

JD.com (JD US/9618 HK)

Strength in operational improvement

- Rationalizing new businesses investments and cost control would result in better margins
- Gradual recovery in the e-commerce market, with consumer staples outperforming discretionary
- Maintain **BUY** with a TP of US\$ 84 for **JD-ADR (JD US)** and HK\$ 330 for **JD-SW (9618 HK)**

Strength in operational improvement. Solid margin gains in 2Q22, with core net margin risen to 2.4% vs. 1.8% in 2Q21 and 1.7% in 1Q22, thanks to turnaround in JD Logistics, narrowing losses of new businesses, and better margins of JD Retail. JD is rationalizing investments in new businesses with more emphasis placed on profitability, acquisition of high-quality customers, and controls on spending, especially in marketing. In our view, this could raise margins despite a moderating business expansion.

Gradual recovery underway. The e-commerce market has been recovering since June 2022, with consumer staples outperforming discretionary such as apparel, electronics, among others. We expect gradual recovery to continue, assuming COVID measures will not tighten further over the next few months. We expect revenue growth to be 9% YoY in 2H22 and 15% YoY for 2023E versus 5% YoY in 2Q22, indicating sequential improvement.

Recommendation. Maintain BUY with a TP of US\$ 84 for JD-ADR (JD US) and HK\$ 330 for JD-SW (9618 HK). We believe JD's strong track record in operational improvement could result in better margins in coming quarters. In addition, JD has lower supply risk than its listed peers after the recent divestment by Tencent (700 HK), in our view.

Results and Valuation

FY end Dec 31	2020A	2021A	2022E	2023E
Revenue (RMB mn)	745,802	951,592	1,048,144	1,206,919
Chg (% YoY)	29.3	27.6	10.1	15.1
Net profit (RMB mn)	49,405	-3,560	5,666	17,848
Chg (% YoY)	305.5	NA	NA	215.0
Core net profit (RMB mn)	16,828	17,207	19,315	26,940
Chg (% YoY)	56.5	2.3	12.3	39.5
Earnings per ADS (RMB)	31.7	-2.2	3.6	11.2
Chg (% YoY)	285.6	NA	NA	215.0
Core earnings per ADS (RMB)	10.6	10.8	12.1	16.9
Chg (% YoY)	45.7	2.0	12.5	39.5
Core P/E (x)- ADR	40.5	40.7	36.2	26.0
Core P/E (x)-SW share	39.9	40.1	35.6	25.6
ROAE (%)	34.2	-1.6	2.3	7.0
ROAA (%)	14.5	-0.8	1.1	3.2

*1 ADR = 2 ordinary shares

USD/CNY = 6.92; HKD/CNY = 0.88

Source (s): Bloomberg, ABCI Securities estimates

Company Report

Aug 29, 2022

Rating (ADR): BUY
 TP (ADR): US\$ 84
 Rating (SW-share): BUY
 TP (SW-share): HK\$ 330

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Price (ADR/SW-share)	US\$ 63.4/ HK\$245.0
Est. share price return (ADR/SW-share)	32.6%/34.7%
Est. dividend yield (ADR/SW-share)	NA/NA
Est. total return (ADR/SW-share)	32.6%/34.7%
Last Rating & TP (ADR/SW-share)	BUY, US\$74/ BUY, HK\$290
Previous Report Date	May 23, 2022

Source(s): Bloomberg, ABCI Securities estimates

Key Data

52Wk H/L (HK\$) (SW-share)	364.3/159.5
52Wk H/L (US\$) (ADR)	92.6/41.5
Outstanding shares (mn)	3,123
Market cap (HK\$ mn) (all outstanding shares)	765,135
3-mth avg daily turnover (HK\$ mn) (SW-share)	1,399
3-mth avg daily turnover (US\$ mn) (ADR)	362
Major shareholder(s)	Voting right
Richard Liu	76.1%

Source(s): Bloomberg, HKEx, Company



Strength in operational improvement

In 2Q22, JD Retail's reported RMB8.1bn operating profit with operating margin rising to 3.4% from 2.6% in 2Q21, while JD Logistics reported RMB 36mn in operating profit vs. RMB 357bn operating losses in 2Q21. New businesses, including Jingxi and other technology initiatives, reported RMB 2.0bn in operating losses during the quarter (vs. RMB 2.4bn losses in 1Q22), thanks to lower marketing expenses (-10.7% YoY). As a result, core net margin was 2.4% in 2Q22, higher than the 1.7% in 1Q22 and 1.8% in 2Q21.

New businesses and DaDa collectively reported RMB 2.4bn in operating losses in 2Q22, eroding the RMB 8.1bn operating profit of JD Retail. We believe the losses can be narrowed by further cost control.

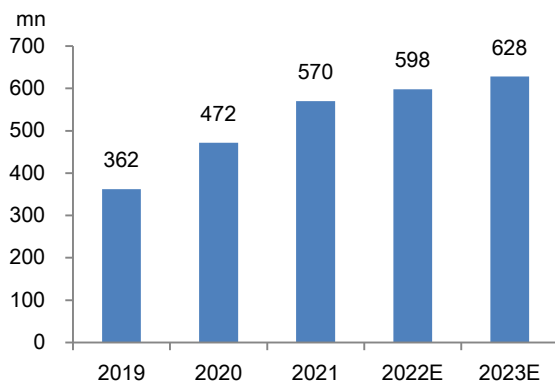
In 2Q22, revenue grew 5% YoY to RMB 267bn. Non-GAAP adjusted net profit (core net profit) increased by 40% YoY to RMB 6.5bn, thanks to better-than-expected operational improvement.

Net product revenue growth was 3% YoY in 2Q22, driven by the 8% YoY revenue growth of general merchandise products amid the flat growth in electronics and home appliance products. This is in line with the industry trend where consumer staples are experiencing stronger demand than discretionary. Net service revenue, which accounted 16% of total revenue in 2Q22, grew 22% YoY on expansion in logistics and other services.

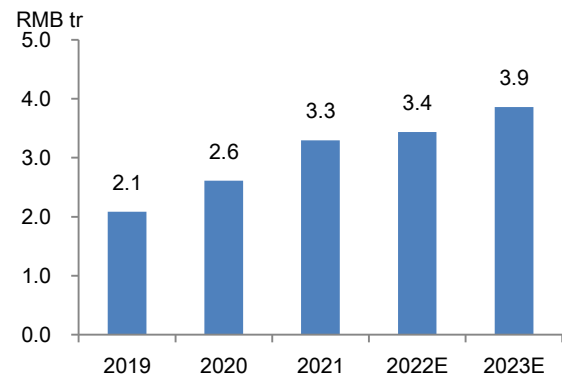
Financial analysis

We expect revenue to increase at 13% CAGR in 2021-23E amid the 8% CAGR in GMV and the 5% CAGR in annual active customer during the period. We expect net product revenue to increase at 10% CAGR in 2021-23E, mainly driven by general merchandise products. We expect net service revenue CAGR to be 25%, thanks to increased corporate demand for quality supply-chain services.

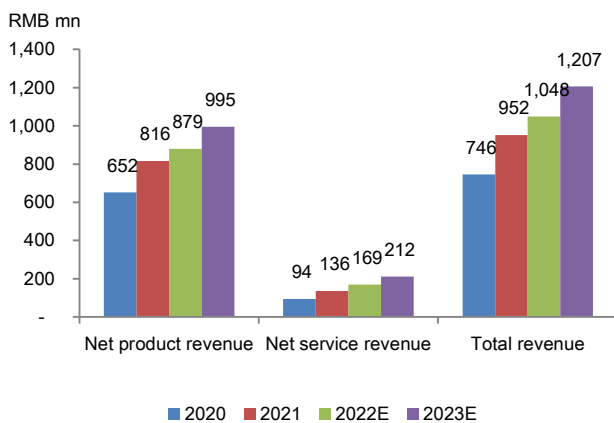
Amid a soft economic environment, JD is rationalizing its business expansion with more emphasis on profitability of new businesses (such as Jingxi and overseas businesses). As the Group seeks to acquire more quality customers with higher average spending, we expect annual active customer to increase at 5% CAGR in 2021-23E. In our view, this strategy could support margins of new businesses despite slower customer growth in the near term.

Exhibit 1: Annual active customer outlook


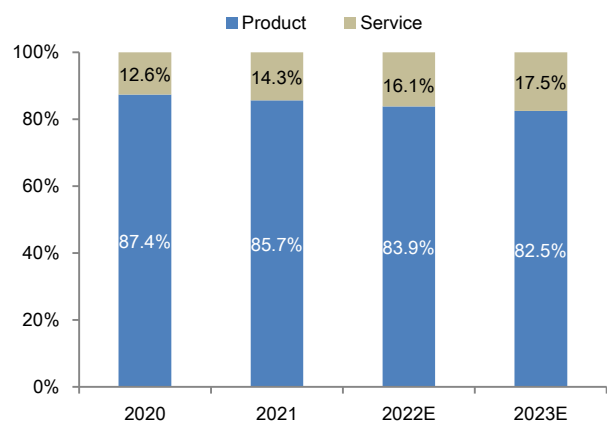
Source(s): Company, ABCI Securities estimates

Exhibit 2: GMV outlook


Source(s): Company, ABCI Securities estimates

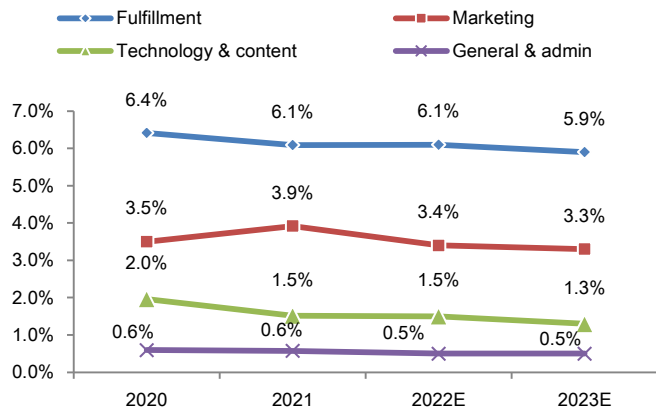
Exhibit 3: Revenue outlook


Source(s): Company, ABCI Securities estimates

Exhibit 4: Revenue mix


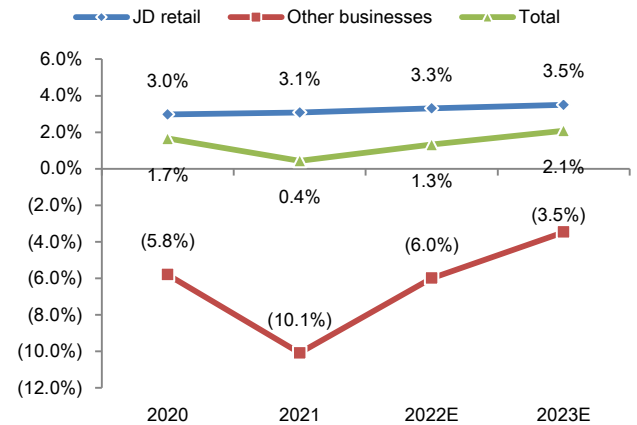
Source(s): Company, ABCI Securities estimates

In terms of segment profitability, we see cost optimization potential of loss-making businesses including Jingxi, technology, and other new businesses given JD's strong track record in cost control. Looking forward, we expect JD Retail's operating margin to improve from 3.1% in 2021 to 3.5% in 2023E, while operating margin of other businesses to improve from -10.1% in 2021 to -3.5% in 2023E.

Exhibit 5: Non-GAAP* cost trend (% of sales)


Source(s): Company, ABCI Securities estimates

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

Exhibit 6: Segment operating margin outlook


Source(s): Company, ABCI Securities estimates

As a result of ongoing cost control and operating improvement, we expect core net margin to stay stable at 1.8% in 2022E and improve to 2.2% in 2023E versus 1.8% in 2021.

Exhibit 7: Forecast changes for 2022E

(RMB mn)	Old	New	Diff.	Comment
Revenues	1,073,939	1,048,144	(2%)	More prudent expansion in new businesses
Core profit	17,175	19,315	12%	Cost control and operational improvement

Source(s): ABCI Securities estimates

Exhibit 8: Forecast changes for 2023E

(RMB mn)	Old	New	Diff.	Comment
Revenues	1,279,482	1,206,919	(6%)	More prudent expansion in new businesses
Core profit	25,763	26,940	5%	Cost control and operational improvement

Source(s): ABCI Securities estimates

Valuation and TP

JD-SW (9618 HK): Our SOTP-based TP is HK\$ 330.

JD-ADR (JD US): Based on our TP for JD-SW, the TP of JD-ADR is US\$ 84 (1 ADR represents 2 shares).

The table below shows our SOTP-based valuation range for JD-SW (9618 HK).

Exhibit 9: JD-SW (9618 HK): SOTP-based valuation range (HK\$ per share)

Segment	Low	High	Comment
Core ecommerce business [#]	252	334	DCF –from 13% to 9% WACC
Investments [*]	55	55	Book/market value/ABCI Securities estimates
Overall	307	389	

[#]Excluding JD Health and JD Logistics (2618 HK) and including new businesses

^{*}JD Health (6618 HK) and JD Logistics (2618 HK) based on market value with a 20% holding discount, and other strategic investments

Source(s): ABCI Securities estimates

Despite near-term macro headwinds, we believe JD's strong track record in operational improvement could lead to better margins in coming quarters. In addition, JD has lower supply risk than its listed peers after the recent divestment by Tencent (700 HK), in our view.

Exhibit 10: TP changes (HK\$ per share)

Old	New	Methodology-old	Methodology-new
290	330	SOTP	SOTP with revised financial forecasts

Source(s): ABCI Securities estimates



Financial forecast

Consolidated income statement (2020A-2023E)

FY Ended Dec 31 (RMB mn)	2020A	2021A	2022E	2023E
Net product revenue	651,879	815,655	879,052	995,393
Net service revenue	93,923	135,937	169,092	211,525
Total revenue	745,802	951,592	1,048,144	1,206,919
Cost of sales	(636,694)	(822,525)	(905,666)	(1,040,438)
Gross profit	109,108	129,067	142,477	166,481
Fulfillment expenses	(48,700)	(59,055)	(65,125)	(72,465)
Marketing expenses	(27,156)	(38,743)	(36,705)	(41,023)
Research and development expenses	(16,149)	(16,332)	(17,414)	(17,471)
General & admin expenses	(6,409)	(11,562)	(9,320)	(10,336)
Gains on disposal	1,649	767	0	0
Operating Profit	12,343	4,141	13,914	25,185
Share of results of equity investees	4,291	(4,918)	(4,500)	(2,500)
Interest expenses, net	1,628	(1,213)	(1,250)	(1,300)
Others, net	32,556	(590)	(1,000)	(1,000)
PBT	50,819	(2,580)	7,164	20,385
Tax	(1,482)	(1,887)	(2,498)	(3,537)
PAT	49,337	(4,467)	4,666	16,848
Minority interests	(68)	(907)	(1,000)	(1,000)
Profit attributable to shareholders	49,405	(3,560)	5,666	17,848
Share-based compensation	4,156	8,293	7,049	7,402
Amortization	723	853	1,048	1,207
Impairment/FV changes of investments	(35,690)	13,371	1,000	0
Other non-core items	(1,767)	(1,750)	4,552	484
Non-GAAP profit attributable to shareholders	16,828	17,207	19,315	26,940
Growth				
Total revenue (%)	29.3	27.6	10.1	15.1
Gross Profit (%)	29.2	18.3	10.4	16.8
Operating Profit (%)	37.2	(66.4)	236.0	81.0
Net profit (%)	305.5	(107.2)	(259.2)	215.0
Non-GAAP net profit (%)	56.5	2.3	12.3	39.5
Operating performance				
Operating margin (%)	1.7	0.4	1.3	2.1
Net margin (%)	6.6	(0.4)	0.5	1.5
Core net margin (%)	2.3	1.8	1.8	2.2
ROAE (%)	34.2	(1.6)	2.3	7.0
ROAA (%)	14.5	(0.8)	1.1	3.2

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

Source(s): the Group, ABCI Securities estimates



Consolidated balance sheet (2020A-2023E)

As of Dec 31 (RMB mn)	2020A	2021A	2022E	2023E
Fixed assets	41,628	53,089	70,989	93,289
Investments	98,916	82,310	85,471	88,790
Other non-current assets	46,944	61,436	59,236	57,036
Total non-current assets	187,487	196,835	215,696	239,116
Cash & equivalents	90,519	76,692	68,205	73,995
Short-term investments and investment securities	60,577	114,564	129,564	154,564
Inventories	58,933	75,601	85,718	82,666
Account receivables	7,112	11,900	10,338	13,227
Other current assets	17,660	20,915	21,488	22,089
Total current assets	234,801	299,672	315,313	346,540
Total assets	422,288	496,507	531,009	585,655
Account payables	127,816	169,590	201,404	227,504
Borrowings and notes	3,260	4,367	6,367	8,367
Other current liabilities	42,941	47,679	47,807	47,942
Total current liabilities	174,016	221,636	255,578	283,812
Payables & accruals	332	1,786	1,875	1,969
Borrowings and notes	12,530	9,386	11,386	13,386
Other non-current liabilities	13,790	16,915	16,980	17,048
Total non-current liabilities	26,652	28,087	30,241	32,403
Total liabilities	200,668	249,723	285,819	316,215
Mezzanine equity	17,133	1,212	1,212	1,212
Equity attributable to shareholders	187,543	208,911	208,317	233,567
Non-controlling interests	16,943	36,661	35,661	34,661
Total equity	204,486	245,572	243,978	268,227

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 statement (2020A-2023E)

As of Dec 31 (RMB mn)	2020A	2021A	2022E	2023E
Net income	49,337	(4,467)	4,666	16,848
Depreciation and amortization	6,068	6,232	6,300	6,400
Other non-cash adjustments	(31,538)	21,588	7,049	7,402
Change in working capital	18,677	18,948	19,807	22,640
Operating cash flow	42,544	42,301	37,823	53,290
Acquisition of fixed asset	(12,437)	(22,255)	(22,000)	(26,500)
Movement of short-term investments	(35,599)	(54,322)	(15,000)	(25,000)
Other investment cash flow	(9,775)	2,329	-	-
Investing cash flow	(57,811)	(74,248)	(37,000)	(51,500)
Financing cash flow	71,072	19,503	(9,309)	4,000
Effective of FX	(5,082)	(1,498)	-	-
Net cash flows	50,723	(13,942)	(8,486)	5,790

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 months, leading to an overall tightened regulatory environment. For example, the State Administration for Market Regulation of the People's Republic of China (the "SAMR") has launched anti-monopoly investigation on selected e-commerce platforms, imposed fines and demanded business restructuring of these platforms.

Market competition

The ecommerce industry is highly competitive, with companies contending on commission rate, promotion discount, brand advertising, technological investment, and more.

Slowdown in ecommerce consumption

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

Non-GAAP financials

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

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

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



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Definition of equity rating

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

Notes: Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months
Market return rate: average market return rate since 2009 (HSI total return index 2009-21 averaged at 9.2%)

Time horizon of share price target: 12-month

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

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