110 for Alibaba-SW (9988 HK) and US$ 113 for Alibaba-ADR (BABA US). Our TP for Alibaba-SW (9988 HK) implies 10.8x FY3/25E core P/E.

In terms of shareholders' return initiatives, the company targets to repurchase c. 3% outstanding share per year over the next three years via its upsized US$ 35.3bn share repurchase program till Mar 2027. In addition, non-core retail asset disposals is under consideration.

Given the dismal state of the market at present, the company is not in a rush to pursue IPO or spin-off for its business units, which may lead to some disappointments among investors.

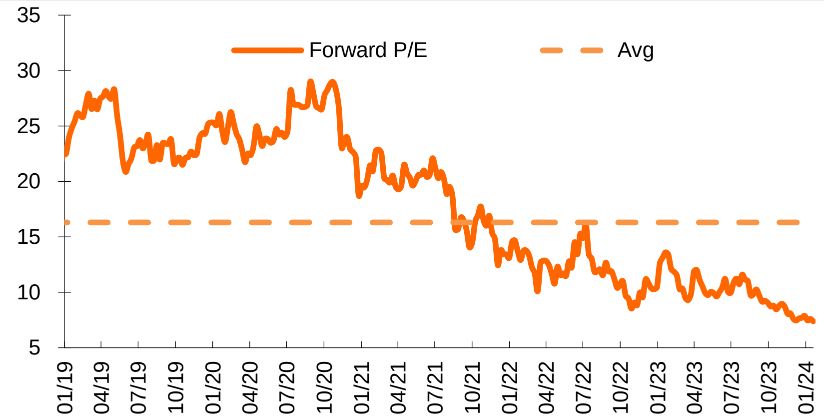
The counter is currently trading at an undemanding valuation. While near-term volatility might still persist, we believe current valuation implies recovery potential in the medium term. In our view, the extent and pace for valuation recovery in coming months would depend on 1) overall market sentiment; 2) near-term business outlook; 3) development of shareholders' return enhancement initiatives.

Exhibit 14: SOTP-based TP for Alibaba-SW (9988 HK)

	HKD per share	% of total	Remarks
Taobao and Tmall	55	49.7%	6.5x FY3/25E P/E
Other businesses (International Digital Commerce/Cainiao/Local service/Cloud/DME)	19	17.1%	0.8x FY3/25E P/S
Investments	16	14.3%	Latest book value with a 40% discount
Net cash	21	18.9%	Latest book value
Total	**110**		

Source(s): ABCI Securities estimates
Note: Refer to Exhibit 10 and 13 for segment financial forecasts.

Exhibit 15: Alibaba's fwd. core P/E



Source(s): Bloomberg, ABCI Securities

Company profile

Business
• After recent **strategic restructuring**, Alibaba now consists of six major business groups (Cloud intelligence, Taobao/Tmall, Local Consumer Service, Cainiao, International Digital Commerce, and Digital media and Entertainment), each with independent management teams and public listing potentials (except for Taobao/Tmall which will remain wholly owned) • **Taobao/Tmall:** Largest ecommerce platform in China with estimated market share at the mid-40s level; we believe its market share has been dropping in recent years due to rising competition from emerging players such as Pinduoduo (PDD US) and short-video platforms. Estimated annual active buyers amounted to RMB ~1bn in China, while estimated GMV per buyer was around RMB 9K in 2022, vs. about RMB 3.3K for Pinduoduo and about RMB 6K for another e-commerce platform • **International Digital Commerce:** Lazada, AliExpress, and Trendyol, etc. • **Local Consumer Services:** "To-Home" business of Ele.me and the "To-Destination" business of Amap. Revenue size about one-third of Meituan's (3690 HK) local service business • **Cainiao:** External customers account for about 70% of revenue • **Cloud Intelligence:** Largest public cloud platform in China with about 33% market share • **Digital Media and Entertainment :** Youku (YOKU US), Damai, and Alibaba Pictures (1060 HK) • Other business include Sun Art (6808 HK), Freshippo, Lingxi Games, Intime, Fliggy, etc. • In 3Q23, Ant Group repurchased approximately 7% equity interest from its existing shareholders and the shares repurchased were allocated to the employee incentive plans of Ant Group. **Alibaba's equity interest in Ant Group on a fully diluted basis remains unchanged at 33%**
Financials
• Taobao/Tmall contributes most of Alibaba's operating profit, while other businesses are either loss-making or has minimal profit contribution. Nonetheless, profitability of these business units has been improving recently • Profit contribution from Ant Group at low-teens level • **Core net margin** dropped from high-20s years ago to high-teens level currently due to industry competition and ongoing investments in new business initiatives • **Strong balance sheet** with about RMB 389bn in net cash and RMB 488bn in equity investment in Dec 2023 • The company has set up a capital management committee to undertake a comprehensive capital management plan to enhance shareholder value, such as capital market transactions, shareholder return initiatives, subsidiary equity incentive plans, fundraisings, IPOs, and spin-offs • **Full spin-off of Cloud was cancelled** due to business uncertainties arising from recent expansion of US restrictions on export of advanced computing chips. **IPO of Freshippo has been put on hold** due to market conditions
Management and shareholder
• **Softbank** (9984 JP) has monetized its stakes in Alibaba via forward contracts. There are no shareholders with a stake higher than 5% • **Alibaba's partnership** structure limits the ability of its shareholders to influence corporate matters, such as the nomination and election of directors. For example, its Articles of Association allow the Alibaba Partnership to nominate or, in limited situations, appoint a simple majority of board of directors. There are 28 partners in total and election of new partners requires the approval of at least 75% of all of the partners • **Jack Ma** stepped down as Chairman in 2019. He will also give up its voting control on Ant Group after Ant's restructuring • A series of **management changes** occur due to the strategic reorganization. In June 2023 ,Daniel Zhang, who succeeded Jack's Chairman role since 2019, resigned as Group Chairman and took up the role of Chairman and CEO of Cloud Intelligence Group. Joseph Tsai succeeded Zhang as the new Group Chairman. Yet, only after three months, Daniel Zhang has stepped down from his role of Chairman and CEO of Cloud Intelligence Group in Sep 2023, which surprised the market
Shareholders' return
• Declare an **annual cash dividend of** US$ 1 per ADS for FY3/2023 of US$ 1 per ADS • The company has been ramping up its **share repurchase program** in recent years. The company has boosted its share repurchase program by US$ 25bn through the end of March 2027. Following the increase, it currently has US$ 35.3bn available for share repurchase. The company **targets to repurchase c. 3% outstanding share per year** over the next three years

• Organization restructuring including **spin-off, asset disposal, IPOs**, etc might increase shareholders' return. • The company will form a new asset management company to manage its non-core assets to improve return on capital and enhance shareholders' value • Potential increase in shareholders return constrained by availability of **offshore cash**
Corporate governance/information disclosure
• RMB18.2bn in Antitrust fine in 2021 • Ant Group: Listing suspended in 2020 and RMB 7.07bn in regulatory fine in 2023 • Increase information disclosure as a result of strategic reorganization • Various ESG initiatives in recent years

Source(s):Company, ABCI Securities

Financial Forecast

Consolidated income statement (FY23A-FY26E)

FY Ended Mar 31 (RMB mn)	FY23A	FY24E	FY25E	FY26E
Total revenue	**868,687**	**942,779**	**1,009,352**	**1,093,782**
Cost of sales	(549,695)	(583,301)	(630,472)	(688,678)
Gross profit	**318,992**	**359,478**	**378,880**	**405,104**
Product development expenses	(56,744)	(53,518)	(59,510)	(64,487)
Selling & marketing expenses	(103,496)	(110,689)	(124,159)	(134,544)
General & admin expenses	(42,183)	(37,827)	(40,781)	(44,193)
Amortization/Impairment	(16,218)	(33,627)	(11,103)	(12,032)
Operating Profits	**100,351**	**123,817**	**143,328**	**149,848**
Interest and investment income	(11,071)	1,000	1,500	2,000
Interest expenses	(5,918)	(7,500)	(7,400)	(7,200)
Other income	5,823	5,500	5,500	5,500
Share of results of equity investees	(8,063)	(2,000)	(1,000)	1,000
Profit before tax	**81,122**	**120,817**	**141,928**	**151,148**
Tax	(15,549)	(24,163)	(28,386)	(30,230)
Profit after tax	**65,573**	**96,654**	**113,542**	**120,919**
Minority interests	7,210	4,833	9,083	9,673
Accretion of mezzanine equity	(274)	(171)	(207)	(220)
Profits attributable to ordinary shareholders	**72,509**	**101,316**	**122,419**	**130,372**
Share-based compensation	30,831	18,856	25,234	27,345
Amortization and impairment	37,855	39,906	21,103	22,032
Gains on disposals/revaluation of investments	13,857	1,000	(1,500)	(1,000)
Other non-core items	(11,061)	171	207	220
Non-GAAP profits attributable to ordinary shareholders (Core net profit)	**143,991**	**161,248**	**167,462**	**178,968**
Growth				
Total revenue (%)	1.8	8.5	7.1	8.4
Gross Profits (%)	1.7	12.7	5.4	6.9
Operating Profits (%)	44.1	23.4	15.8	4.5
Net profit (%)	17.0	39.7	20.8	6.5
Core net profit (%)	0.3	12.0	3.9	6.9
Operating performance				
Operating margin (%)	11.6	13.1	14.2	13.7
Net margin (%)	8.3	10.7	12.1	11.9
Core net margin (%)	16.6	17.1	16.6	16.4

Individual items may varies from reported figures due to rounding differences/definition differences
Source(s): Company, ABCI Securities estimates

Consolidated balance sheet (FY23A-FY26E)

As of Mar 31 (RMB mn)	FY23A	FY24E	FY25E	FY26E
Fixed assets	176,031	178,031	179,531	181,031
Investments	453,117	456,117	460,117	466,117
Other non-current assets	425,930	413,303	417,200	420,169
Total non-current assets	**1,055,078**	**1,047,451**	**1,056,848**	**1,067,317**
Cash & equivalents	193,086	222,461	276,925	351,762
Restricted cash and escrow receivables	36,424	38,245	40,157	40,157
Short-term investments and investment securities	331,384	351,384	371,384	396,384
Prepayments, deposits & other assets	137,072	150,779	165,857	165,857
Total current assets	**697,966**	**762,869**	**854,324**	**954,161**
Total assets	**1,753,044**	**1,810,320**	**1,911,172**	**2,021,477**
Accrued expenses, accounts payable and other liabilities	275,950	271,210	290,362	314,650
Other payables & accruals	12,543	13,170	13,829	13,829
Borrowings and notes	12,266	20,266	28,266	34,266
Deferred revenue	71,295	75,422	80,748	87,503
Merchants deposits	13,297	13,962	14,660	14,660
Total current liabilities	**385,351**	**394,031**	**427,864**	**464,907**
Borrowings and notes	149,088	154,088	159,088	164,088
Other non-current liabilities	95,684	98,771	102,013	102,013
Total non-current liabilities	**244,772**	**252,859**	**261,101**	**266,101**
Total liabilities	**630,123**	**646,890**	**688,965**	**731,008**
Net current assets	**312,615**	**368,838**	**426,459**	**489,254**
Mezzanine equity	9,858	10,029	10,236	10,456
Equity attributable to shareholders	989,657	1,034,828	1,102,481	1,180,198
Non-controlling interests	123,406	118,573	109,490	99,816
Total equity	**1,113,063**	**1,153,401**	**1,211,971**	**1,280,014**

Individual items may varies from reported figures due to rounding differences/definition differences
Source(s): Company, ABCI Securities estimates

Consolidated cash flows statement (FY23A-FY26E)

As of Mar 31 (RMB mn)	FY23A	FY24E	FY25E	FY26E
Net income	65,573	96,654	113,542	120,919
Depreciation and amortization	46,938	50,627	39,603	40,532
Other non-cash adjustments	123,759	20,856	26,234	26,345
Change in working capital	(36,518)	(11,761)	12,085	31,042
Operating cash flow	**199,752**	**156,375**	**191,464**	**218,837**
Investing cash flow	**(135,506)**	**(65,000)**	**(70,000)**	**(75,000)**
Financing cash flow	**(65,619)**	**(62,000)**	**(67,000)**	**(69,000)**
Net cash flows	**(1,373)**	**29,375**	**54,464**	**74,837**

Individual items may varies from reported figures due to rounding differences/definition differences
Source(s): Company, ABCI Securities estimates

Kuaishou (1024 HK)

Live-streaming e-commerce as growth driver

- Successfully leveraged user traffic to live-streaming e-commerce in recent years
- Improvement in profitability driven by cost control and operating efficiency
- Maintain **BUY** with revised TP of HK$ 65

Company Report

Rating: BUY
TP: HK$ 65

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

Share price (HK$)	44.3
Est. share price return	46.7%
Est. dividend yield	NA
Est. total return	46.7%
Previous Rating &TP	BUY/HK$85
Previous Report Date	Dec 1, 2023

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L(HK$)	72.5/38.4
Issued class B shares (mn)	3,599
Class B share market cap (HK$ mn)	159,436
Avg daily turnover (HK$ mn)	790
Major shareholder(s)	
Mr. Su Hua	9.8%
Mr. Cheng Yixiao	7.8%

Source(s): Bloomberg, ABCI Securities

E-commerce- a bright spot. In our view, Kuaishou has successfully leveraged its user traffic into live-streaming e-commerce in recent years. It is now one of the three major live-streaming platforms in China (Alibaba, Douyin, and Kuaishou) with an estimated market share of mid-single digits in China's e-commerce market. E-commerce GMV achieved strong growth in recent years, supporting e-commerce advertising revenue and other related value-added services. Strategically, the company has been improving its e-commerce business towards 1) an increased variety of e-commerce scenarios, such as short-video and shelf-based vs. live-streaming; 2) a more balanced mix with more mid-tier/long-tail KOLs.

Improving profitability. The company has demonstrated higher profitability in recent quarters thanks to cost control and improving operating leverage. In addition, its China business has achieved a positive operating profit while losses in overseas business have been narrowing. Looking forward, we expect core net margin to improve to 11.9% in 2025E.

Recommendation. Maintain **BUY** with a revised DCF-based TP of HK$ 65 due to improving profitability and exposure in live-streaming e-commerce business. Our TP implies 14.9x 2025E core P/E. After recent share price corrections, the counter is currently trading at about 10x 2025E core P/E, which is undemanding in our view.

Results and Valuation

FY end Dec 31	2022A	2023E	2024E	2025E
Revenue (RMB mn)	94,183	113,473	130,512	143,057
Chg (%,YoY)	*16.2*	*20.5*	*15.0*	*9.6*
Net profit (RMB mn)	(13,690)	4,160	7,813	12,560
Core net profit (RMB mn)	(5,753)	8,160	12,313	17,060
EPS (RMB)	(3.2)	1.0	1.8	2.9
Core EPS (RMB)*	(1.3)	1.9	2.9	4.0
P/S (x)	1.8	1.5	1.3	1.2
Core P/E (x)*	NA	21.5	14.3	10.3
ROAE (%)	NA	18.6	22.7	24.8
ROAA (%)	NA	8.7	11.6	14.0

Source(s): Company, ABCI Securities estimates
*Excluding share-based compensation, impairments, fair value changes of investment, etc.

Financial outlook

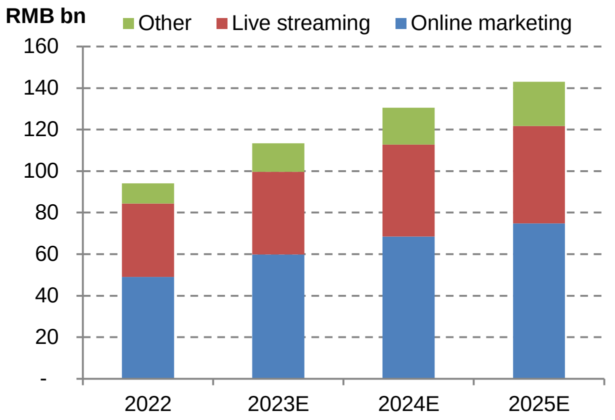
We expect overall revenue to grow at 12% CAGR in 2023-25E.

Online marketing: We expect online marketing revenue to expand at 12% CAGR in 2023-25E amid 5% CAGR in DAU and 6% CAGR in average online marketing revenue per DAU during the same period. We expect e-commerce-related advertising to be the main driver, mitigating the near-term softness in external advertising demand.

Live streaming: We expect live streaming revenue to grow at 9% CAGR in 2023-25E, driven by 4% CAGR in live-streaming MPUs (monthly paying users) and 4% CAGR in live-streaming monthly ARPPU (average revenue per paying user) during the same period.

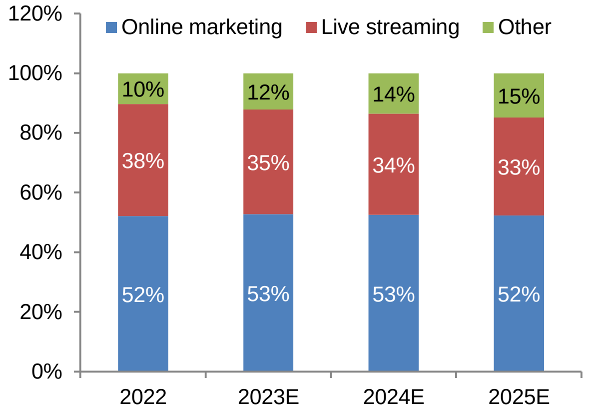
Others: We expect other revenue, mainly consists of e-commerce business and other value-added services, to grow at 24% CAGR in 2023-25E, primarily driven by e-commerce business.

Exhibit 16: Revenue outlook



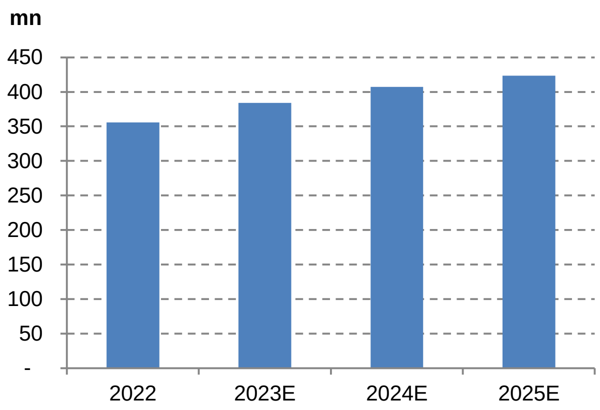
Source(s): Company, ABCI Securities estimates

Exhibit 17: Revenue mix outlook



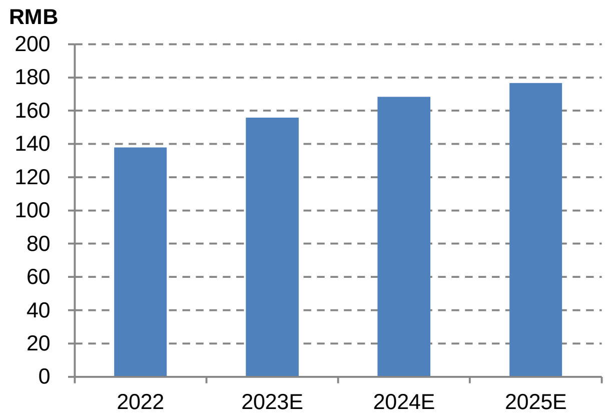
Source(s): Company, ABCI Securities estimates

Exhibit 18: DAU trend



Source(s): Company, ABCI Securities estimates

Exhibit 19: Avg. quarterly online marketing service revenue per DAU



Source(s): Company, ABCI Securities estimates

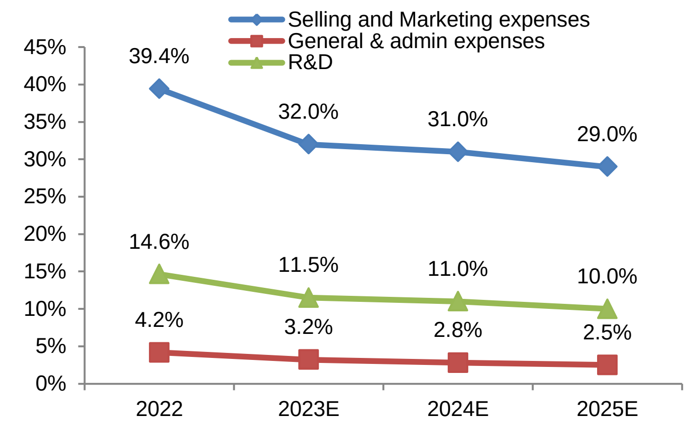
Selling and marketing expenses: Selling and marketing expenses have been a major cost item. The company has been strengthening cost control and improving operational efficiency to boost margins. In particular, domestic business has already achieved a quarterly breakeven. We expect selling and the marketing expenses/revenue ratio to fall to 29% in 2025E due to cost control and improving operating leverage.

General and admin expenses: Thanks to the higher economies of scale and operational improvement, we expect general and the admin cost-to-revenue ratio to drop from 3.2% in 2023E to 2.5% in 2025E.

R&D: We expect R&D cost-to-revenue ratio to drop from 11.5% in 2023E to 10.0% in 2025E, thanks to improving economies of scale.

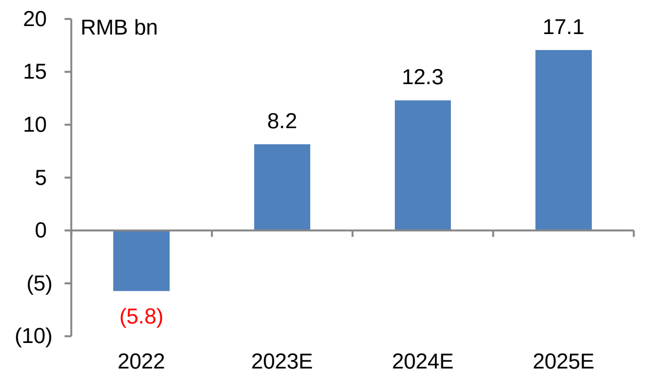
Based on above growth trends, we expect a core net profit of RMB 16.9bn in 2025E vs. RMB8.2bn in 2023E.

Exhibit 20: Cost trend (% of revenue)



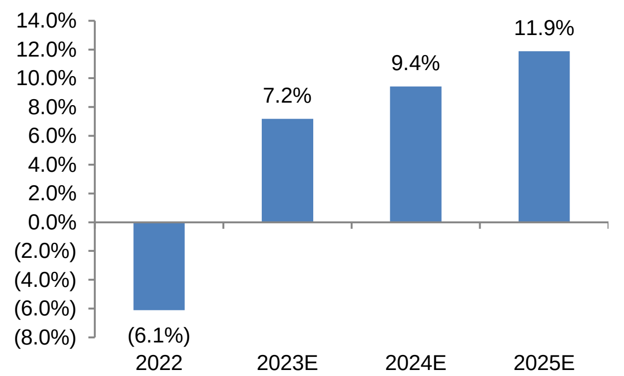
Source(s): Company, ABCI Securities estimates

Exhibit 21: Core net profit trend



Source(s): Company, ABCI Securities estimates

Exhibit 22: Core net margin



Source(s): Company, ABCI Securities estimates

Exhibit 23: Forecast changes

	2024E			
RMB mn	**Old**	**New**	**Diff**	**Comment**
Revenues	130,789	130,512	-0.2%	Fine-tuning growth assumption
Core profit	12,328	12,313	-0.1%	

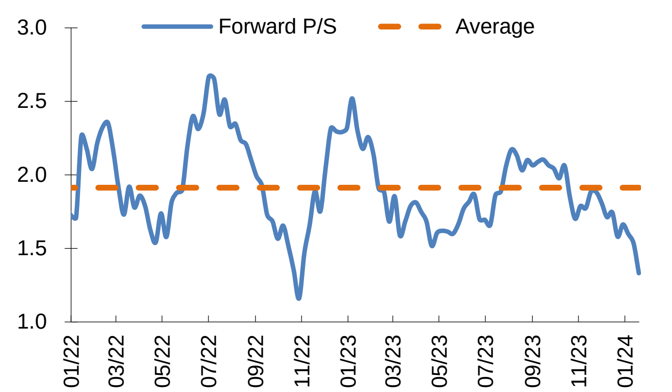
Source(s): ABCI Securities estimates

2023E financial forecast remains unchanged

Recommendation

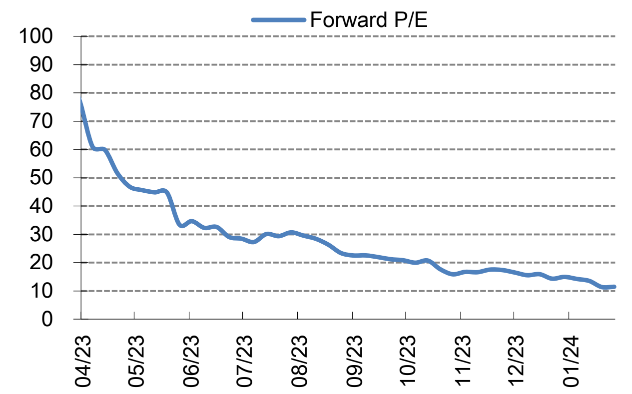
Maintain **BUY** with a revised DCF-based TP of HK$ 65. Our TP implies 14.9x 2025E core P/E. After recent share price corrections, the counter is currently trading at about 10x 2025E core P/E, which is undemanding in our view. As the business is still turning to profit, we think the counter's valuation foundation is moving from P/S to P/E basis.

Exhibit 24: P/S trend



Source(s): Bloomberg, ABCI Securities

Exhibit 25: Forward P/E trend



Source(s): Bloomberg, ABCI Securities

Exhibit 26: DCF sensitivity (in HK$)

		WACC				
		13%	**14%**	**15%**	**16%**	**17%**
Terminal growth	**2.0%**	77	69	62	56	51
	2.5%	79	70	63	57	52
	3.0%	81	72	65	58	53
	3.5%	84	74	66	60	54
	4.0%	86	76	68	61	55

Source (s): ABCI Securities estimates

Exhibit 27: TP changes (HK$ per share)

Old	New	Comment
85	**65**	DCF-based; TP implies 14.9x 2025E P/E vs. 26.8x 2024E P/E previously on 15% WACC versus 13% previously reflecting overall weaker market sentiment on the sector

Source(s): ABCI Securities estimates

Company profile

Business
• Second-largest short video and live-streaming platform in China. According to Questmobile, its MAU was ~62% of that of its closest peer Douyin in Sep 2023 • Successfully leverage its user traffic into live-streaming e-commerce in recent years. It's now **one of the three major live-streaming platforms in China** (Alibaba, Douyin, and Kuaishou) with an estimated market share of mid-single digits in the entire e-commerce market. E-commerce GMV achieved strong growth in recent years • **The GMV mix of the company has been diversified.** The share of mid-tier and long-tail KOLs in the total KOL-related GMV has climbed to almost 50% as of 3Q23**,** compared to more than 20% at the start of 2021 • Introduction of **shelf-space e-commerce**. In 3Q23, shelf-based e-commerce accounted for about 20% of total GMV • Exploring opportunities in the **local service** segment in lower tier cities • Rising competition with Weixin's Video Account, which has seen rising popularity • Developing AIGC technology to enhance user experience and long-term competitiveness
Financials
• **Revenue mix:** Online marketing is the major revenue contributor in 2022 (52%), followed by live streaming (38%) and others (mainly e-commerce related) (10%) • Online marketing businesses consist o**f e-commerce related advertising** (advertising by merchants in its e-commerce platform) and **external advertising** (advertising by brands, etc.) • Segment revenue growth was mainly driven by e-commerce related advertising in recent quarters • We estimate that the **share of revenue related to e-commerce activities** (online advertising spending, service charges, etc. by e-commerce merchants) are broadly in the 30s range • **Improving profitability** in recent quarters mainly by **rationalizing selling and marketing expenses** • Domestic business currently achieves a positive operating profit, while overseas business is still loss-making • Clean balance sheet with about RMB 30bn in cash and deposits and no debts in Sep 2023
Management and shareholder
• Co-founders Su Hua and Cheng Yixiao, which collectively owned 17.6% of economic interest and about 68.1% voting right of the Company via **dual-class shareholding structure** • **Change of Chairman:** In Oct 2023, Kuaishou announced that Su Hua ceased to be the Chairman and that Cheng Yixiao, the current CEO, would take up the Chairman role • A strategic investor (major online platform in China) holds c. 15.6% stakes
Shareholders' return
• **No dividend** record since listing • **Share repurchase** in recent months. In 3Q23, the company repurchased HK$ 680mm worth of shares
Corporate governance/information disclosure
• Various corporate social responsibilities initiatives in recent years

Financial Forecast

Consolidated income statement (2022A-2025E)

FY Ended Dec 31 (RMB mn)	2022A	2023E	2024E	2025E
Total revenue	**94,183**	**113,473**	**130,512**	**143,057**
Cost of sales	(52,051)	(56,736)	(63,951)	(70,098)
Gross profit	**42,131**	**56,736**	**66,561**	**72,959**
Selling and Marketing expenses	(37,121)	(36,311)	(40,459)	(41,487)
General & admin expenses	(3,921)	(3,631)	(3,654)	(3,576)
R&D	(13,784)	(13,049)	(14,356)	(14,306)
Other income/losses	137	800	700	700
Operating Profits	**(12,558)**	**4,545**	**8,792**	**14,290**
Net finance expenses	166	400	450	450
FV change of CB	0	0	0	0
Others, net	(139)	(50)	(50)	(50)
PBT	**(12,531)**	**4,895**	**9,192**	**14,690**
Income tax benefits	(1,158)	(734)	(1,379)	(2,130)
PAT	**(13,689)**	**4,160**	**7,813**	**12,560**
Minority interests	1	0	0	0
Profits attributable to shareholders	**(13,690)**	**4,160**	**7,813**	**12,560**
Share-based compensation	6,249	4,000	4,500	4,500
Impairment/FV changes of CB	0	0	0	0
Other non-core items	1,689	0	0	0
Non-GAAP profits attributable to shareholders	**(5,753)**	**8,160**	**12,313**	**17,060**
Growth				
Total revenue (%)	16.2	20.5	15.0	9.6
Gross Profits (%)	23.8	34.7	17.3	9.6
Operating Profits (%)	NA	NA	93.5	62.5
Net profit (%)	NA	NA	87.8	60.8
Non-GAAP net profit (%)	NA	NA	50.9	38.6
Operating performance				
Operating margin (%)	(13.3)	4.0	6.7	10.0
Net margin (%)	(14.5)	3.7	6.0	8.8
Core net margin (%)	(6.1)	7.2	9.4	11.9
ROAE (%)	NA	18.6	22.7	24.8
ROAA (%)	NA	8.7	11.6	14.0

Source(s): The Company, ABCI Securities estimates

Notes: Individual items may not sum to total due to rounding differences
Individual items may varies from reported figures due to rounding differences/definition differences

Consolidated balance sheet (2022A-2025E)

As of Dec 31 (RMB mn)	2022A	2023E	2024E	2025E
Fixed assets	25,143	25,643	26,143	26,643
Investments	4,564	9,778	15,004	20,004
Other non-current assets	13,742	14,390	15,071	15,071
Total non-current assets	**43,449**	**49,812**	**56,218**	**61,718**
Cash & equivalents	13,274	11,293	13,483	20,043
Short-term deposit	8,318	8,318	8,318	8,318
Financial assets	13,814	18,814	23,814	28,814
Account receivables	6,288	6,602	6,933	6,933
Other current assets	4,165	4,370	4,586	4,586
Total current assets	**45,859**	**49,398**	**57,133**	**68,693**
Total assets	**89,307**	**99,209**	**113,351**	**130,411**
Account payables	33,058	34,201	35,402	35,402
Other current liabilities	7,652	7,814	7,984	7,984
Total current liabilities	**40,710**	**42,015**	**43,386**	**43,386**
Borrowings and notes	-	-	-	-
Other non-current liabilities	8,760	9,196	9,654	9,654
Total non-current liabilities	**8,760**	**9,196**	**9,654**	**9,654**
Total liabilities	**49,469**	**51,211**	**53,039**	**53,039**
Equity attributable to shareholders	39,830	47,990	60,303	77,363
Non-controlling interests	8	8	8	8
Total equity	**39,838**	**47,998**	**60,311**	**77,371**

Source(s): The Company, ABCI Securities estimates

Notes: Individual items may not sum to total due to rounding differences
Individual items may varies from reported figures due to rounding differences/definition differences

Consolidated cash flow statement (2022A-2025E)

As of Dec 31 (RMB mn)	2022A	2023E	2024E	2025E
Net profit	(13,689)	4,160	7,813	12,560
Depreciation and amortization	6,573	7,000	7,000	7,000
Share-based compensation	6,249	4,000	4,500	4,500
Other operating cash flow	3,065	359	377	-
Operating cash flow	**2,198**	**15,519**	**19,690**	**24,060**
Capital expenditure	(4,619)	(7,500)	(7,500)	(7,500)
Other investment cash flow	(12,929)	(5,000)	(5,000)	(5,000)
Investing cash flow	**(17,548)**	**(12,500)**	**(12,500)**	**(12,500)**
Financing cash flow	**(4,482)**	**(5,000)**	**(5,000)**	**(5,000)**
Effective of FX	494	-	-	-
Net cash flows	**(19,338)**	**(1,981)**	**2,190**	**6,560**

Source(s): The Company, ABCI Securities estimates

Notes: Individual items may not sum to total due to rounding differences
Individual items may varies from reported figures due to rounding differences/definition difference

Meituan-W (3690 HK)

Mixed outlook

- Moderating growth outlook due to less favorable base, ongoing competition, and weaker demand amid a softening economy
- Margin pressure in core local commerce cushioned by narrowing losses of new initiatives
- Trim TP to HK$ 110 amid near-term operational headwinds

Company Report

Rating: BUY

TP: HK$ 110

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

A moderating outlook ahead. We overall see a less favorable outlook in 2024E-25E due to 1) higher comparison base for hotel/travel which experienced strong growth in 2023E driven by pent-up demand during COVID; 2) Softer demand for food delivery amid a slowing economy that necessitates user subsidies/incentives to stimulate growth; 3) Competition from short-video platforms especially in the in-store segment. As a result, we expect revenue growth to moderate to 15% CAGR in 2024E-25E.

Resilient margins. We expect operating margin of core local commerce to moderate to 16.2% in 2025E due to increased customer incentives amid stiff competition. We expect profits of new initiatives to improve on cost control, alleviating partially the margin pressure of core local commerce. We estimate core net margin to increase to 9.6% in 2025E.

Recommendation. We trim our DCF-based TP to HK$110 due to near-term margin pressure of the core local commerce segment. Our TP implies 17.7x 2025E core P/E. After recent share price correction, the counter is trading towards the low-end of its historical range. In our view, extent and pace for valuation recovery in coming months would depend on 1) overall market sentiment; 2) near-term business outlook; 3) development of the company's share repurchase plan of up to US$ 1bn.

Share price (HK$)	87.8
Est. share price return	25.3%
Est. dividend yield	NA
Est. total return	25.3%
Previous Rating &TP	BUY/HK$190
Previous Report Date	Aug 30, 2023

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L(HK$)	150.0/61.1
Issued shares (mn)	6,244
of which	
Listed B shares (mm)	5,640
Unlisted shares (mm)	604
B share market cap (HK$ mn)	495,192
Avg daily turnover (HK$ mn)	3,253
Major shareholder(s)	**Voting right**
Wang Xing	41.8%

Source(s): Bloomberg, Company, ABCI Securities

Results and Valuation

FY end Dec 31	2022A	2023E	2024E	2025E
Revenue (RMB mn)	219,955	272,631	318,521	368,557
Chg (%,YoY)	*22.8*	*23.9*	*16.8*	*15.7*
Net profit (RMB mn)	(6,686)	10,752	16,989	24,488
Chg (%,YoY)	*NA*	*NA*	*58.0*	*44.1*
Core net profit (RMB mn)*	2,827	19,804	26,827	35,039
Chg (%,YoY)	*NA*	*NA*	*NA*	*NA*
EPS (RMB)	(1.1)	1.8	2.8	4.0
Chg (%,YoY)	*NA*	*NA*	*NA*	*NA*
Core EPS (RMB)*	0.5	3.2	4.4	5.7
Chg (%,YoY)	*NA*	*NA*	*NA*	*NA*
P/S (x)	2.2	1.8	1.6	1.3
Core P/E (x)*	NA	25.0	18.4	14.1
ROAE (%)	(5.3)	7.8	10.6	12.8
ROAA (%)	(2.8)	4.1	5.7	7.1

*Excl. share-based compensation, amortization, impairment, etc.
Source(s): Bloomberg, ABCI Securities estimates

Financial Outlook

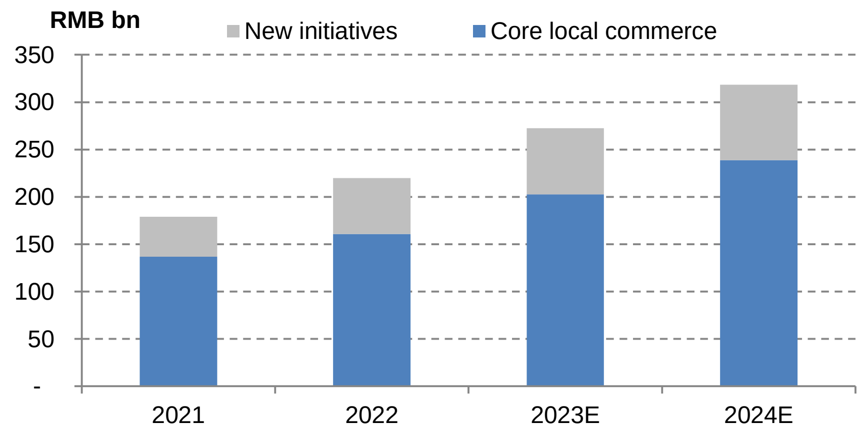
We expect revenue to grow at 16% CAGR in 2023-25E.

Core local commerce: We expect core commerce revenue (food delivery, Meituan Instashopping, in-store/hotel/travel, etc.) to grow at 17% CAGR in 2023-25E due to less favorable comparison base for Meituan Instashopping and hotel/travel and weaker demand on food delivery amid a moderating economy. For example, demand for food delivery in workplace could be affected but value-for-money services such as "Pin Hao Fan"("拼好飯") might help mitigating the impact.

For the sub-segments, we expect food delivery revenue CAGR in 2023E-25E to be in the mid-teens level, while revenue CAGR of Meituan Instashopping and in-store/hotel/travel to be in low-20s range during the same period.

New initiatives: We expect segment revenue to increase at 13% CAGR in 2023-25E. In our view, Meituan Select and Meituan Grocery are likely to see flatter growth due to "de-stocking" effect of food and groceries items post-COVID as well as adjustment in business strategy. In addition, other new initiatives such as ride-sharing have recently seen business mix changes (1P vs. 3P) which would result in lower reported growth ahead.

Exhibit 28: Revenue trend



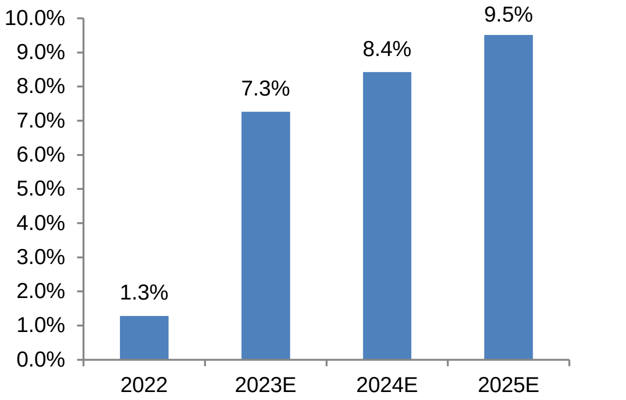
Source(s): Company, ABCI Securities estimates

In terms of segment profitability, we expect operating margin of core local commerce to moderate 16.2% in 2025E due to rising competition from short-video platforms as well as increased customer incentives, but increased labor supply for delivery rider would help counteract the impact on margins. We factor in low-teens operating margins for food delivery and low-30s operating margins for in-store/hotel/travel in 2024E-25E.

We expect new initiatives to continue to improve its profitability due to cost control, reducing the margin pressure from core local commerce. Operating losses of new initiatives would narrow to RMB 15.4bn in 2025E.

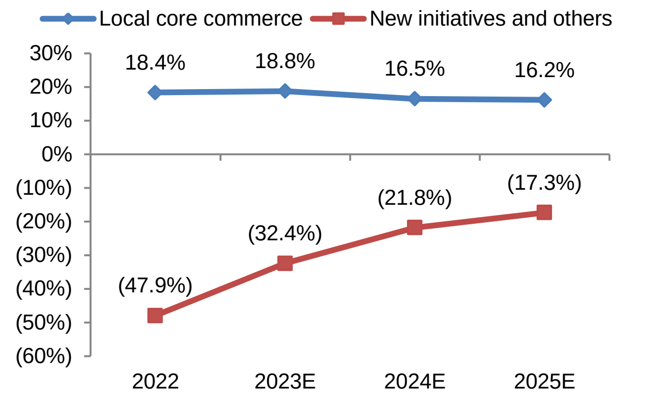
We estimate core net margin to increase to 9.5% in 2025E.

Exhibit 29: Core net margin



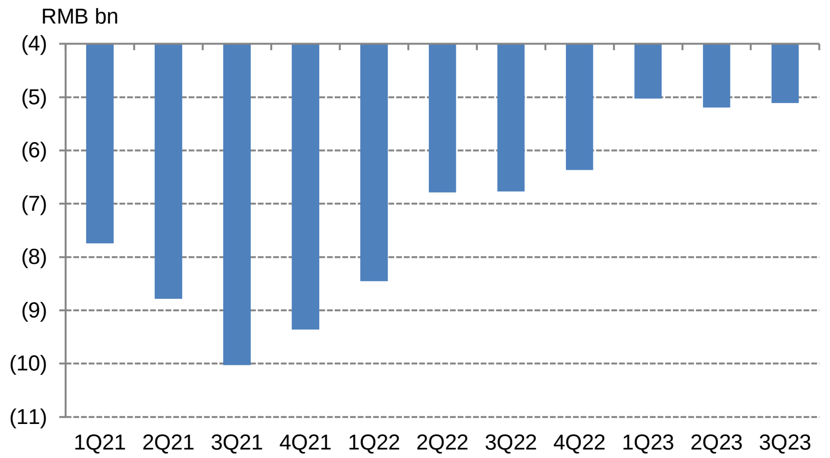
Source(s): Company, ABCI Securities estimates

Exhibit 30: Segment operating profit margin



Source(s): Company, ABCI Securities estimates

Exhibit 31: Operating losses – New initiatives



Source(s): Company, ABCI Securities

Exhibit 32: Forecast changes

	2023E			
RMB mn	Old	New	Diff	Comment
Revenues	272,667	272,631	0.0%	
Core profit	20,180	19,804	-1.9%	Cost pressure

Source(s): ABCI Securities estimates

Exhibit 33: Forecast changes

	2024E			
RMB mn	Old	New	Diff	Comment
Revenues	318,227	318,521	0.1%	
Core profit	27,706	26,827	-3.2%	Cost pressure

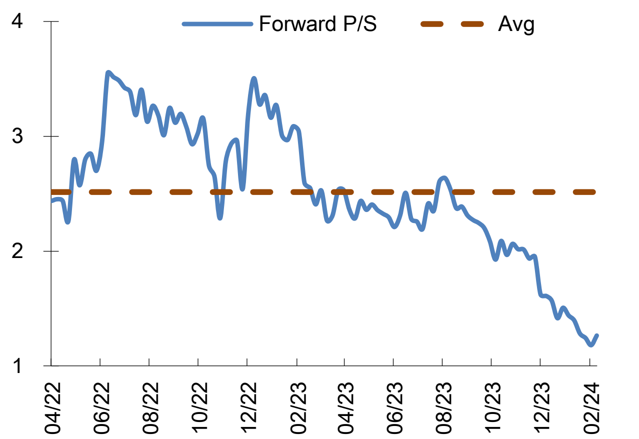
Source(s): ABCI Securities estimates

Valuation and TP

We trim our DCF-based TP to HK$110 to due to near-term macro headwinds, which could lead pressure margins of the core local commerce segment. Our TP implies 17.7x 2025E core P/E.

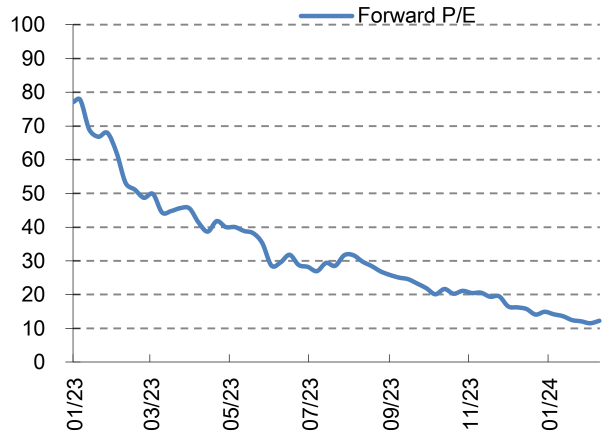
After recent share price correction, the counter is trading at towards the low-end of its historical range. In our view, current valuation has priced in a moderating near-term growth outlook. In our view, potential room and pace for valuation recovery in coming months would depend on 1) overall market sentiment; 2) near-term business outlook; 3) development of the company's potential share repurchase plan of up to US$ 1bn.

Exhibit 34: P/S



Source(s): Bloomberg, ABCI Securities

Exhibit 35: Forward core P/E



Source(s): Bloomberg, ABCI Securities

Exhibit 36: DCF sensitivity (in HK$)

		WACC				
		14.0%	15.0%	16.0%	17.0%	18.0%
Terminal growth	2.0%	132	117	105	95	86
	2.5%	135	120	107	97	88
	3.0%	139	123	110	99	89
	3.5%	143	126	112	101	91
	4.0%	148	130	115	103	92

Source (s): ABCI Securities estimates

Exhibit 37: TP changes (HK$ per share)

Old	New	Remark
190	110	DCF-based TP implies 17.7x 2025E core P/E vs. 2.2x 2024E P/S previously on revised financial forecast as well as higher WACC (16% vs. 14% previously) reflecting overall weaker market sentiment on the sector

Source(s): ABCI Securities estimates

Company profile

Business
• **Largest local service platform in China**; Core local commerce (on-demand delivery and in-store/hotel/travel) revenue size about 3x vs. Alibaba's Ele.me in 2022 • **Business segment** - **Core local commerce** mainly includes the Food delivery and In-store, hotel & travel segments, Meituan Instashopping (美团闪购), alternative accommodations and transportation ticketing; **New initiatives** mainly includes Meituan Select (美团优选), Meituan Grocery (美团买菜), B2B food distribution (快驴), ride sharing, and other new initiatives • 678mn annual transacting users and 9.3mn active merchants at end-2022 • **Platform based business model** that does not bear inventories. Its on-demand delivery network is co-operated with delivery partners who are responsible for recruiting riders and other day-to-day management • Actively expanding into community group purchase and grocery in recent years • In-store segment faces rising **competition from short video platforms**
Financials
• Core local commerce accounted for 73% of revenue in 2022, while new initiatives accounted for the remaining 27%. • Core local commerce is the profit contributor with operating margin at around 20% in recent quarters • **New initiatives are still loss-making** but its operating losses are narrowing in recent quarters. • Sales and marketing expenses are the largest cost item accounting for about 18% of revenue in recent quarters mainly due to price subsidies and incentives for consumers • The company has achieved **positive core net profit** since 2Q22 • Overall **strong liquidity position** with RMB 25bn cash and RMB 108bn short-term treasury investment against RMB 57bn debts at Sept 2023 • The company raised USD10bn via share placement and convertible bonds in Apr 2021 • Meituan holds about **15.1% stake in Li Auto**
Management and shareholder
• Wang Xing currently hold ~41.8% of voting right of the company • Wang Xing is also a **major investor of Li Auto** with a 21.79% stake • Co-founder Wang Huiwen retired from management role at Meituan in 2020. He further resigned from his non-executive director role in June 2023 • **Divestment risk** from strategic investors
• **Shareholders' return**
• The company plans to share repurchase of up to US$ 1bn to enhance shareholders' return
• **Corporate governance/information disclosure**
• RMB3.4bn in **antitrust fine** in 2021 • The company acquired Mobike, a bike-sharing platform, for US$ 2.7bn in Apr 2018 but decided to book **RMB 1.7bn impairment related to bike-sharing/Mobike** in Mar 2019 • The company **acquired AI start-up Light Year** founded by Meituan's co-founder and ex-director Wang Huiwen for US$ 281mn in Jun 2023 • Less disclosure on operational and financial metrics such as GTV, food delivery and in-store/hotel/travel segment revenue, etc. in recent years • Various ESG initiatives in recent years

Financial Forecast

Consolidated income statement (FY22A-FY25E)

FY Ended Dec 31 (RMB mn)	FY22A	FY23E	FY24E	FY25E
Total revenue	**219,955**	**272,631**	**318,521**	**368,557**
Cost of sales	(158,202)	(179,937)	(210,861)	(245,091)
Gross profit	**61,753**	**92,695**	**107,660**	**123,467**
Other gains/losses	3,152	4,500	4,500	4,500
Selling & marketing expenses	(39,745)	(54,526)	(62,111)	(68,183)
R&D expenses	(20,740)	(21,810)	(22,296)	(23,956)
General & admin expenses	(9,772)	(8,997)	(9,237)	(9,582)
Impairment	(469)	(500)	(500)	(500)
Operating Profits	**(5,820)**	**11,361**	**18,015**	**25,745**
Finance income, net	(971)	(500)	(500)	(500)
Share of gains of investments	36	0	0	0
Profit before tax	**(6,756)**	**10,861**	**17,515**	**25,245**
Tax	70	(109)	(525)	(757)
Profit after tax	**(6,686)**	**10,752**	**16,989**	**24,488**
Minority interests	0	0	0	0
Profit attributable to shareholders	**(6,686)**	**10,752**	**16,989**	**24,488**
Share-based compensation	8,743	8,452	9,237	9,951
Amortization and impairment	471	600	600	600
Adjustments on disposals/revaluation	193	0	0	0
Other adjustments	105	0	0	0
Core net profit	**2,827**	**19,804**	**26,827**	**35,039**
Growth				
Total revenue (%)	22.8	23.9	16.8	15.7
Gross Profits (%)	45.4	50.1	16.1	14.7
Operating Profits (%)	NA	NA	58.6	42.9
Net profit (%)	NA	NA	58.0	44.1
Core profit (%)	NA	600.6	35.5	30.6
Operating performance				
Operating margin (%)	(2.6)	4.2	5.7	7.0
Net margin (%)	(3.0)	3.9	5.3	6.6
Core net margin (%)	1.3	7.3	8.4	9.5
ROAE (%)	(5.3)	7.8	10.6	12.8
ROAA (%)	(2.8)	4.1	5.7	7.1

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

Consolidated balance sheet (FY22A-FY25E)

As of Dec 31 (RMB mn)	FY22A	FY23E	FY24E	FY25E
Fixed assets	22,201	18,701	15,001	11,301
Intangible assets	30,643	31,143	31,643	32,143
Investment in associates and JV	23,187	28,187	33,187	38,187
Financial assets	18,904	19,849	19,849	19,849
Other non-current assets	6,400	6,645	6,645	6,645
Total non-current assets	**101,335**	**104,525**	**106,325**	**108,125**
Cash & equivalents	20,159	49,512	87,051	133,084
Restricted cash	14,606	15,336	15,336	15,336
Account receivables	2,053	2,988	3,491	4,039
Deposit, prepayments and other assets	13,293	13,957	13,957	13,957
Inventories	1,163	1,673	1,954	2,261
Short term investment	91,873	91,873	91,873	91,873
Total current assets	**143,146**	**175,338**	**213,662**	**260,550**
Total assets	**244,481**	**279,864**	**319,988**	**368,676**
Accounts payable	17,379	23,155	27,052	31,302
Borrowings and notes	17,562	22,562	27,562	32,562
Deferred revenue	5,053	5,306	5,306	5,306
Other current liabilities	36,435	36,543	36,543	36,543
Total current liabilities	**76,430**	**87,566**	**96,464**	**105,714**
Deferred revenue	-	-	-	-
Borrowings	35,156	40,156	45,156	50,156
Other non-current liabilities	4,189	4,231	4,231	4,231
Total non-current liabilities	**39,345**	**44,387**	**49,387**	**54,387**
Total liabilities	**115,774**	**131,953**	**145,851**	**160,101**
Net current assets	**66,716**	**87,772**	**117,198**	**154,837**
Equity attributable to shareholders	128,762	147,966	174,192	208,631
Non-controlling interests	(56)	(56)	(56)	(56)
Total equity	**128,706**	**147,910**	**174,136**	**208,575**

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 (FY22A-FY25E)

As of Dec 31 (RMB mn)	FY22A	FY23E	FY24E	FY25E
PBT	(6,756)	10,861	17,515	25,245
Depreciation and amortization	9,730	9,500	9,700	9,700
Other operating cash flow	9,250	8,343	8,712	9,194
Change in working capital	(813)	3,094	3,113	3,394
Operating cash flow	**11,411**	**31,798**	**39,040**	**47,533**
Acquisition of fixed asset	(5,731)	(6,000)	(6,000)	(6,000)
Purchase of investment	(7,782)	(5,000)	(5,000)	(5,000)
Other investment cash flow	(1,201)	(1,445)	(500)	(500)
Investing cash flow	**(14,714)**	**(12,445)**	**(11,500)**	**(11,500)**
Financing cash flow	**(9,990)**	**10,000**	**10,000**	**10,000**
Net cash flows	**(13,292)**	**29,353**	**37,540**	**46,033**

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

NetEase (9999 HK/NTES US)

An incumbent in online games

- Second-largest online gaming player in China with solid R&D record; market share gains in recent years
- Comprehensive gaming portfolio to support future growth
- Reasonable valuation for long-term investment

Company Initiation

Rating: BUY
Rating (S-share): BUY
TP (S-share): HK$ 200
Rating (ADR): BUY
TP (ADR): US$ 128

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

Leading online gaming play with solid R&D record. Having established a robust portfolio of in-house games, NetEase stands as the second-biggest participant in China's online gaming industry. Over the years, it has developed various blockbusters such as “Fantasy Westward Journey” and the “Westward Journey” series. We estimate its online gaming revenue is currently at about 40% of that of the top online gaming platform in China, up from roughly 35% in 2020, due to the continued development of its gaming portfolio. This indicates a narrowing of the market share gap during the period.

Comprehensive gaming portfolio. In recent months, the company's classic main game, "Fantasy Westward Journey" (FWJ), remained in the top 10 in terms of revenue in China’s iPhone platform. Furthermore, two recently released games, "Justice Mobile" and "Egg Party," had great performances and entered the top 10 in 2023 in China’s iPhone platform. Supported by a comprehensive gaming portfolio, we expect a 11% CAGR in revenue growth for 2023E-25E.

Initiate BUY with DCF-based TP at HK$ 200 for NetEase-S (9999 HK) and US$ 128 for NetEase-ADR (NTES US). Its current valuation is below the average of its historical range, presents a reasonable entry point for long-term investors in our view. Compared with other major gaming companies, such as Activision Blizzard (ATVI US) and Electronic Arts (EA US), NetEase’s current valuation represents good relative value, in our view.

Price (ADR/S-share)	US$105.9/ HK$166.9
Est. share price return (ADR/S-share)	20.9%/19.8%
Est. dividend yield (ADR/S-share)	2.7%/2.8%
Est. total return (ADR/S-share)	23.6%/22.6%
Last Rating &TP (ADR/S-share)	NA
Previous Report Date	NA

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L (HK$) (S-share)	185.7/116.1
52Wk H/L (US$) (ADR)	118.8/76.8
Issued shares (mn)	3,213
Market cap (HK$ mn)	546,250
3-mth avg daily turnover (HK$ mn) (S-share)	1,221
3-mth avg daily turnover (US$ mn) (ADR)	233
Major shareholder(s) (%):	
Shinning Globe International	45.0%

Source(s): Bloomberg, HKEx, Company

Results and Valuation

FY end Dec 31	2022	2023	2024E	2025E
Revenue (RMB mn)	96,496	103,468	115,807	128,255
Chg (%,YoY)	*10.1*	*7.2*	*11.9*	*10.7*
Net profit (RMB mn)	19,713	29,417	32,112	35,185
Chg (%,YoY)	*16.9*	*49.2*	*9.2*	*9.6*
Core net profit (RMB mn)*	22,808	32,608	35,312	38,385
Chg (%,YoY)	*15.4*	*43.0*	*8.3*	*8.7*
EPS (RMB)	6.0	9.1	10.0	10.9
Core EPS (RMB)*	7.0	10.1	11.0	11.9
Core P/E (x)-S share	22.0	15.1	14.0	12.9
Core P/E (x)-ADR	25.5	16.7	15.3	13.9
Dividend yield (%) -S share	1.4	2.0	2.8	3.1
Dividend yield (%) -ADR	1.3	1.8	2.7	2.9
ROAE (%)	21.9	27.6	25.4	23.7
ROAA (%)	14.0	18.2	18.1	17.9

1 ADR = 5 ordinary shares
*Excluding share-based compensation, impairments, fair value changes of investment, etc.
Source (s): Bloomberg, ABCI Securities estimates

An incumbent in online games

NetEase is the second-largest player in China's online gaming market with a strong track record of developing in-house games. Over the years, it has created various blockbusters such as "Fantasy Westward Journey" (FWJ, 梦幻西游) and "Westward Journey" (大话西游) series, and has a track record of maintaining a long life cycle for its legacy games.

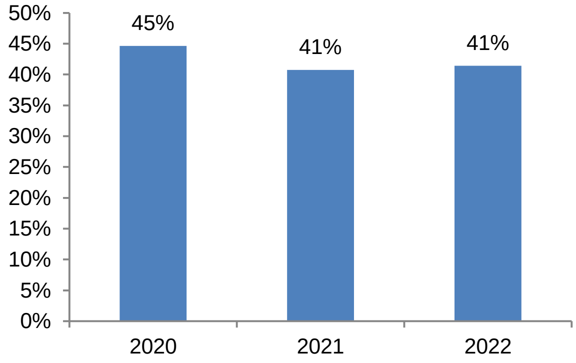
Based on our estimates, its online gaming revenue reached about 40% of that of China's largest online gaming platform in 2022, up from 35% in 2020, thanks to its expanding gaming portfolio. This implies a rather swift market share gain during the period.

In our view, regulatory hurdle on new game approvals and long development cycles of blockbuster games have discouraged potential new entrants such as short-video platforms, resulting in a largely stable competitive environment in recent years.

The company has diversified its gaming revenue away from established flagship titles (such as FWJ) in recent years by co-operating with external parties such as Blizzard, Marvel, Microsoft (MSFT US), and Warner Bros. (WBD US) to co-develop/operate games such as "Diablo Immortal", "MARVEL Super War", "Marvel Duel", "Harry Potter: Magic Awakened", as well as developing new in-house franchises, including "Onmyoji", "Identity V", and "Egg Party".

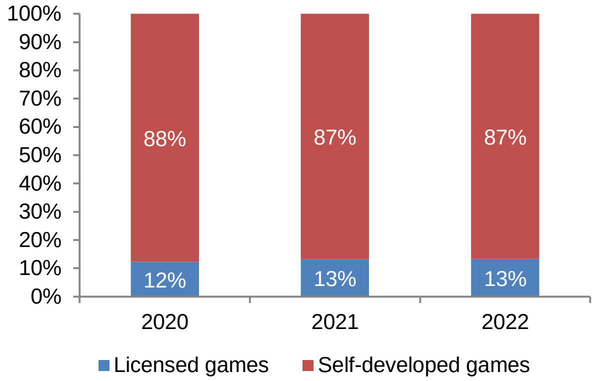
As a result, it managed to lower the contribution of top five games to ~41% of total online gaming revenue in 2022 vs. 45% in 2020. Contribution from licensed games remained at ~13% in recent years, which reduces its exposure to license renewal risk. For example, its license agreement with Blizzard ended in Jan 2023, and the impacted titles only had a low-single-digit contribution to revenue.

Exhibit 38: Online gaming revenue – top five games contribution



Source(s): Company, ABCI Securities

Exhibit 39: Online gaming revenue mix

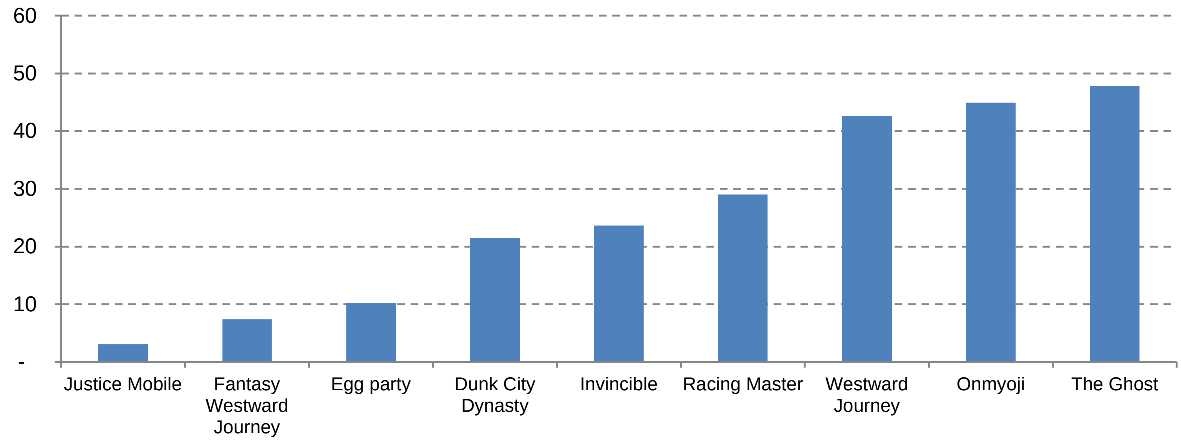


Source(s): Company, ABCI Securities

Among its major mobile games, its evergreen game FWJ has maintained a top 10 position in the revenue ranking in China's iPhone platform. In addition, its newly released games, including "Justice Mobile", "Dunk City Dynasty", and "Egg Party", entered the top 20 position in China's iPhone platform in 2023. These new games would be a major near-term growth driver. Among the new games, "Justice Mobile", an open world MMORPG, uses machine-learning technology in game development to enhance user experience. E.g., it provides computer-generated non-player characters that engage with players and influence the game's storyline.

Other incumbent games such as “Invincible”, “Western Journey”, “Onmyoji”, and “The Ghost” generally were within the top 50 positions in China’s iPhone platform in 2023, making steady contribution to the company.

Exhibit 40: Average daily revenue ranking of NetEase’s major mobile games (2023)



Source(s): Qimai, ABCI Securities

Note: China’s iPhone platform

Investing in overseas expansion

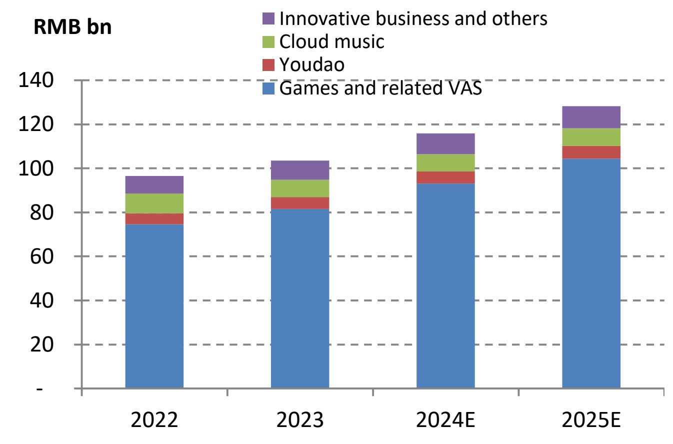
Internationally, the company has launched various key titles overseas, such as “Knives Out”, “Identity V”, “MARVEL Super War”, “The Lord of the Rings: Rise to War”, “Naraka: Bladepoint”, etc. in recent years. To expand its overseas market, the company has acquired or set up various overseas studios in recent years to strengthen its R&D capabilities. NetEase currently has over 10 games studios overseas in Japan, the US, Canada, and Europe.

Financial Outlook

We expect revenue to grow at 11% CAGR in 2023-25E manly driven by 13% CAGR of games and related VAS revenue. In particular, we expect mobile game revenue to expand at 16% CAGR based on the new game launch, while PC and console games would increase at 5% CAGR during the same period.

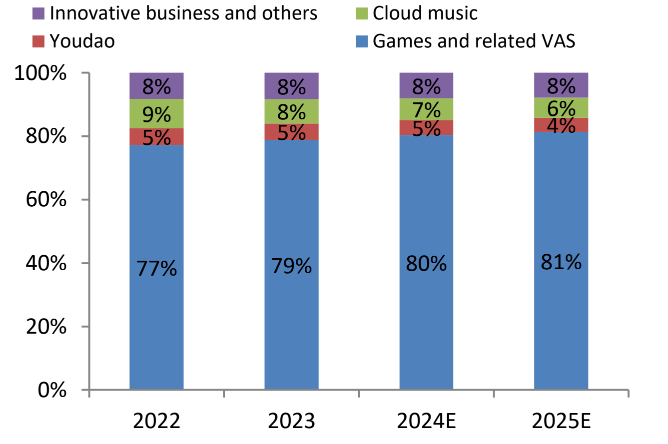
Among its major mobile games, recently launched games including “Justice Mobile”, “Dunk City Dynasty”, and “Egg Party” have been gaining traction in recent months, and we expect them to be a major growth driver in the near term, while incumbent games such as “Invincible”, “Western Journey”, “Onmyoji”, and “The Ghost” would continue to make steady contribution to the company. Key new games in the pipeline include “Where Winds Meet”, “Condor Heroes”, and “Naraka Bladepoint mobile”.

Exhibit 41: Revenue outlook



Source(s): Company, ABCI Securities estimates

Exhibit 42: Revenue mix outlook



Source(s): Company, ABCI Securities estimates

We expect gross margin to improve to 61.5% in 2025E due to lower contribution from lower-margin games, such as licensed games, and optimization of channel mix (official channels vs. iOS/Android).

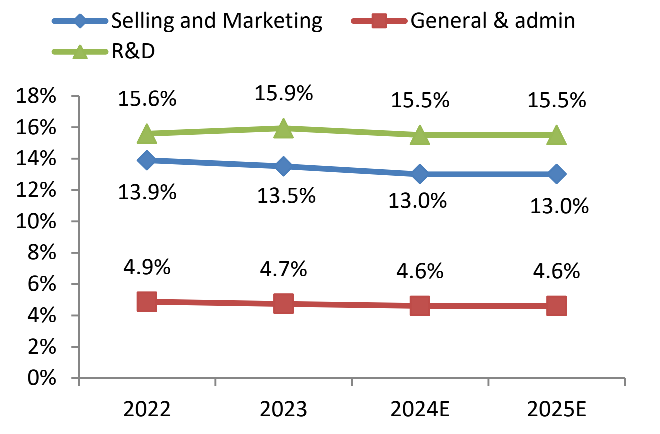
Selling and marketing expenses: We expect selling and marketing expenses/revenue ratio to be stable at 13.0% in 2024-25E.

General and admin expenses: Thanks to the higher economies of scale and operational improvement, we expect general and admin cost-to-revenue ratio to drop to 4.6% in 2025E.

R&D: We expect R&D cost-to-revenue ratio to be at 15.5% in 2024-25E since the company continues to invest in gaming development.

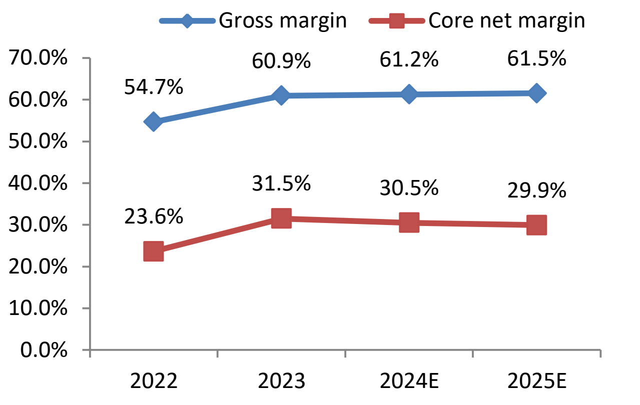
As a result, we expect core net profit to increase at 8% CAGR in 2023-25E.

Exhibit 43: Cost trend (as a % of revenue)



Source(s): Company, ABCI Securities estimates

Exhibit 44: Margin trend



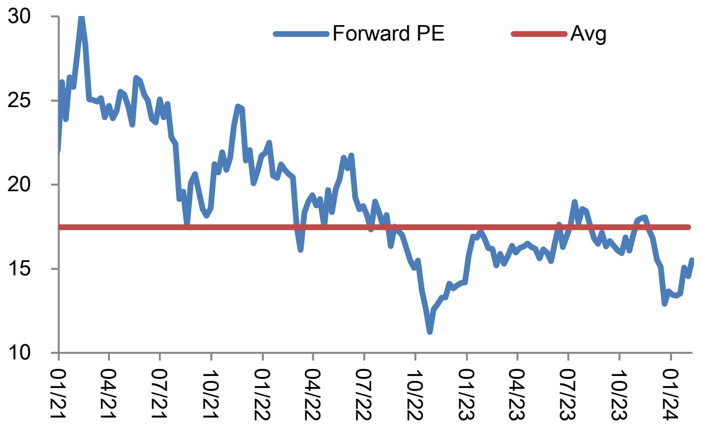
Source(s): Company, ABCI Securities estimates

Valuation and TP

Initiate **BUY** with DCF-based TP at HK$ 200 for NetEase-S (9999 HK) and US$ 128 for NetEase-ADR (NTES US) (1 ADR represents 5 shares). Our TP implies 17.8x 2024E core P/E.

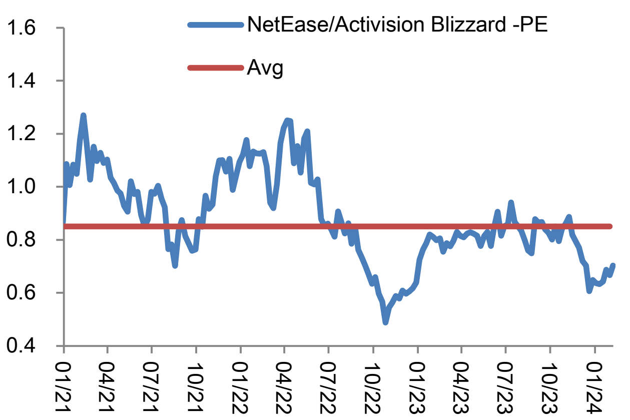
We believe NetEase's current valuation presents a reasonable entry point for long-term investors. Compared with other major gaming companies such as Activision Blizzard (ATVI US) and Electronic Arts (EA US), NetEase's current valuation also represents a good relative value, in our view.

Exhibit 45: NetEase – forward P/E



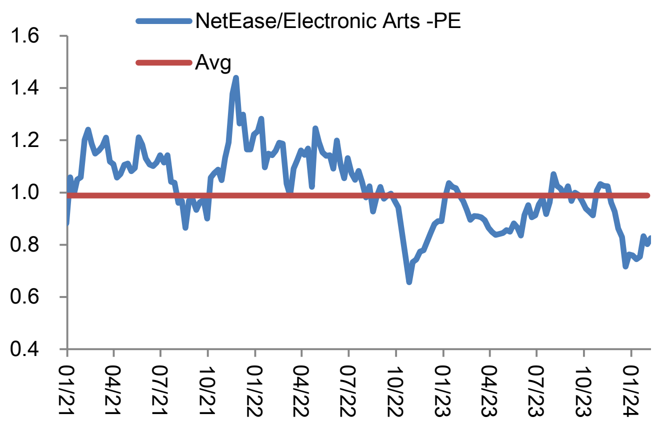
Source(s): Bloomberg, ABCI Securities

Exhibit 46: Relative value against Activision Blizzard



Source(s): Bloomberg, ABCI Securities

Exhibit 47: Relative value vs. Electronic Arts



Source(s): Bloomberg, ABCI Securities

Exhibit 48: DCF sensitivity (in HK$)

		WACC				
		10%	**11%**	**12%**	**13%**	**14%**
Terminal growth	**2.0%**	232	210	192	177	165
	2.5%	239	215	195	180	167
	3.0%	247	220	200	183	170
	3.5%	257	227	204	187	172
	4.0%	267	234	210	190	175

Source (s): ABCI Securities estimates

Company profile

Business
• Second-largest player in China's online gaming market with a strong track record of self-developed games. Over the years, it has created various blockbusters such as "Fantasy Westward Journey" (FWJ, 梦幻西游) and "Westward Journey" (大话西游) series • We estimate its online gaming revenue is currently about 40% of that of the largest online gaming platform in China, up from about 35% in 2021 • The company has diversified its gaming revenue away from established flagship titles in recent years by co-operating with external parties such as Blizzard, Marvel, Microsoft (MSFT US), and Warner Bros. (WBD US) to co-develop/operate games such as "Diablo Immortal", "MARVEL Super War", "Marvel Duel", "Harry Potter: Magic Awakened", as well as developing new in-house franchises such as "Onmyoji", "Identity V", and "Egg Party" • To expand its overseas market, the company has acquired or set up various overseas studios in recent years to strengthen its R&D capabilities. NetEase currently has over 10 games studios overseas in Japan, the US, Canada, and Europe • It managed to lower the contribution of top five games to ~41% of total online gaming revenue in 2022 vs. 45% in 2020. On the other hand, contribution from licensed games remained at a low level at ~13% in recent years, which reduces license renewal risk • NetEase's Cloud Music (9899 HK) is a music streaming and social entertainment platform in China. It accounted for about 8% of NetEase's revenue in 2023 • Youdao (DAO US) is an online learning platform in China providing various online learning tools, online STEAM course, and smart devices such as dictionary pen, learning pads, etc. It accounted for about 5% of NetEase's revenue in 2023
Financials
• Gaming and related value added service is a major revenue contributor accounting for ~ 80% of total revenue, while non-gaming businesses including Youdao, Cloud music, and innovative business collectively accounting for the remaining c. 20% • R&D expense is the largest cost item accounting for c. 15%-16% of revenue, followed by selling and marketing expenses (c.14% of revenues) • Gaming business is the major profit driver, as profitability of Cloud music and Youdao is still weak at the moment
Management and shareholder
• William Lei Ding, founder and CEO, owns 45.0% of the company
Shareholders' return
• Dividend payout of ~ 30% • USD5bn share repurchase program from Jan 2023 to Jan 2026 with USD644m utilized as of end-2023.
Corporate governance/information disclosure
• In Jun 2022, NetEase delayed the launch of "Diablo Immortal" China version after the game's Weibo account was suspended due to posting of "violation of relevant laws and regulations"

Financial Forecast

Consolidated income statement (2022A-2025E)

FY Ended Dec 31 (RMB mn)	2022	2023	2024E	2025E
Total revenue	**96,496**	**103,468**	**115,807**	**128,255**
Cost of sales	(43,730)	(40,405)	(44,882)	(49,350)
Gross profit	**52,766**	**63,063**	**70,926**	**78,905**
Selling and Marketing expenses	(13,403)	(13,970)	(15,055)	(16,673)
General & admin expenses	(4,696)	(4,900)	(5,327)	(5,900)
R&D	(15,039)	(16,485)	(17,950)	(19,879)
Operating profit	**19,629**	**27,709**	**32,594**	**36,452**
Investment income/losses	54	1,307	500	500
Net finance income	2,150	4,120	4,200	4,000
Others, net	2,418	921	700	700
PBT	**24,250**	**34,057**	**37,994**	**41,652**
Income tax benefits	(5,032)	(4,700)	(6,079)	(6,664)
PAT*	**19,218**	**29,357**	**31,915**	**34,988**
Accretion of redeemable non-controlling interests	(3)	(3)	(3)	(3)
Minority interests	497	63	200	200
Net profit*	**19,713**	**29,417**	**32,112**	**35,185**
Share-based compensation	3,096	3,191	3,200	3,200
Core net profit	**22,808**	**32,608**	**35,312**	**38,385**
Growth				
Total revenue (%)	10.1	7.2	11.9	10.7
Gross profit (%)	12.3	19.5	12.5	11.2
Operating profit (%)	19.6	41.2	17.6	11.8
Net profit (%)	16.9	49.2	9.2	9.6
Core net profit (%)	15.4	43.0	8.3	8.7
Operating performance				
Operating margin (%)	20.3	26.8	28.1	28.4
Net margin (%)	20.4	28.4	27.7	27.4
Core net margin (%)	23.6	31.5	30.5	29.9
ROAE (%)	21.9	27.6	25.4	23.7
ROAA (%)	14.0	18.2	18.1	17.9

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

Source(s): Company, ABCI Securities estimates

*continuing operations

Consolidated balance sheet (2022A-2025E)

FY Ended Dec 31 (RMB mn)	2022	2023	2024E	2025E
Fixed assets	10,464	12,150	13,150	15,150
Time deposit	2,974	1,050	1,050	1,050
Other non-current assets	27,720	30,032	31,456	32,950
Total non-current assets	**41,158**	**43,232**	**45,656**	**49,150**
Cash & equivalents	24,889	21,429	23,215	28,631
Short-term deposit	84,948	100,856	110,856	120,856
Short-term investment	7,623	4,436	6,436	8,436
Account receivables	5,003	6,422	6,744	7,081
Other current assets	9,141	9,549	10,460	11,508
Total current assets	**131,603**	**142,692**	**157,711**	**176,511**
Total assets	**172,760**	**185,924**	**203,366**	**225,662**
Account payables	6,240	5,738	925	971
Short term loans	23,876	19,240	14,240	12,240
Other current liabilities	26,713	28,864	33,849	33,984
Total current liabilities	**56,829**	**53,842**	**49,014**	**47,196**
Borrowings and notes	3,655	428	428	428
Other non-current liabilities	3,404	3,570	3,570	3,570
Total non-current liabilities	**7,059**	**3,998**	**3,998**	**3,998**
Total liabilities	**63,888**	**57,840**	**53,012**	**51,194**
Redeemable non-controlling interest	136	116	119	122
Equity attributable to shareholders	104,731	124,286	146,753	171,064
Non-controlling interests	4,006	3,683	3,483	3,283
Total equity	**108,737**	**127,968**	**150,235**	**174,346**

Individual items may varies from reported figures due to rounding differences/definition differences
Source(s): Company, ABCI Securities estimates

Consolidated cash flows statement (2022A-2025E)

FY Ended Dec 31 (RMB mn)	2022	2023	2024E	2025E
Net profit	19,218	29,357	31,915	34,988
Depreciation and amortization	2,858	3,055	3,000	3,000
Share-based compensation	3,174	3,243	3,200	3,200
Other operating cash flow	2,459	(323)	(2,484)	(2,699)
Operating cash flow	**27,709**	**35,331**	**35,631**	**38,489**
Capital expenditure	(2,100)	(2,302)	(4,000)	(5,000)
Other investment cash flow	(5,270)	(14,742)	(10,000)	(10,000)
Investing cash flow	**(7,370)**	**(17,043)**	**(14,000)**	**(15,000)**
Financing cash flow	**(10,238)**	**(21,467)**	**(19,845)**	**(18,074)**
Effective of FX	110	(202)	-	-
Net cash flows	**10,212**	**(3,382)**	**1,786**	**5,415**

Individual items may varies from reported figures due to rounding differences/definition differences
Source(s): Company, ABCI Securities estimates

Pinduoduo (PDD US)

Ongoing market share gains

- Superior revenue growth vs. peers demonstrate the success of its "value-for-money" offering and international expansion
- Continued investments in new businesses and user engagement could shave margins ahead
- Maintain **BUY** with a TP of US$ 180

Company Report

Rating: BUY
TP: US$ 180

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

Price	US$ 121.3
Est. share price return	48.4%
Est. dividend yield	NA
Est. total return	48.4%
Last Rating &TP	BUY, US$180
Previous Report Date	Dec 1, 2023

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L (US$)	152.9/59.6
Outstanding shares (mn)	5,462
Market cap (US$ mn)	165,650
3-mth avg daily turnover (US$ mn)	1,004
Major shareholder(s)	
Zheng Huang	26.5%

Source(s): Bloomberg, Company

Ongoing market share gains. Pinduoduo has attained strong revenue growth in recent quarters, indicating market share gain against peers. In our view, this can be attributed to 1) solid position in the industry as a "value-for-money" platform amid tightened spending in a slowing economy; 2) improving monetization capabilities driven by operational improvement; 3) optimized product portfolio driven by deepened cooperation with brands and continuous investments in agriculture and other areas; 4) increased contribution of emerging businesses, including Duoduo Grocery and Temu. We expect revenue to grow at 32% CAGR 2023-25E. Based on our estimates, we believe Pinduoduo now commands a mid-20s market share in China's e-commerce market, challenging incumbents such as Alibaba (9988 HK, BABA/US).

Robust revenue growth mitigating margin dilution. In our view, the improved operating leverage arising from strong revenue growth has provided financial resources for the company to compete in the market by allowing for higher subsidiaries and investment in new businesses.

Maintain BUY. We maintain our **BUY** rating with a revised TP of US$180 given Pinduoduo's strong growth momentum. Our TP implies 26.7x 2024E core P/E. In our view, current valuation is supported by its growth momentum. Also, we believe divestment risk from its major strategic shareholder has lessened.

Results and Valuation

FY end Dec 31	2022A	2023E	2024E	2025E
Revenue (RMB mn)	130,558	233,140	311,196	404,775
Chg (%,YoY)	*39.0*	*78.6*	*33.5*	*30.1*
Net profit (RMB mn)	31,538	48,687	57,792	73,062
Chg (%,YoY)	*306.0*	*54.4*	*18.7*	*26.4*
Core net profit*(RMB mn)	39,529	58,513	70,740	89,753
Chg (%,YoY)	*185.8*	*48.0*	*20.9*	*26.9*
Earnings per ADS (RMB)	21.9	33.8	40.1	50.7
Chg (%,YoY)	*302.6*	*54.4*	*18.7*	*26.4*
Core earnings per ADS (RMB)	27.4	40.6	49.1	62.3
Chg (%,YoY)	*183.4*	*48.0*	*20.9*	*26.9*
Core P/E (x)	31.8	21.5	17.8	14.0
P/S (x)	9.6	5.4	4.0	3.1
ROAE (%)	32.7	33.2	26.9	24.3
ROAA (%)	15.1	17.1	15.8	15.8

Note:1ADR=4 ordinary shares
Source (s): Bloomberg, ABCI Securities estimates

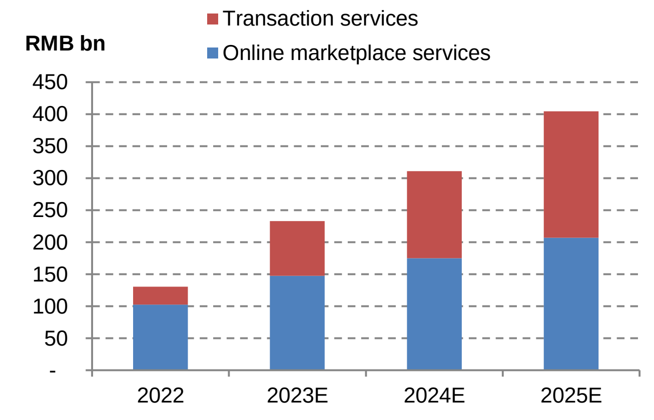
Financial outlook

We expect revenue to increase at 32% CAGR in 2023E-25E, largely driven by improving monetization via providing more valued-added services to merchants, in addition to rising contribution from emerging businesses such as Temu and Duoduo Grocery.

Online marketing service: We expect online marketing service, which mainly includes performance-based marketing services, such as search ranking, recommendation feeds, among others, to increase at 19% CAGR in 2023E-25E, driven by increased monetization through better service offerings and merchants' stickiness.

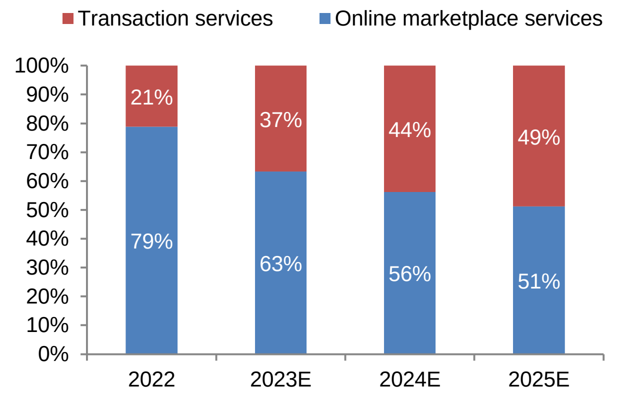
Transaction services: We expect transaction services revenue to increase at 52% CAGR in 2023E-25E on increasing contribution from emerging businesses such as Temu and Duoduo Grocery. As a result, we expect the segment's contribution to total revenue to increase from 37% in 2023E to 49% in 2025E. Specifically, Temu, which takes on a "value-to-money" market position, has been gaining popularly since its launch. We expect its overall revenue contribution to Pinduoduo to be close to the 30% level by 2025E.

Exhibit 49: Revenue trend



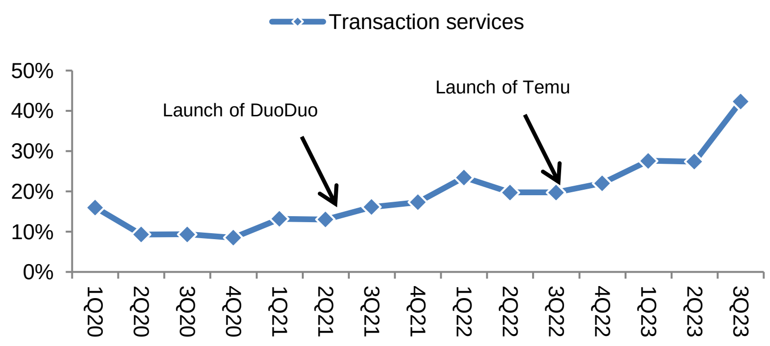
Source(s): Company, ABCI Securities estimates

Exhibit 50: Revenue mix



Source(s): Company, ABCI Securities estimates

Exhibit 51: Rising contribution of transaction service (% of revenue)



Source(s): Company, ABCI Securities

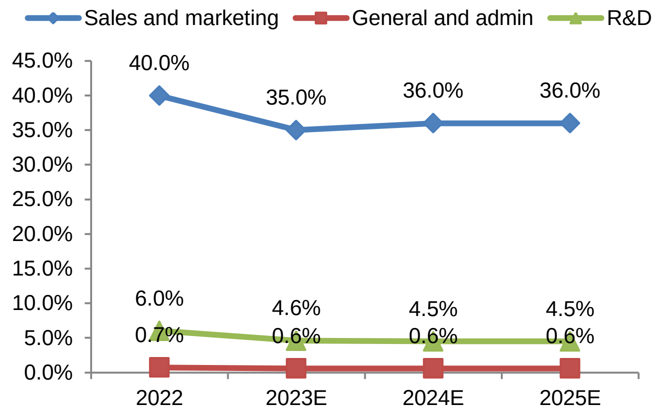
We expect gross margin to stay relatively stable at around 65% in 2024-25E.

Sales and marketing expenses has been the largest cost item to support the company's "value-to-money" market position. The company's strategic shift from marketing to R&D and emphasis on quality growth has led to more disciplined sales and marketing expenses in recent quarters.

In our view, the improved cost control has provided additional financial resources to compete in the market by allowing for higher subsidiaries and investment in new businesses, such as Temu.

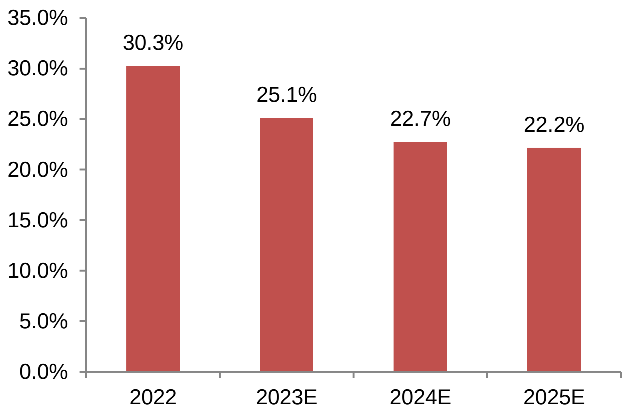
Looking forward, we expect non-GAAP sales and marketing expenses/revenue ratio to be 36.0% in 2024E-25E. In addition, we expect R&D expenses/revenue ratio to be 4.5% in 2024E-25E. Overall, we expect non-GAAP core net profit to expand at 24% CAGR in 2023-25E. Our 2023-24E financial forecast remains unchanged.

Exhibit 52: Non-GAAP cost trend (% of revenue)



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

Exhibit 53: Core net margin



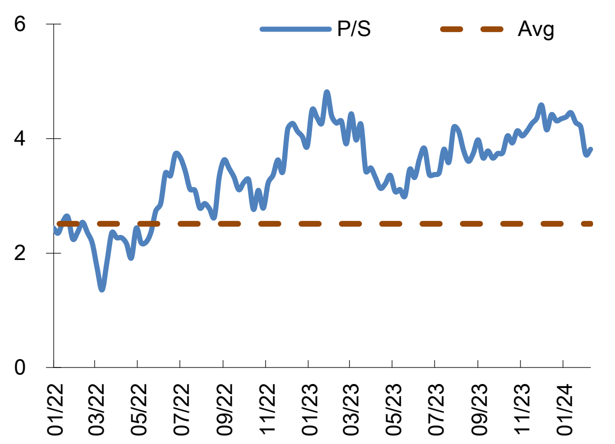
Source(s): Company, ABCI Securities estimates

Valuation and TP

We maintain our **BUY** rating on the counter with TP of US$ 180 to reflect Pinduoduo's robust growth momentum. Our TP implies 26.7x 2024E core P/E.

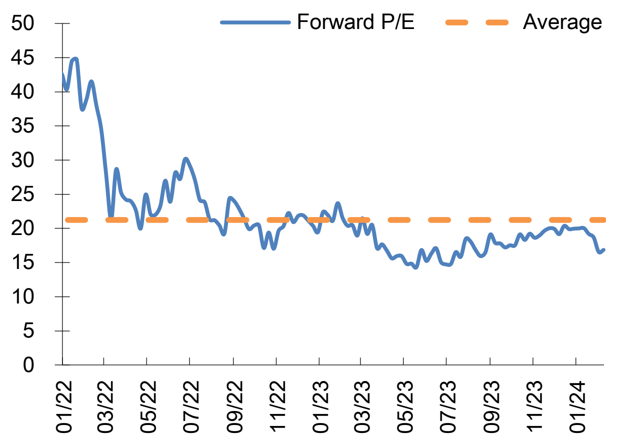
On the flip side, US delisting risks will remain as the company is one of the few major internet platforms without a dual listing status. Positively, divestment risk from the company's strategic stakeholder, which presently owns around 14.7% of the company's stakes, has lessened, in our view.

Exhibit 54: P/S trend



Source(s): Bloomberg, ABCI Securities

Exhibit 55: Forward P/E trend



Source(s): Bloomberg, ABCI Securities

Exhibit 56: DCF sensitivity (in US$)

		WACC				
		10.0%	**11.0%**	**12.0%**	**13.0%**	**14.0%**
Terminal growth	**1.0%**	206	181	161	145	131
	2.0%	222	193	170	152	136
	3.0%	242	207	181	160	143
	4.0%	268	225	194	169	150
	5.0%	305	250	211	181	159

Source (s): ABCI Securities estimates

Company profile

Business
• Major ecommerce platform in China with an **estimated market share at the mid-20s level** • Platform based business model which generally does not bear inventories • **Rapid growth in recent years** despite a relatively short operating history since 2015 • Rising popularity driven by its **innovative business model** that provides buyers with value-for-money products and interactive shopping experiences. For example, it provides various "mini-games" for users to earn coupons • "RMB 10bn subsidy" has been its major marketing program in recent years to reinforce its **"value-for-money" proposition** • Annual active buyers estimated to be over 900mn, similar to Alibaba • Estimated GMV per buyer around RMB 3.3K in 2022, vs. about RMB 9K for Alibaba, illustrating its focus on the value-for-money segment • Strategic partnership with Weixin to leverage its traffic • **Strategic investments in agriculture** in recent years • **Launched Temu for international market** in 3Q22 with growing popularly globally
Financials
• High gross margin over 60% thanks to platform based business model but a changing business mix towards emerging businesses may shave margins • **Marketing expenses has been a major cost item** and swing factor for profitability given its "value-for-money" proposition • **Strategic shift from marketing to R&D** and emphasis on quality growth has led to more controlled marketing expenses in recent quarters, thus improving overall profitability • Achieved break-even since 2Q21 with core net margin rising to 25%-35% range in recent quarters • **Swing factors for future profitability** includes potential increase in customer subsidies to compete in the market as well as Temu's profitability • **Strong balance sheet** with RMB 203bn cash and short-term investment against RMB 16bn convertible bonds in Sep 2023
Management and shareholder
• Largest shareholder and co-founder Zheng Huang (26.5% stake) **stepped down from his management role** of Chairman/member of board of directors in Mar 2021. He also gave up his 1:10 super voting power and entrusted his voting rights to the board. CEO Lei Chen was appointed as the new Chairman. • **PDD partnership:** PDD partnership is entitled to appoint executive directors and nominate and recommend the CEO • **No dividend record** since listing • **US delisting risk** arising from tightened regulatory requirement • **Strategic shareholder**, a major online platform in China, holds about a 14.7% stake
Corporate governance/information disclosure
• Like other major e-commerce platforms, the company has ceased disclosing some operational metrics such as GMV/users in recent years • **Google reportedly suspended Pinduoduo app in Mar 2023** due to information security concern, while Pinduoduo has rejected its claim • Various ESG initiatives in recent years

Financial Forecast

Consolidated income statement (2022A-2025E)

FY Ended Dec 31 (RMB mn)	2022A	2023E	2024E	2025E
Total revenue	**130,558**	**233,140**	**311,196**	**404,775**
Cost of sales	(31,462)	(79,308)	(108,973)	(141,742)
Gross profit	**99,095**	**153,832**	**202,223**	**263,033**
Sales and marketing	(54,344)	(84,207)	(115,512)	(150,247)
General and admin	(3,965)	(5,029)	(6,713)	(8,731)
R&D	(10,385)	(13,771)	(18,071)	(23,504)
Operating Profits	**30,402**	**50,825**	**61,928**	**80,550**
Interest income	3,997	7,500	7,500	7,500
Interest expenses	(52)	(100)	(100)	(100)
Fx gain	(150)	0	0	0
Others, net	2,221	1,000	1,000	1,000
Share of results of investee	(155)	150	150	150
PBT	**36,264**	**59,375**	**70,478**	**89,100**
Tax	(4,726)	(10,687)	(12,686)	(16,038)
PAT	**31,538**	**48,687**	**57,792**	**73,062**
Minority interests	0	0	0	0
Profits attributable to shareholders	**31,538**	**48,687**	**57,792**	**73,062**
Share-based compensation	7,718	9,326	12,448	16,191
Other non-core items	273	500	500	500
Non-GAAP profits attributable to shareholders	**39,529**	**58,513**	**70,740**	**89,753**
Growth				
Total revenue (%)	39.0	78.6	33.5	30.1
Gross Profit (%)	59.2	55.2	31.5	30.1
Operating Profit (%)	340.8	67.2	21.8	30.1
Net profit (%)	306.0	54.4	18.7	26.4
Non-GAAP net profit (%)	185.8	48.0	20.9	26.9
Operating performance				
Operating margin (%)	23.3	21.8	19.9	19.9
Net margin (%)	24.2	20.9	18.6	18.1
Core net margin (%)	30.3	25.1	22.7	22.2
ROAE (%)	32.7	33.2	26.9	24.3
ROAA (%)	15.1	17.1	15.8	15.8

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

Consolidated balance sheet (2022A-2025E)

As of Dec 31 (RMB mn)	2022A	2023E	2024E	2025E
Fixed assets	1,045	3,045	5,045	7,045
Intangible assets	134	141	148	148
Other non-current assets	19,323	40,812	42,781	42,781
Total non-current assets	**20,502**	**43,997**	**47,974**	**49,974**
Cash & equivalents	34,326	60,333	109,560	232,040
Restricted cash	57,974	63,772	70,149	70,149
Short-term investments	115,113	155,113	160,113	165,113
Account receivables	588	617	648	648
Other current assets	8,617	8,933	9,265	9,265
Total current assets	**216,618**	**288,767**	**349,734**	**477,214**
Total assets	**237,119**	**332,764**	**397,708**	**527,187**
Payable to merchants	63,317	92,582	87,481	120,492
Merchant deposit	15,058	20,421	20,558	26,773
Borrowings and notes	13,886	14,886	8,806	2,726
Other current liabilities	24,629	24,812	25,005	25,005
Total current liabilities	**116,890**	**152,702**	**141,849**	**174,996**
Convertible bonds	1,576	1,654	-	-
Other non-current liabilities	884	2,625	2,756	2,756
Total non-current liabilities	**2,459**	**4,280**	**2,756**	**2,756**
Total liabilities	**119,349**	**156,981**	**144,605**	**177,752**
Equity attributable to shareholders	117,771	175,784	253,103	349,437
Non-controlling interests	-	-	-	-
Total equity	**117,771**	**175,784**	**253,103**	**349,437**

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 flows (2022A-2025E)

As of Dec 31 (RMB mn)	2022A	2023E	2024E	2025E
Net income	31,538	48,687	57,792	73,062
Depreciation and amortization	2,224	2,000	2,000	2,000
Other non-cash adjustments	7,323	9,326	12,448	16,191
Change in working capital	7,423	8,994	(15,013)	39,226
Operating cash flow	**48,508**	**69,007**	**57,227**	**130,480**
Acquisition of fixed asset	(636)	(4,000)	(4,000)	(4,000)
Net purchase of investments	(21,090)	(40,000)	(5,000)	(5,000)
Other investment cash flow	(636)	-	-	-
Investing cash flow	**(22,362)**	**(44,000)**	**(9,000)**	**(9,000)**
Financing cash flow	**10**	**1,000**	**1,000**	**1,000**
Fx effect	100	-	-	-
Net cash flow	**26,256**	**26,007**	**49,227**	**122,480**

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

Risk factors

Tightened regulatory environment

The government has implemented various regulations in recent years, leading to a tightened regulatory environment. E.g., the State Administration for Market Regulation of the People's Republic of China (the "SAMR") has launched the anti-monopoly investigation on several e-commerce platforms, imposed fines, and demanded business restructuring of these platforms.

Market competition

The e-commerce industry is a competitive one. Commission rate, promotion discount, brand advertising, technological investment, among others, are crucial in determining success.

Slowdown in ecommerce consumption

As the industry is dependent on consumer spending, any significant slowdown of consumption in China will 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 (core 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.

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Definition of equity rating

Rating	Definition
Buy	Stock return rate≥ Market return rate (~7%)
Hold	- Market return rate (~-7%) ≤ Stock return rate < Market return rate (~+7%)
Sell	Stock return < - Market return (~-7%)

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 2005 (For reference: HSI total return index 2005-23 averaged at 7.4%)

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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