

## 2022 Outlook: No more regulatory shocks

- **Steadier regulatory environment based on takeaways from Central Economic Work Conference**
- **Expect e-commerce and online advertising to recover in 2022, but back-end loaded**
- **Sub-segment preference: Food delivery and e-commerce**
- **Our top picks are [JD](#) and [Meituan](#) due to lower regulatory risk exposure**

**Manageable regulatory risk in 2022.** Our study on the Chinese government's annual Central Economic Work Conference concluded that the key focus in 2022 should be shifting from regulatory enforcement to stabilising economy growth. "Real surprise" is unlikely. Overall risk should be more manageable with more frequent dialogue between internet companies and regulators.

**E-commerce growth back-end loaded.** Macro slow down started dragging e-commerce and online advertising in 3Q21. We expect gradual recovery in 2022, and the growth will be likely back-end loaded. E-commerce growth will be supported by lower-tier city penetration and new business models or initiatives such as community group buy (CGB). We expect the investment loss to be narrowed this year.

**Sub-segment preference: Food delivery and e-commerce.** Both segments' regulatory risks have been mostly priced in. Food delivery growth remains solid in 2022, driven by "everything to home". E-commerce's growth will be more resilient than online ads, amid macro slow down. Online games segment faces higher uncertainty at least in 1Q22 before resumption of games approval process.

**Top picks: JD (9618 HK) and Meituan (3690 HK).** We prefer stocks with resilient growth despite macro slowdown and have lower exposure to regulatory risks. We like JD most, as it is a beneficiary of new antitrust rule, and it will deliver stronger e-commerce growth than the market. We also favour Meituan, as its core delivery and new CGB business are riding on penetration into lower-tier cities and lower income groups.

HSI: 24,402

### ANALYST

Tsz-Wang TAM, CFA +852 36684195 [tszwangtam@dbs.com](mailto:tszwangtam@dbs.com)Lilian LV [lilianlv@dbs.com](mailto:lilianlv@dbs.com)Ryan WANG +86 21 38562896 [ryanwangzx@dbs.com](mailto:ryanwangzx@dbs.com)

### Recommendation & valuation

Company Name	Currency	Price Local\$	Target Price Local\$	Recom	Mkt Cap US\$m
<a href="#">Alibaba # (9988 HK)</a>	HKD	133.00	211.00	BUY	370,423
<a href="#">Baidu (9888 HK)</a>	HKD	133.00	210.00	BUY	6,942
<a href="#">Bilibili (9626 HK)</a>	HKD	333.00	946.88	BUY	16,425
<a href="#">JD.com (9618 HK)</a>	HKD	305.20	419.00	BUY	60,848
<a href="#">Kuaishou (1024 HK)</a>	HKD	85.65	131.00	BUY	46,467
<a href="#">Meituan (3690 HK)</a>	HKD	227.00	342.00	BUY	178,780
<a href="#">Pinduoduo (PDD US)</a>	USD	60.38	96.00	BUY	74,811
<a href="#">Tencent (700 HK)</a>	HKD	480.80	671.00	BUY	592,991
<a href="#">Tongcheng (780 HK)</a>	HKD	14.60	25.00	BUY	4,156

# FY21: FY22; FY22: FY23

Source: Thomson Reuters, DBS Bank (Hong Kong) Limited ("DBS HK"), Bloomberg Finance L.P.



## China Internet Sector

### Introduction

The internet sector de-rated in 2021 mostly due to regulatory tightening, including (1) antitrust policies implemented (e.g., no more “2 choose 1” practice) and (2) policy uncertainties (e.g. games content tightening and personal data protection law). The sector further suffered from a macro slowdown in 2H21, which negatively affected e-commerce’s GMV growth and ads budget, etc.

Looking ahead, we expect that the government will shift the focus from regulatory enforcement in 2021 to stabilise economic growth in 2022. Regulatory risk should be more manageable. We also expect that economic activities will gradually pick up in 3Q and 4Q. The sector valuation is appealing, and we recommend accumulating, as the sector will continue to benefit from structural changes from digitalisation in the longer term.

In this report, we will first discuss the regulatory overview in 2022. In particular, we compared the takeaways from annual Central Economic Work Conference between 2020 and 2021. We will then discuss individual sub-segments: (1) e-commerce, (2) food delivery, (3) online games, (4) online advertising, (5) short video and (6) online travel. We will focus on the growth drivers and regulatory risks.

### Regulatory risk: more manageable in 2022

**Framework was set in 2021; expect fewer “shocks” in 2022.** China Internet sector has witnessed the strictest regulatory scrutiny in 2021, from antitrust, data protection regulation, suspension of online games approval to “common prosperity” initiatives last year. The sector-wide regulatory changes have directly or indirectly eroded company-level profitability since 2Q21.

### Key regulatory developments and enforcement timeline

Antitrust Law	Data Protection	Common Prosperity Commitment
<p><b>Nov 20:</b> Ant's IPO suspension kick off year long regulations crackdown.</p> <p><b>Dec 20:</b> Enforcing antitrust law and prevention of unordered capital expansion (強化反壟斷和防止資本無序擴張) was listed as one of key tasks for 2021 at annual Central Economic Work Conference.</p> <p><b>Feb 21:</b> SAMR (State Administration for Market Regulation) released antitrust guidance for platform economies 《關於平台經濟領域的反壟斷指南》</p> <p><b>Mar-Oct 21:</b> Alibaba, Meituan was fined Rmb18.2bn/Rmb3.44bn due to monopolistic practice for forcing “two choose one”.</p> <p><b>Apr 21:</b> Tencent was given a Rmb100k fine due to improper filing regarding previous acquisition and investment.</p> <p><b>Jul 21:</b> Regulator issued draft rules banning below cost selling and using big data differential pricing on platforms. 《價格違法行為行政處罰規定 (徵求意見稿)》</p> <p><b>Nov 21:</b> SAMR imposed Rmb 500K fines on internet platforms including Alibaba, JD, Tencent, Baidu etc for failing to disclose 43 M&amp;A deals.</p>	<p><b>Jul 21:</b> Regulators called Didi to stop accepting new user registrations citing violation of collecting personal data after US IPO.</p> <p><b>Sep 21:</b> New data security take effective, which sets up framework that classified data collected and use of sensitive data . 《數據安全法》</p> <p><b>Sep 21:</b> Regulator released rules regarding to data security and appropriate use of algorithms for ads recommendation. 《關於加強互聯網信息服務算法綜合治理的指導意見》</p> <p><b>Nov 21:</b> Personal Information Protection Law came into effect, which required user consent before processing user data. 《個人信息保護法》</p>	<p><b>Aug 21:</b> President Xi promoted “Common prosperity” as the major goal in top Communist Party conference, business and entrepreneurs are called to help reduce income inequality.</p> <p><b>Aug 21:</b> Tax hike for internet giants -- Alibaba, Tencent and other big internet companies will no longer enjoy preferential tax status, higher effective tax will take effective next year.</p> <p><b>Aug 21:</b> Increase investment to help promote “Common prosperity” -- Alibaba, Tencent and Pinduoduo committed to invest Rmb100bn, 50bn, and 10bn echoing common prosperity theme.</p> <p><b>Sep 21:</b> Improve social welfare for protecting workers -- Regulator released guidance requiring platforms like Meituan, Ele.me to purchase social insurance for delivery riders. 《維護新就業形態勞動者勞動保障權益的指導意見》</p>

Source: SAMR, Xinhua, DBS HK

**China Internet Sector**

The government used to set a tone for economic work in the coming year during annual Central Economic Work Conference every Dec. We did a comparison between 2020 and 2021 outlines and concluded that the key focus in 2022 should be shifting from regulatory enforcement to stabilising economy growth.

We expect that follow-up regulatory measures in 2022 will fall under the existing framework. Second, internet companies should hold more frequent dialogues with regulators. Overall regulatory risk should give less surprise

to the market and is expected to be more manageable after a year-long adjustment. We will provide updates on individual sub-segments in the following respective sessions.

**Comparison table of Central Economic Work Conference (2021 vs 2020)**

Subjects	2021 version	2020 version	Implications
Overview takeaways	<ul style="list-style-type: none"> <li>Call for launching supportive policies to maintain stable growth (明年經濟工作要穩...各方面要積極推出有利於經濟穩定的政策)</li> </ul>	<ul style="list-style-type: none"> <li>Concentrate on promoting reform and innovation, given the high GDP growth base in 2020 (要用好寶貴時間窗口，集中精力推進改革創新)</li> </ul>	Shifting focus from structural adjustment to stable growth
Key observations	<ul style="list-style-type: none"> <li>Mentioned "stability" (穩) 25 times</li> <li>2022 GDP growth forecast: 5.3%</li> </ul>	<ul style="list-style-type: none"> <li>Mentioned "stability" (穩) 13 times</li> <li>2021 GDP growth forecast: 8%</li> </ul>	
Key messages about antitrust and capital development	<ul style="list-style-type: none"> <li>Stimulate the vitality of market entities as a major task for 2022 (激發市場主體活力...提振市場主體信心...加強反壟斷和反不正當競爭)</li> <li>Give full play to positive role of capital as a production factor, while support and guide its healthy development (發揮資本作為生產要素的積極作用...支持和引導資本規範健康發展)</li> </ul>	<ul style="list-style-type: none"> <li>Step up antitrust work and prevent disorderly expansion of capital were listed as one of the policy priorities for 2021 (強化反壟斷和防止資本無序擴張...)</li> <li>Resolutely against monopoly and call for strengthening regulations on platform economies (堅決反對壟斷...完善平台企業壟斷認定、數據收集使用管理...法律規範)</li> </ul>	Softening wordings on antitrust
Key observations	<ul style="list-style-type: none"> <li>Mentioned "antitrust" (反壟斷) 1 time</li> </ul>	<ul style="list-style-type: none"> <li>Mentioned "antitrust" (反壟斷) 3 times</li> </ul>	

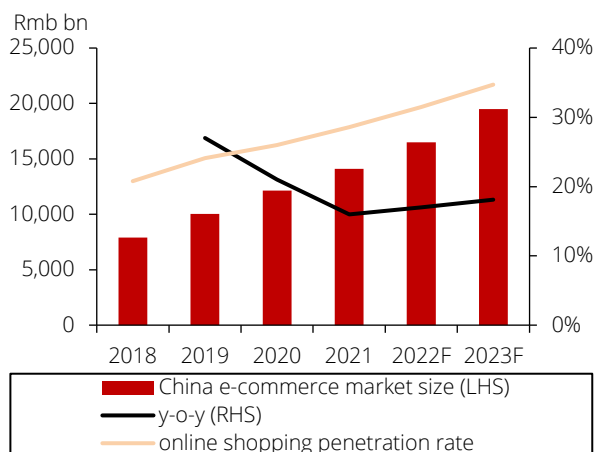
Source: Gov.cn, DBS HK

**E-commerce: driven by lower-tier cities and CGB**

**E-commerce growth back-end loaded in 2022.** China e-commerce market size is projected to grow by 17% in 2022, reaching c.Rmb15tn. We expect slower growth in 1Q and 2Q, given (1) a high base in 1H21 and (2) macro slowdown due to resurgence of the pandemic. We expect growth momentum to gradually recover in the second half of 2022. Medium-term growth drivers include further penetration into lower-tier cities, as well as expansion into low-penetrated categories such as fresh groceries.

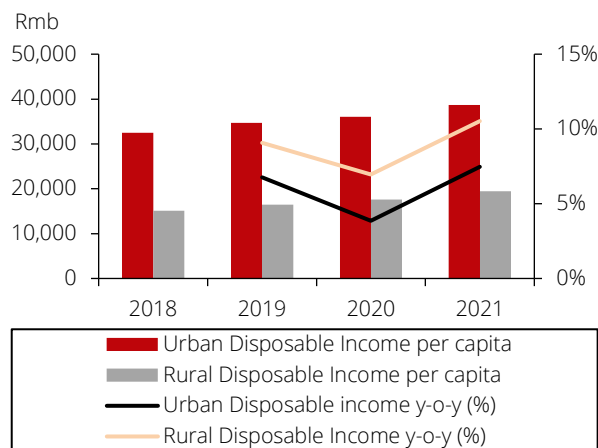
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China e-commerce market size and penetration



Source: iResearch, DBS HK

China disposable income growth (rural vs urban)



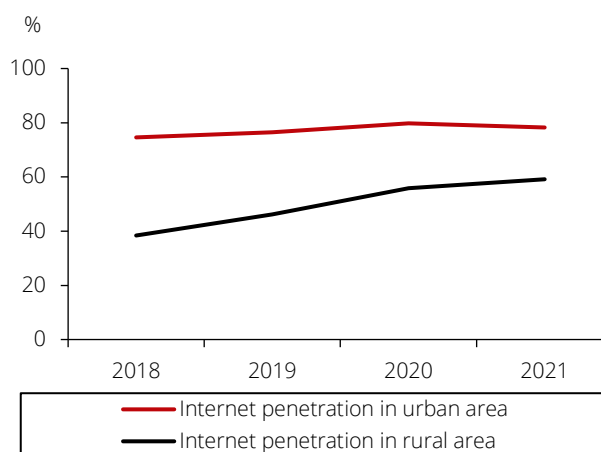
Source: Euromonitor, DBS HK

E-commerce by product category (2019-2022F)

Category	Rmb (Bn)			
	2019	2020	2021F	2022F
Apparel and Footwear	578.5	732.4	594	627.3
y-o-y	24%	27%	-19%	6%
Electronics	675.1	748	809.4	868.7
y-o-y	6%	11%	8%	7%
Food and Drink	394.4	469.3	509	555.2
y-o-y	20%	19%	8%	9%
Consumer Health	68.3	87.5	92.9	98.5
y-o-y	25%	28%	6%	6%
Beauty and Personal	127.9	166.3	175.5	191.3
y-o-y	30%	30%	6%	9%

Source: Euromonitor, DBS HK

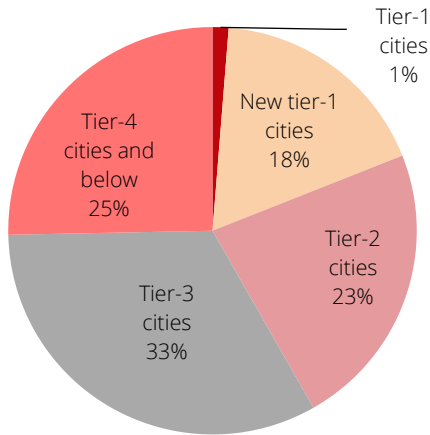
Internet penetration in urban area and rural area



Source: CNNIC, DBS HK

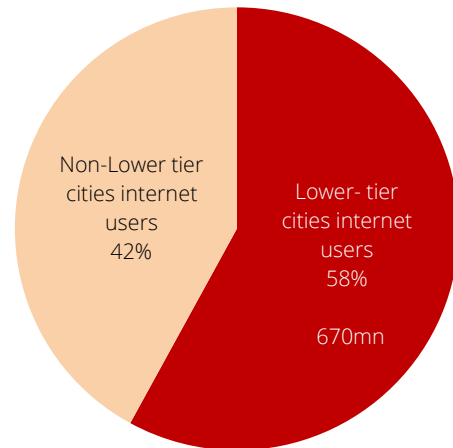
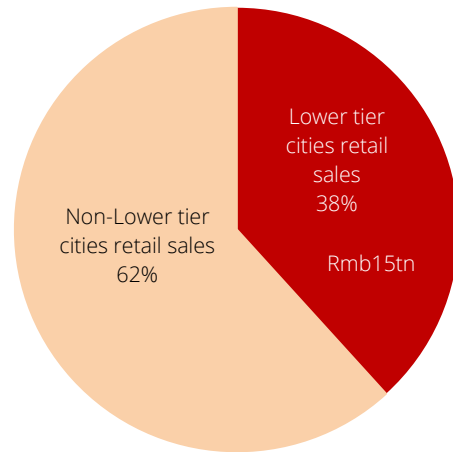
**Driver 1: Expansion into lower-tier cities.** Lower-tier cities (including rural area) represent a Rmb15tn retail market size or 38% of China total retail sales in 2020. The growth potential has yet to be fully explored. **(1) Rising e-commerce penetration.** Currently, Internet users in lower-tier cities account for 58% of total Internet users in China, but the population accounts for c.70% of total.. As internet penetration continues to increase, we expect more new users to come from these less developed regions. As of 3Q21, lower-tier cities contributed c.60% of total new e-commerce users addition. **(2) faster disposable income growth.** Per capital disposable incomes in rural area is estimated to increase by 29% during 2018 to 2022E, 10ppt faster than that in urban area. The narrowing income gap represents higher consumption powers.

**E-commerce new user contribution by different city level in 3Q21**



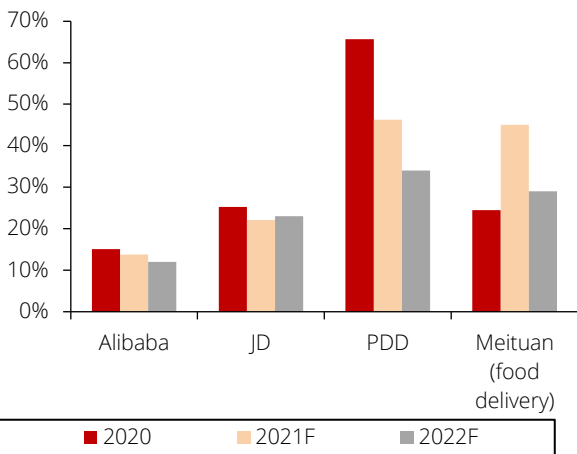
Source: QuestMobile, DBS HK

**China internet users and retail sales in lower-tier cities**



Source: CEIC, QuestMobile, DBS HK

**Key e-commerce players GMV growth (2020-2022F)**



Source: Company, DBS HK

E-commerce players are building platforms targeting users in lower-tier cities, e.g., Alibaba's Taobao deal and JD's Jingxi. The development of new business models such as Community Group Buy (CGB) is also a way to cater to the shopping behaviour in lower-tier cities.

**Driver 2: Investing into e-grocery.** China online grocery market is expected to grow by 37% to reach Rmb921bn in 2022. The growth was led by fresh groceries with a low penetration rate of 12% vs. the overall online retail penetration rate of c.24% in 2021.

CGB is a new business model and key initiative adopted by leading e-commerce platforms to cater fresh groceries. It particularly allows products or baskets with smaller order value without last mile delivery.

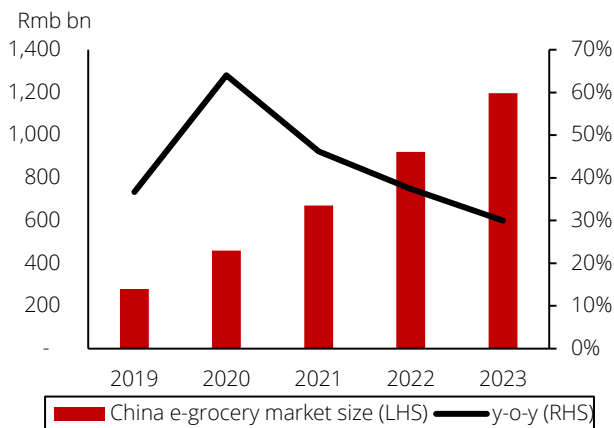
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Major e-grocery business model and players

Business model	Target cities	Covered areas	Pricing strategy	Product variety (SKUs)	Avg basket size	Fulfillment cost (of revenue)	Delivery	Operating model	Key players
DMW (Distributed Mini Warehouse)	1-2 tier cities	1km-3km	110-115%	medium	Rmb70-80	28%-40%	0.5-1h	Self-operated business, directly work with upstream suppliers and offer fulfillment as well as last-mile delivery for fresh groceries	Missfresh (每日優鮮), Dingdong Fresh (叮咚買菜), Meituan grocery (美團買菜)
CGB (Community Group Buy)	3-5 and lower tier cities	0.5-1km	70-85%	low	Rmb15-20	8-10%	next-day	Platform provides supply chain logistics and sorting products, customer-end pick-up points are operated by group leaders	Meituan Select (美團優選), Duoduo Grocery (多多買菜), Taocaicai (淘菜菜), Jingxi pinpin (京喜拼拼)
Supermarket O2O	1-2 tier cities	1km-3km	100%	high	Rmb60-100	15-18%	0.5-1h	Platforms cooperate with supermarkets and offer last-mile delivery from retailers to customers	JD Daojia (京東到家), Taoxianda (淘鮮達), Meituan Instashop (美團閃購)

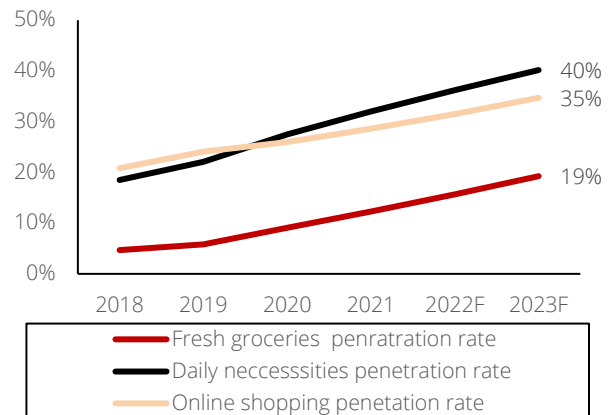
Source: iResearch, 36kr, DBS HK

China e-grocery market size (2019-2023F)



Source: iResearch, DBS HK

China fresh groceries penetration rate (2018-2023F)



Source: China Insight Consultancy, iResearch, DBS HK

CGB still on investment upcycle but expect losses to ease. E-commerce platforms are investing heavily into CGB, and the segment is still loss-making in 3Q21. The investment areas include supply chain, fulfillment, and user acquisition (e.g., operating 1P with a zero margin to enrich product portfolio). We expect the CGB loss to gradually narrow in 2022 as (1) less aggressive expansion amid tightened regulation (2) economies of scale, benefited by higher order density and stronger logistics ecosystems (e.g., inviting third-party logistic partners to invest and run distribution warehouses).

**China Internet Sector**

We expect top CGB players market shares to consolidate, backed by their strong execution capabilities and operational network. Yet, more smaller players potentially exit the market.

**Regulatory Risks**

- Absence of “2 choose 1” practice has been in place for some time. E-commerce players should have augmented their business models.

- The relevant antitrust penalty of Rmb18.2bn for Alibaba was booked in 2QFY3/22. Further penalty and changes in market practice should be limited.
- Personal data protection law requires user consent for future content recommendation and advertisement. It will take time for the impact to be reflected.
- Regulator also discouraged irrational subsidies for CGB.
- Further regulatory risk should be manageable.

**Regulatory implications for e-commerce and food delivery players**

Key regulation measures	Alibaba	JD.com	Pinduoduo	Meituan
1.Antitrust penalty	√	N/A	N/A	√
2.CGB: Penalty for over-subsidy	√	N/A	√	√
3.Social security insurance for delivery riders	√	N/A	N/A	√
4.Common prosperity initiative	√	N/A	√	N/A

Note: √ - refers to penalty or regulation risks priced in; N/A- non applicable

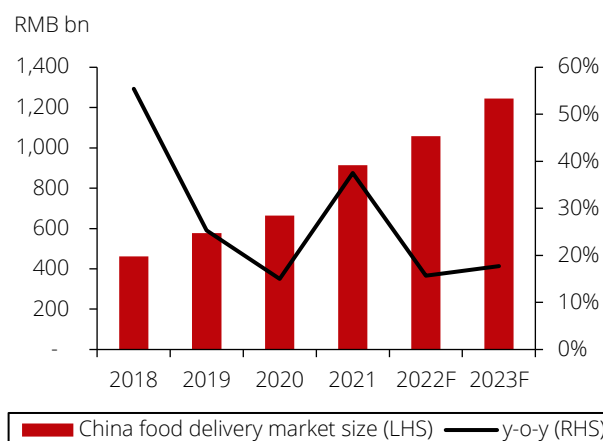
Source: DBS HK

**Food delivery: riding on from food to home to everything to home**

**Maintain solid growth in 2022.** China food delivery market size is expected to grow 16% in 2022F (vs 38% in 2021) thanks to a larger user base, higher order frequency, and accelerated expansion in lower-tier cities. The growth will remain relatively slow in the 1Q and 2Q of 2022, partly due to Covid resurgence, and will gradually recover in 2H22.

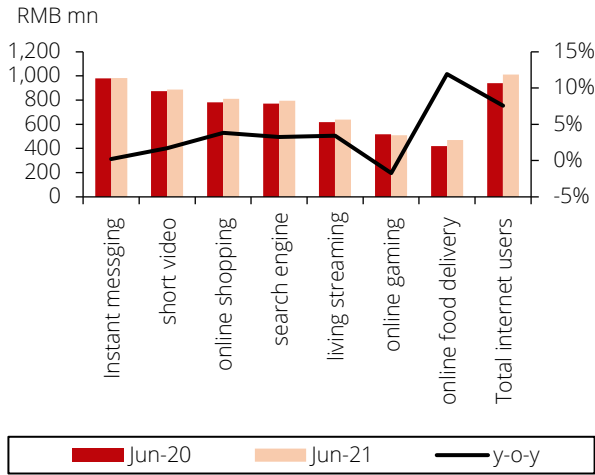
Online delivery monthly active users increased by 12% y-o-y, reaching 469m in July 2021. The growth is much higher than other internet categories, such as short video, e-commerce. Looking ahead, delivery platforms further diversify categories like late night snacks and milk tea to increase order frequency and platform stickiness.

**China food delivery market size (2018-2023F)**



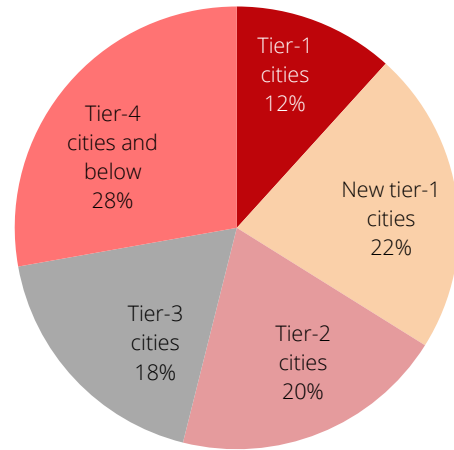
Source: Trustdata, DBS HK

**Number of MAU growth in internet categories**



Source: Bloomberg Finance L.P., DBS HK

**Food delivery user distribution in different city level**

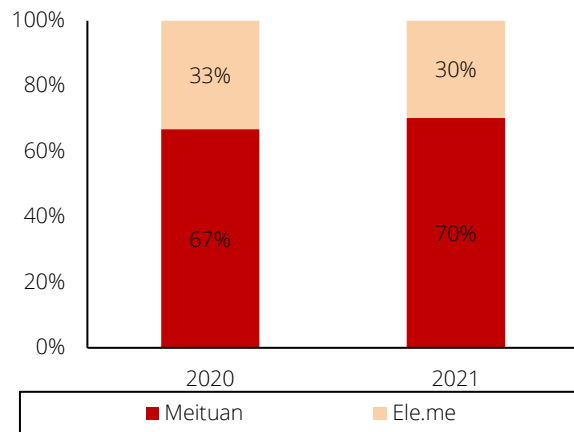


Source: Aurora Mobile, DBS HK

**Expansion into non-food categories.** Delivery players are expanding their merchant networks and product coverages to meet users' growing demands for convenient life. The quick commerce model creates synergies with its food-delivery business by (1) maximising rider network especially during non-peak food delivery hour and (2) increasing customer stickiness and spending on the platform, (3) increasing future ads potential. In 3Q21, Meituan's GTV for supermarket grew 140% and Ele.me's order numbers from pharmacies and liquor stores also grew over 100%.

**Duopoly landscape intact.** Meituan has a leading market share of 70% in terms of GTV, while Ele.me takes most of the rest in 2021. Meituan gained market share from 67% to 70% last year, supported by (1) growing number of merchants, (2) superior city-based operation, and (3) stronger presence in lower-tier cities which representing 46% of total food delivery user base.

**Food delivery market size % (Meituan and Ele.me)**

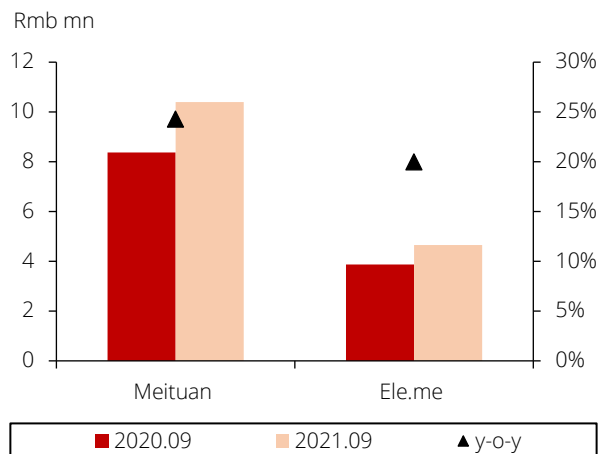


Source: Trustdata, Company, DBS HK



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Monthly active merchant numbers



Source: QuestMobile, DBS HK

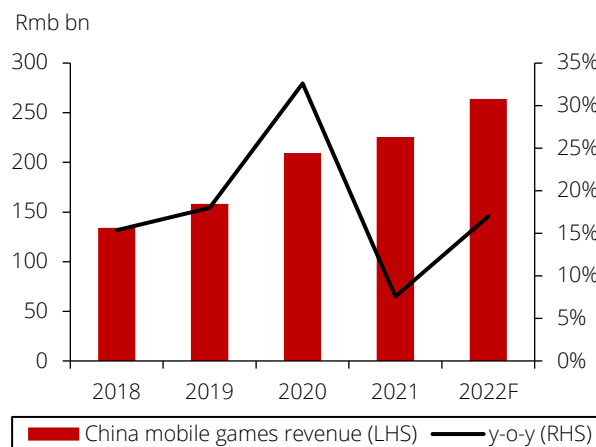
Regulatory Risks

- Absence of “2 choose 1” practice has been in place since 1Q21. The impact is manageable as merchant and user growth remained robust in 3Q21.
- Meituan’s antitrust penalty of Rmb3.44bn has been finalised in 3Q21. Further penalty and changes in market practice should be limited.
- Social security insurance cost on riders is estimated to be Rmb0.5 per order. Based on Meituan’s average order size of Rmb45+, it should be easily absorbed by the platform or passed on to end customers.

Online games: growth to resume, overseas expansion still aggressive

**Stronger growth momentum in 2022.** We expect China's online games revenue to accelerate to 12% y-o-y to 2022 (vs 6.4% in 2021). Mobile games revenue grew faster at 17%, taking up 76% of total online games market, based on market estimates on leading players’ games revenue growth. The overall slowdown in 2021 was mainly due to (1) less spending time as the boost from stay-at-home economy winding down; (2) tightening contents regulations and suspensions of new games licences approval since Aug 21. Given that new regulations targeting minors have been in place, we expect games approve to resume gradually in 2022.

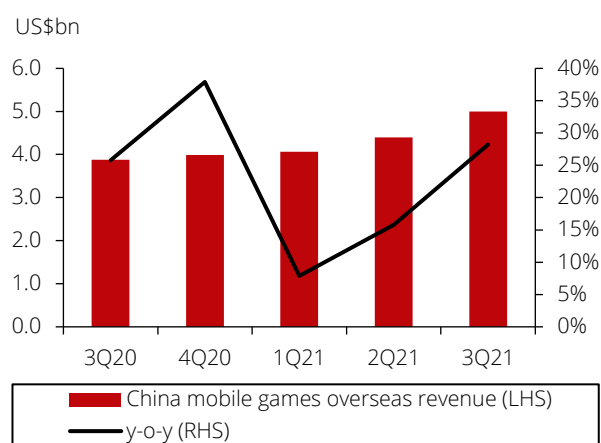
China mobile games revenue growth (2018-2022F)



Source: GPC, DBS HK

**Focus on overseas market expansion.** China self-developed games overseas revenue recorded a robust growth of 28% in 3Q21 (vs 33% in FY20), despite a high base and slower domestic growth. We expect game developers to increase focus on overseas markets, due to (1) more uncertainties in domestic market partly due to tightening regulation; (2) domestic blockbuster games continue to gain more traction overseas; (3) strong government support, as games is one of “cultural product” to seek soft power overseas. In terms of key overseas regions, the top three countries are the US, Japan, and South Korea, contributing 58% of total overseas incomes in 2021.

China mobile games overseas revenue



Source: CNG, DBS HK

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TOP 10 China games revenue from overseas markets

Rank	Name	company
1	Genshin Impact	MiHoYo Games
2	PUBG Mobile	Tencent
3	State of Survival	FUNPLUS
4	Rise of Kingdoms	Lilith Games
5	Puzzles & Survival	Sanqi Interactive
6	Lords Mobile	IGG; Fantasy Plus
7	TOP War: Battle Game	Topwaer Studio
8	Harry Potter : Nafuc Awakend	Netease
9	Mafla City	Yotta Games
10	Mobile Legends: Bang Bang	Moonton Tech

Source: App Annie as of Nov 2021, DBS HK

**Market consolidation post regulatory changes.** Two leading players' games revenue takes up around 80% of China's online games market share in 2021, up from 76% in 2020. They have stronger games pipeline (vs. smaller game developers) and thus short-term games approval suspension will have less impact on revenue.

**Regulatory Risks**

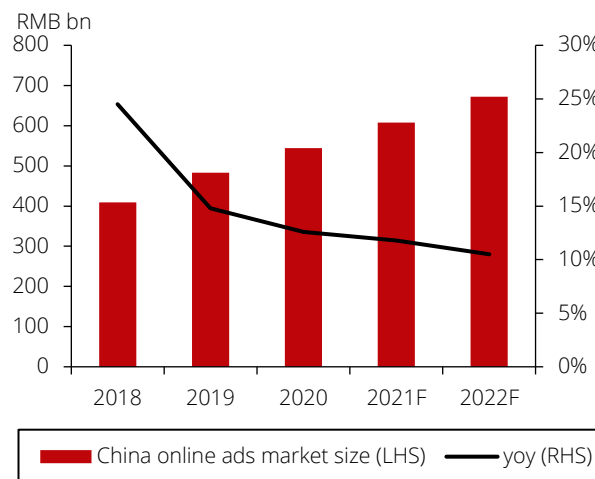
- Regulator launched various policies aiming at cracking down minor's time spent on online games. Note that number of users under 18 was at single digit, and the revenue only accounts for c.1% for leading players such as Tencent and NetEase. The potential financial impact is limited.
- Regulator suspended games approval since Aug 2021. The market believes that the regulator is taking time to execute content control. This was a key de-rating factor last year. We expect resumption in 2022.

**Online advertising: growth under pressure**

**Cautious outlook amid regulatory changes.** We expect china online ads revenue to grow by 11% in 2022F. The overall growth deteriorated in 2H21 due to regulation impact in vertical sectors (like games, education etc.) and macro slowdown.

We expect the weakness to persist into 1H22, which could drag the overall growth of internet platforms, as online advertng is one of the key revenue streams. But certain ads format will register faster growth, such as social media and e-commerce.

China online ads market size (2018-2022F)



Source: iResearch, DBS HK

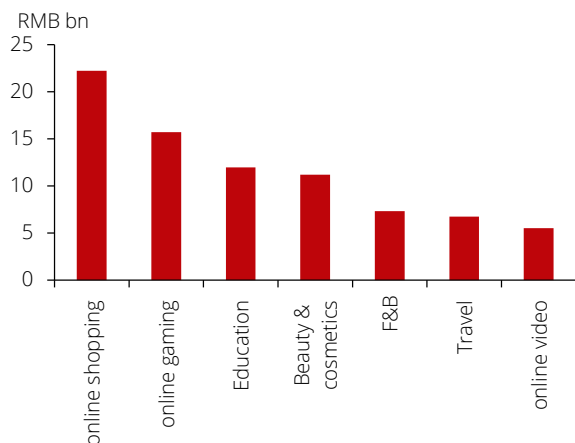
**E-commerce and social media ads gain importance**

Online shopping, online games and education are key vertical sectors and top three key contributor for online ads income.

In terms of ads format, e-commerce and social media accounted for 46.5% and 16.6% respectively in 2021, increasing from 45.9% and 15.2% respectively in 2020. We expect them to continue gain importance in 2022.

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Ads budgets by vertical sectors in 1H21



Source: QuestMobile, DBS HK

Market share of different ads formats

Market share of different ads formats			
	2020	2021F	2022F
E-commerce	45.9%	46.5%	47.8%
Social media	15.2%	16.6%	17.3%
Long video	4.4%	4.3%	4.3%
Short video	13.1%	13.2%	12.9%
News feeds	7.3%	6.2%	5.2%
Search advertising	11.3%	10.4%	9.8%
Others	2.8%	2.8%	2.7%

Source: QuestMobile, DBS HK

Regulatory Risks

- The implementation of Personal Information Protection Law (PIPL) offers user option to withdraw consent for collecting their private data. This may in turn reduce ads ROI, and therefore ads revenue. Our channel check suggests that the opt-out percentage remains limited.

Short video: focus on commercialisation

Commercialisation will support continuous revenue growth of short video. We expect commercialisation to accelerate, despite user growth slowing down. Traffic growth used to be the core revenue driving force from 2018 to 2021. Now, after years of rapid development, short video becomes a key contributor to internet traffic and the growth rate is moderating. There is an ample potential for the so-far inadequate commercialisation. The increase in monetisation rate (such as ad load rate, e-commerce commission rate, and share ratio) will become the new revenue growth driver. In addition, short video platforms will extend to the upstream of industrial chains, expand kinds of physical and service consumption, self-developed games, and improve the supply chain and fulfilment ability of e-commerce etc.

After rapid overseas expansion, monetisation is worth looking forward to.

Both short video and online games sectors achieved remarkable results in overseas market expansion. The commonality is that they rely on the global leading R&D advantages accumulated by the dividends of Chinese engineers and have strong localisation capabilities. In addition, short video and games rely on the relatively mature overseas distribution channel, operating in a relatively light asset mode. Meanwhile, algorithm-based operation replaces complicated contents management, and effectively reducing the influence of cultural differences.

Regulatory Risks

- The core assets of the ads model of short video are data and algorithm. Regulations on the protection of personal information, algorithm policies, and ads content may affect the recommendation of advertisements, which in turn may affect the ads monetisation model.
- However, anti-monopoly has given short video platforms more opportunities to expand live e-commerce and local life service business.

## China Internet Sector

## Regulatory implications for online ads platforms

Key regulation measures	Tencent	JD	Alibaba	Meituan	Baidu	Pinduoduo	Kuaishou	Bilibili
1. Exposure to big data-enabled price discrimination against customers (大數據殺熟)	N/A	√	√	√	√	√	N/A	N/A
2. Ads recommendation based on user's characteristics	√	√	√	√	√	√	√	√
3. Exposure to heavily regulated verticals (e.g. online education)	√	√	√	N/A	N/A	N/A	N/A	N/A

Note: √ - refers to penalty or regulations risks priced in; N/A- non applicable

Source: DBS HK

### Online travel: domestic growth continues despite Covid uncertainty

#### Covid resurgent still the biggest uncertainty in 1H22.

We reckon stricter domestic travel policy in 2H21 due to Covid resurgence and expect it to persist into 1Q22 after Winter Olympic Games. Thus, we expect slower y-o-y growth in 1H22 and momentum to pick up in 2H22. As for overseas travel, border opening is still invisible in the short term.

#### Favour domestic players with higher exposure in lower-tier cities.

We like domestic players such as Tongcheng, which had 90% revenue from domestic travel even before Covid. The growth driver is lower-tier city penetration, given that online travel penetration in lower-tier cities is only 25-30%, while tier 1-2 cities penetration is as high as 40-45%. We expect the growth of Tongcheng to recover faster than the sector. We do not see major regulatory risks for the segment.

### Conclusion and stock recommendations

Food delivery and e-commerce segments' regulatory risks have been mostly priced in. Food delivery growth remains solid in 2022, driven by "everything to home". E-commerce's growth will be more resilient than online ads, amid macro slow down. Online games segment faces higher uncertainty at least in 1Q22 before resumption of approval process.

We prefer stocks with lower exposure to regulatory risks and macro slow down. We like JD most, as it is actually a beneficiary of new antitrust law, and it is outperforming the overall e-commerce segment. We also favour Meituan as its core delivery and new CGB business are riding on the growth of lower-tier cities and lower income groups.

**JD (9618 HK, BUY).** We have kept our earnings forecast unchanged for FY21-23. We forecast non-GAAP net profit growth of -13%, 55%, and 45% for FY21F, FY22F, and FY23F respectively. We expect JD to deliver stronger GMV growth than the market, and increase its ads revenue by expanding its 3P marketplace business. Maintain BUY with TP of HK\$419/US\$107 based on SOTP methodology: (1) a 25x PE on FY23F core profit (HK\$275); (2) JD Logistics: based on market value (HK\$40); (3) JD Health: valuation based on market value (HK\$49); (4) JD Digits: valuation as per last financing round (HK\$49); (5) Dada: valuation based on market value (HK\$6).

**Meituan (3690 HK, BUY).** We have kept our forecast unchanged for FY21-23. We forecast revenue growth of 58%, 37%, and 31% for FY21F, FY22F, and FY23F respectively. We expect moderate growth in 1Q and 2Q, partly due to a high base in 1H20, as well as mobility restriction due to recent Covid resurgence. Overall growth momentum will pick up again in 2H22 along with macro recovery. We expect profitability to continue to improve with a narrowing loss from new businesses (such as CGB). Maintain BUY with TP of HK\$342 based on SOTP valuation: Food delivery: 6x FY22F price-to-sales (P/S), (2) In-store, hotel and travel: 25x FY22F earnings, (3) New initiatives and others: 8x FY22F P/S.

**Alibaba (9988, HK, BUY).** We have revised down our non-GAAP net profit forecast by 10%, 8% and 4% for FY3/22F, FY3/23F and FY3/24F due to higher investments. The company's growth focus will be shifting from domestic e-commerce to international business and cloud, etc. The valuation is attractive at 15x FY3/22 P/E, far below the historical average of 28x. Re-iterate BUY with TP of HK\$211/US\$216 based on SOTP methodology: (1) 20x PE on FY3/22 core business (HK\$171); (2) Cloud: 5x Price-to-

## China Internet Sector

sales on FY22F (HK\$22); (3) Digital media and entertainment: (HK\$9).

**Tencent (700 HK, BUY).** We have kept our earnings forecast unchanged for FY21-23. We forecast non-IFRS net profit growth of 12%, 21%, and 18% for FY21F, FY22F, and FY23F respectively. Games approval resumption will be a key share price catalyst in the near term. Fundamentally speaking, given the stronger-than-market games portfolio and pipeline, we expect games segment growth to be maintained at a healthy level of 11% for 2022. We are bullish on the long-term outlook of the WeChat ecosystem. Maintain BUY with TP of HK\$671 based on SOTP methodology: (1) 25x FY22F core net profit (HK\$521) and (2) Fair value of listed investee companies (HK\$150).

**Tongcheng (780 HK, BUY).** We have kept our forecast unchanged for FY21-23. We forecast non-IFRS net profit growth of 36%, 29%, and 49% for FY21F, FY22F, and FY23F. Tongcheng's near-term outlook and profitability will very much depend on domestic travel restriction. However, the long-term outlook remains intact, supported by the expansion of lower-tier cities with low online travel penetration of 25-30%, vs. tier 1-2 cities' 40-45%. Maintain BUY with TP of HK\$25 based on 18x FY23F adjusted EPS.

**Pinduoduo (PDD US, BUY).** We have kept our forecast unchanged for FY21-23. We forecast revenue growth of 69%, 30%, and 28% for FY21F, FY22F, and FY23F respectively. Pinduoduo's revenue growth started moderating last year, vs. FY20's c.97% growth; but it was still the highest in the industry. Pinduoduo has 700m+ MAU which represents ample monetisation potential. Share price correction is overdone. Upgrade to BUY with a TP of US\$96, based on 6x FY22F P/S, largely in line with leading players' historical average.

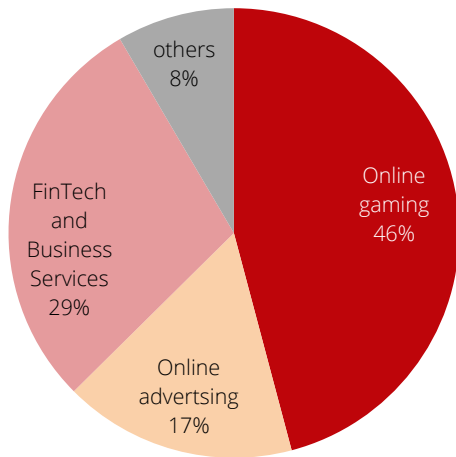
**Baidu (9888 HK, BUY).** We have kept our forecast unchanged for FY21-23. We forecast revenue growth of -9%, 15%, and 19% for FY21F, FY22F, and FY23F respectively. Baidu's ads demand should remain sluggish in 1H22 due to macro slowdown, which should be well expected by the market. In the longer term, we expect Baidu to benefit from the growing demand for cloud and monetisation of autonomous driving investments. Maintain BUY with TP of HK\$210/US\$216 based on SOTP methodology: (1) Baidu core: 12x on FY22F non-GAAP net profit (HK\$122); (2) Cloud: 5x FY22F Price-to-sales (HK\$45); (3) Autonomous driving: (HK\$29) and (4) Market value of major listed investees (HK\$14).

**Kuaishou (1024 HK, BUY).** We have kept our earnings forecast unchanged for FY21-23. We forecast revenue

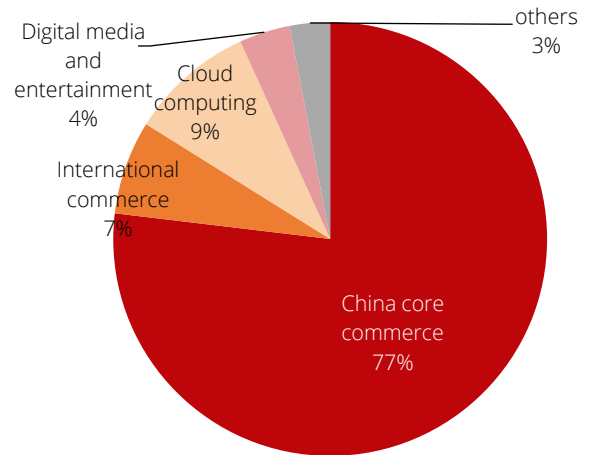
growth of 48%, 33%, and 27% for FY21F, FY22F, and FY23F respectively. We expect its ads and e-commerce to maintain rapid growth in 2022. Despite the stock being overcorrected, we are confident that Kuaishou's underlying values are "inclusive and fair", decentralised traffic distribution, and unique community concepts will enable it to maintain leading position in short video. Its high user spending time and user base represent huge potential for commercialisation. Maintain BUY with TP of HK\$131 based on SOTP valuation methodology: (1) 4x FY22F P/S for the Community & Online marketing services/ live streaming segments; (2) 0.15x FY22F P/GMV for e-commerce business.

**Bilibili (9626 HK, BUY).** We have kept our earnings forecast unchanged for FY21-23. We forecast revenue growth of 58% and 47% for FY21F and FY22F. Bilibili is a unique platform as one of the leaders in China's online video and social community sector. After rapid user expansion, Bilibili is still likely to keep users growing at a healthy clip, while keeping them engaged, especially as it grows its active content creators, improves quality user-generated content, and manages to maintain its community culture. Bilibili to appeal to a wider user base and build more comprehensive online entertainment platform, which in turn should result in expanded total addressable market and monetization opportunities. Maintain BUY with TP of HK\$947 based on 10x FY22F P/S.

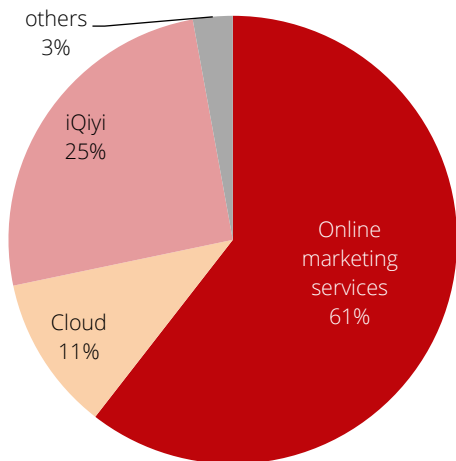
Revenue mix - Tencent (FY21)



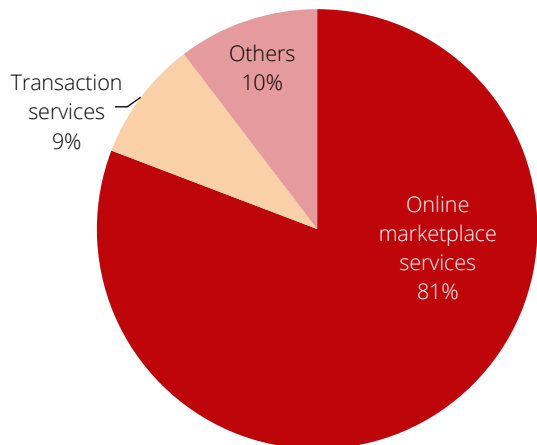
Revenue mix - Alibaba (FY3/22)



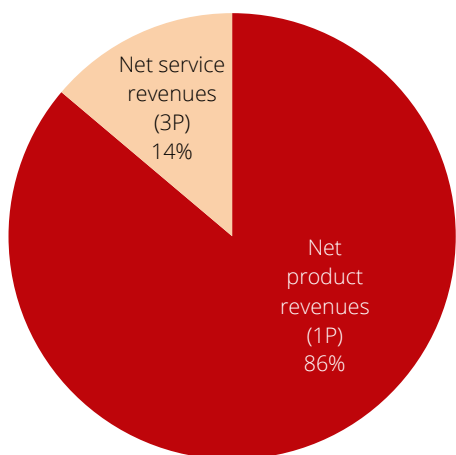
Revenue mix - Baidu (FY21)



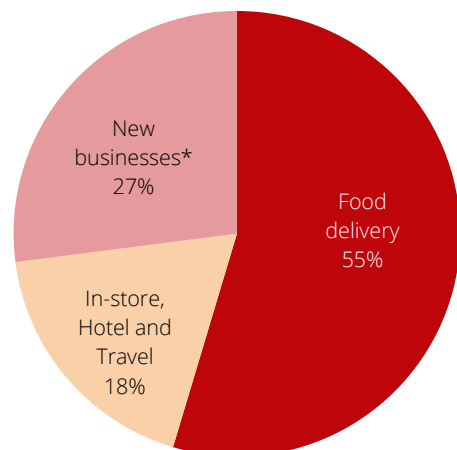
Revenue mix - Pinduoduo (FY21)



Revenue mix - JD (FY21)



Revenue mix - Meituan (FY21)



Source: Company, DBS HK

## Peers table

Company Name	Code	Currency	Price Local\$	Mkt Cap US\$m	Fiscal Yr	PE	PE	P/S	P/S	EV/EBITDA		ROE	ROE
						21F	22F	21F	22F	21F	22F	21F	22F
						x	x			x	x	%	%
<b>China internet platform</b>													
Alibaba Group*#	9988 HK	HKD	133.00	370,423	Mar	18.3	15.4	2.7	2.2	14.7	11.3	12.6	12.8
Alibaba Group*#	BABA US	USD	137.41	373,504	Mar	18.4	15.5	2.7	2.2	14.8	11.4	12.6	12.8
Baidu 'A' *	BIDU US	USD	159.36	55,467	Dec	10.2	23.2	2.9	2.5	4.9	7.7	16.3	6.0
Baidu 'A'*	9888 HK	HKD	155.40	6,942	Dec	10.2	23.2	2.9	2.6	4.9	7.7	16.3	6.0
Bilibili *	BILI US	USD	41.70	16,025	Dec	n.a.	n.a.	5.4	3.6	(105.0)	(92.0)	(62.0)	(76.5)
Bilibili 'Z'*	9626 HK	HKD	333.0	16,425	Dec	n.a.	n.a.	5.5	3.7	(30.9)	(26.9)	(62.0)	(76.5)
JD.com*	9618 HK	HKD	305.20	60,848	Dec	37.6	25.1	0.8	0.7	17.7	12.7	5.1	7.1
JD.com*	JD US	USD	76.40	118,670	Dec	73.3	48.9	0.8	0.7	40.4	29.4	5.1	7.1
Kuaishou Technology*	1024 HK	HKD	85.7	46,467	Dec	n.a.	n.a.	3.4	2.6	(4.0)	(179.9)	138.7	(17.3)
Meituan*	3690 HK	HKD	227.00	178,780	Dec	n.a.	n.a.	6.3	4.6	(58.9)	574.8	(26.8)	(4.9)
Netease	NTES US	USD	106.01	71,131	Dec	25.8	21.8	5.2	4.5	21.5	17.8	17.5	18.8
Pinduoduo*	PDD US	USD	60.38	74,811	Dec	356.7	91.9	4.8	3.7	705.2	58.2	2.2	7.5
Tencent Holdings*	700 HK	HKD	480.80	592,991	Dec	22.6	19.2	6.6	5.5	15.5	13.3	21.0	20.0
Tongcheng-Elong*	780 HK	HKD	14.60	4,156	Dec	37.6	24.3	3.5	2.6	20.7	11.6	4.6	6.5
Trip Com Group	TCOM US	USD	24.86	15,847	Dec	148.0	41.0	5.1	4.1	112.1	33.3	0.5	2.3
Weibo Adr 1:1	WB US	USD	35.1	8,540	Dec	11.4	10.5	3.8	3.4	6.9	6.2	17.7	17.2
<b>Average</b>						<b>51.1</b>	<b>25.6</b>	<b>3.4</b>	<b>2.7</b>	<b>70.5</b>	<b>50.8</b>	<b>18.9</b>	<b>5.8</b>

# FY21: FY22; FY22: FY23

Source: Thomson Reuters, \*DBS HK

## Share performance table

Share price performance (%)	1-mth	3-mth	6-mth	12-mth	YTD
Alibaba Group (BABA US)	9.9	(15.7)	(33.1)	(39.1)	15.7
Baidu (BIDU US)	6.7	(0.1)	(11.7)	(33.4)	7.1
JD.com (JD US)	(4.2)	(2.6)	4.4	(13.7)	9.0
Meituan (3690 HK)	(6.6)	(15.6)	(20.4)	(24.8)	0.7
Pinduoduo (PDD US)	(5.1)	(35.4)	(45.4)	(64.4)	3.6
Tencent (700 HK)	3.8	(0.5)	(10.0)	(18.5)	5.3
Tongcheng (780 HK)	(16.7)	(24.0)	(23.0)	0.7	1.1
<b>HSI Index</b>	<b>1.7</b>	<b>(2.2)</b>	<b>(11.3)</b>	<b>(13.7)</b>	<b>4.3</b>
<b>HSTECH Index</b>	<b>(2.2)</b>	<b>(4.8)</b>	<b>(21.5)</b>	<b>(32.4)</b>	<b>4.0</b>

Source: Thomson Reuters, \*DBS HK



# China/Hong Kong Company Update

## Alibaba Group

Bloomberg: 9988 HK Equity | BABA US Equity | Reuters: 9988.HK | BABA.N

Refer to important disclosures at the end of this report.

DBS Group Research . Equity

13 Jan 2022

### HK: BUY

Last Traded Price ( 12 Jan 2022): HK\$133.00 (HSI : 24,402)  
Price Target 12-mth: HK\$211 (58.6% upside) (Prev HK\$228)

### US: BUY

Last Traded Price ( 12 Jan 2022): US\$137.41 (NASDAQ : 15,188)  
Price Target 12-mth: US\$216 (57.2% upside) (Prev US\$234)

#### Analyst

Tsz-Wang TAM, CFA +852 36684195 tszwangtam@dbs.com  
Lilian LV lilianlv@dbs.com

### What's New

- Revised down non-GAAP net profit forecast by 10%, 8%, and 4% for FY3/22F, FY3/23F, and FY3/24F due to higher investments and slower core business growth
- Growth focus will be shifting from domestic e-commerce to international business and cloud
- The valuation is attractive at c.15x forward PE, much lower than the historical average of 28x
- Maintain BUY with lower TP of HK\$211/US\$216

## Encouraging user growth and promising cloud outlook

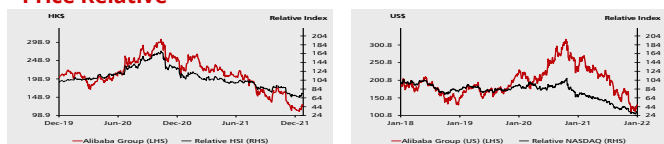
### Investment Thesis

Largest e-commerce platform with marketplaces as a key driver. Alibaba continues investing in community marketplaces to deepen penetration into lower-tier cities via multiple consumer touch points in its ecosystem like Taobao Deals and Taobao Grocery.

**Cloud leader in China.** Alibaba leads the China cloud services market with 39% of market share in 2020, which is expected to grow at c.43% CAGR during FY20-23. Alibaba Cloud has benefited from a larger client base and strong demand from merchants.

**International e-commerce new engine driver.** Alibaba sees accelerated growth to the international e-commerce market; and it is well positioned to capitalise on the Southeast Asia market by leveraging its existing supply chain and logistics networks.

### Price Relative



### Forecasts and Valuation (H Shares)

FY Mar (RMBm)	2021A	2022F	2023F	2024F
Turnover	717,289	873,163	1,072,864	1,303,122
EBITDA	152,153	139,302	171,598	218,315
Pre-tax Profit	172,562	159,302	191,598	238,315
Net Profit	150,308	128,276	152,498	187,536
Core profit)	179,009	148,276	172,498	207,536
Core Profit Gth (%)	26.6	(14.7)	18.9	23.0
EPS (RMB)	6.95	5.93	7.05	8.67
EPS (HK\$)	8.52	7.27	8.64	10.63
EPS Gth (%)	(2.1)	(14.7)	18.9	23.0
Diluted EPS (HK\$)	8.38	7.15	8.50	10.45
DPS (HK\$)	0.00	0.00	0.00	0.00
BV Per Share (HK\$)	52.94	61.87	72.18	84.46
PE (X)	15.6	18.3	15.4	12.5
P/Cash Flow (X)	10.1	10.2	9.2	8.1
P/Free CF (X)	12.4	13.2	11.6	9.9
EV/EBITDA (X)	14.0	14.7	11.3	8.3
Net Div Yield (%)	0.0	0.0	0.0	0.0
P/Book Value (X)	2.5	2.1	1.8	1.6
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE(%)	17.8	12.6	12.8	13.5
Earnings Rev (%)		(10)	(8)	(4)
Consensus EPS (RMB)		6.46	7.29	8.44
Other Broker Recs:		B:38	S:0	H:2

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

### Valuation:

We derive our TP of HK\$211/US\$216 based on SOTP methodology: (1) 20x PE on FY3/22 core business (HK\$171); (2) Cloud: 5x price -to -sales on FY22F (HK\$22); and (3) Digital media and entertainment: (HK\$9).

### Where we differ:

**More optimistic on e-commerce growth.** We believe Alibaba will capture a sizeable market share in the fast-growing e-grocery segment, leveraging on its resources in new retail, supply chain and logistics, leading to revenue upside.

### Key Risks to Our View:

(1) Policy risks from regulators; (2) intense competition from other e-commerce platforms; and (3) earnings drag from investments in new initiatives.

### At A Glance

Issued Capital (m shrs)	21,699
Mkt Cap (HK\$m/US\$m)	2,885,967 / 370,423
Major Shareholders (%)	
Free Float (%)	100.0
3m Avg. Daily Val. (US\$m)	648.34
GICS Industry: Information Technology / Software & Services	



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## Alibaba Group

### Company Background

Alibaba is China's largest e-commerce platform company, with Taobao and Tmall having monthly active users (MAUs) of over 800m. It has an extensive e-commerce ecosystem including Alipay, Cainiao Logistics, and AliCloud. Its revenue is derived from e-commerce (86%), cloud computing (8%), digital media & entertainment (5%) (i.e., Youku Tudou and UCWeb), and innovation initiatives and others (1%) (i.e., Dingtalk and AutoNavi).

### Income Statement (RMB m)

FY Mar	2021A	2022F	% chg	yoy
Revenue	717,289	873,163		21.7
Cost of Goods Sold	(421,205)	(523,898)		24.4
<b>Gross Profit</b>	<b>296,084</b>	<b>349,265</b>		<b>18.0</b>
Other Opng (Exp)/Inc	(206,406)	(269,964)		30.8
<b>Operating Profit</b>	<b>89,678</b>	<b>79,302</b>		<b>(11.6)</b>
Other Non Opg (Exp)/Inc	7,582	5,000		(34.1)
Associates & JV Inc	6,984	5,000		(28.4)
Net Interest (Exp)/Inc	68,318	70,000		2.5
Exceptional Gain/(Loss)	0	0		nm
<b>Pre-tax Profit</b>	<b>172,562</b>	<b>159,302</b>		<b>(7.7)</b>
Tax	(29,278)	(39,825)		36.0
Minority Interest	7,294	9,000		23.4
<b>Net Profit</b>	<b>150,308</b>	<b>128,276</b>		<b>(14.7)</b>
Net Profit before Except.	150,578	128,476		(14.7)
EBITDA	152,153	139,302		(8.4)
<b>Margins &amp; Ratio</b>				
Gross Margins (%)	41.3	40.0		
Opg Profit Margin (%)	12.5	9.1		
Net Profit Margin (%)	21.0	14.7		

Source: Company, DBS HK

### Historical PE and PB band

Forward PE band (x)



PB band (x)



Source: Thomson Reuters, DBS HK

## Alibaba Group

### Key Assumptions

FY Mar	2020A	2021A	2022F	2023F	2024F
China GMV (Rmb bn)	6,589.0	7,494.0	8,552.9	9,408.2	10,349.0
Annual active users (m)	726.0	811.0	916.4	1,008.1	1,108.9
Monetisation rate	0.0	0.0	0.0	0.0	0.0

Source: Company, DBS HK

### Segmental Breakdown (RMB m)

FY Mar	2020A	2021A	2022F	2023F	2024F
<b>Revenues (RMB m)</b>					
Core commerce	436,104	621,146	748,886	918,746	1,111,011
Cloud computing	40,016	60,120	84,168	109,418	142,244
Digital media and entertainment	26,948	31,186	34,305	37,735	41,509
Others	6,643	4,837	5,804	6,965	8,358
<b>Total</b>	<b>509,711</b>	<b>717,289</b>	<b>873,163</b>	<b>1,072,864</b>	<b>1,303,122</b>

Source: Company, DBS HK

### Income Statement (RMB m)

FY Mar	2020A	2021A	2022F	2023F	2024F
Revenue	509,711	717,289	873,163	1,072,864	1,303,122
Cost of Goods Sold	(282,367)	(421,205)	(523,898)	(638,354)	(768,842)
<b>Gross Profit</b>	<b>227,344</b>	<b>296,084</b>	<b>349,265</b>	<b>434,510</b>	<b>534,280</b>
Other Opng (Exp)/Inc	(135,914)	(206,406)	(269,964)	(322,912)	(375,965)
<b>Operating Profit</b>	<b>91,430</b>	<b>89,678</b>	<b>79,302</b>	<b>111,598</b>	<b>158,315</b>
Other Non Opg (Exp)/Inc	7,439	7,582	5,000	5,000	5,000
Associates & JV Inc	(5,733)	6,984	5,000	5,000	5,000
Net Interest (Exp)/Inc	67,776	68,318	70,000	70,000	70,000
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>160,912</b>	<b>172,562</b>	<b>159,302</b>	<b>191,598</b>	<b>238,315</b>
Tax	(20,562)	(29,278)	(39,825)	(47,899)	(59,579)
Minority Interest	9,083	7,294	9,000	9,000	9,000
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>149,263</b>	<b>150,308</b>	<b>128,276</b>	<b>152,498</b>	<b>187,536</b>
Net Profit before Except.	149,433	150,578	128,476	152,698	187,736
EBITDA	135,563	152,153	139,302	171,598	218,315
<b>Growth</b>					
Revenue Gth (%)	35.3	40.7	21.7	22.9	21.5
EBITDA Gth (%)	42.8	12.2	(8.4)	23.2	27.2
Opg Profit Gth (%)	60.2	(1.9)	(11.6)	40.7	41.9
Net Profit Gth (%)	70.4	0.7	(14.7)	18.9	23.0
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	44.6	41.3	40.0	40.5	41.0
Opg Profit Margin (%)	17.9	12.5	9.1	10.4	12.1
Net Profit Margin (%)	29.3	21.0	14.7	14.2	14.4
ROAE (%)	23.9	17.8	12.6	12.8	13.5
ROA (%)	13.1	10.0	7.1	7.4	7.9
ROCE (%)	8.6	6.2	4.2	5.4	6.8
Div Payout Ratio (%)	0.0	0.0	0.0	0.0	0.0
Net Interest Cover (x)	NM	NM	NM	NM	NM

Source: Company, DBS HK

## Alibaba Group

### Balance Sheet (RMB m)

FY Mar	2020A	2021A	2022F	2023F	2024F
Net Fixed Assets	103,387	147,412	157,412	167,412	177,412
Invt in Associates & JVs	189,632	200,189	235,189	270,189	305,189
Other LT Assets	557,043	699,257	771,257	843,257	915,257
Cash & ST Invt	378,694	518,652	585,854	678,477	804,643
Inventory	0	0	0	0	0
Debtors	84,229	124,708	174,591	244,428	342,199
Other Current Assets	0	0	0	0	0
<b>Total Assets</b>	<b>1,312,985</b>	<b>1,690,218</b>	<b>1,924,303</b>	<b>2,203,762</b>	<b>2,544,700</b>
ST Debt	5,154	13,437	13,437	13,437	13,437
Creditors	161,536	260,929	326,161	407,702	509,627
Other Current Liab	75,182	102,992	122,369	146,589	176,865
LT Debt	120,276	135,716	135,716	135,716	135,716
Other LT Liabilities	71,186	93,510	93,510	93,510	93,510
Shareholder's Equity	764,504	946,143	1,104,619	1,287,318	1,505,054
Minority Interests	115,147	137,491	128,491	119,491	110,491
<b>Total Cap. &amp; Liab.</b>	<b>1,312,985</b>	<b>1,690,218</b>	<b>1,924,303</b>	<b>2,203,762</b>	<b>2,544,700</b>
Non-Cash Wkg. Capital	(152,489)	(239,213)	(273,939)	(309,863)	(344,293)
Net Cash/(Debt)	253,264	369,499	436,701	529,324	655,490
Debtors Turn (avg days)	51.1	53.2	62.6	71.3	82.2
Creditors Turn (avg days)	212.4	206.5	226.1	227.6	232.9
Inventory Turn (avg days)	N/A	N/A	N/A	N/A	N/A
Asset Turnover (x)	0.4	0.5	0.5	0.5	0.5
Current Ratio (x)	1.9	1.7	1.6	1.6	1.6
Quick Ratio (x)	1.9	1.7	1.6	1.6	1.6
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	36.2	29.0	34.9	34.9	34.9
Z-Score (X)	NA	NA	NA	NA	NA

Source: Company, DBS HK

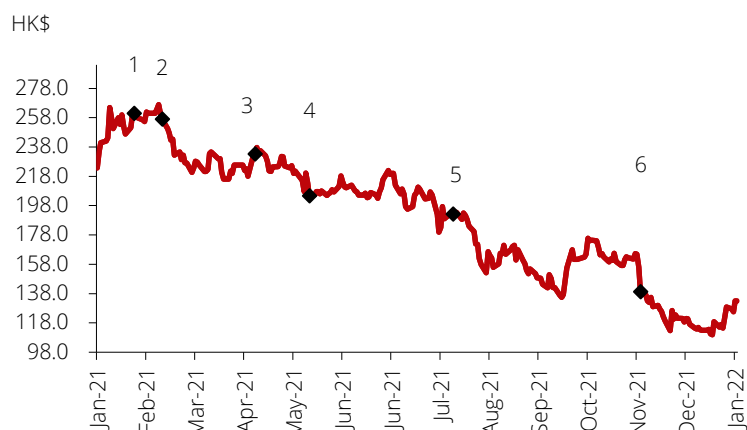
### Cash Flow Statement (RMB m)

FY Mar	2020A	2021A	2022F	2023F	2024F
Pre-Tax Profit	160,912	172,562	159,302	191,598	238,315
Dep. & Amort.	42,427	47,909	50,000	50,000	50,000
Tax Paid	(20,562)	(29,278)	(39,825)	(47,899)	(59,579)
Assoc. & JV Inc/(loss)	5,733	(6,984)	(5,000)	(5,000)	(5,000)
(Pft)/ Loss on disposal of FAs	(77,165)	(58,957)	0	0	0
Chg in Wkg.Cap.	21,418	50,508	34,726	35,924	34,430
Other Operating CF	47,844	56,026	30,000	30,000	30,000
<b>Net Operating CF</b>	<b>180,607</b>	<b>231,786</b>	<b>229,202</b>	<b>254,623</b>	<b>288,167</b>
Capital Exp.(net)	(45,386)	(43,185)	(52,000)	(52,000)	(52,000)
Other Invt.(net)	(36,053)	(165,060)	(80,000)	(80,000)	(80,000)
Invt in Assoc. & JV	(24,410)	(16,123)	(30,000)	(30,000)	(30,000)
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(2,223)	(19,826)	0	0	0
<b>Net Investing CF</b>	<b>(108,072)</b>	<b>(244,194)</b>	<b>(162,000)</b>	<b>(162,000)</b>	<b>(162,000)</b>
Div Paid	0	0	0	0	0
Chg in Gross Debt	(15,953)	31,349	0	0	0
Capital Issues	91,506	(598)	0	0	0
Other Financing CF	(4,700)	(669)	0	0	0
<b>Net Financing CF</b>	<b>70,853</b>	<b>30,082</b>	<b>0</b>	<b>0</b>	<b>0</b>
Currency Adjustments	4,100	(7,187)	0	0	0
Chg in Cash	147,488	10,487	67,202	92,623	126,167
Opg CFPS (RMB)	7.57	8.39	9.00	10.12	11.74
Free CFPS (RMB)	6.43	8.72	8.20	9.37	10.92

Source: Company, DBS HK

**Alibaba Group**

**HK Share - Target Price & Ratings History**

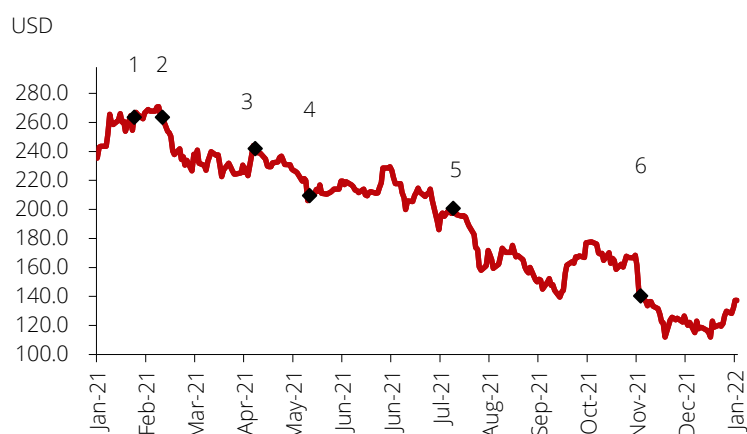


S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	3-Feb-21	HK\$260.00	HK\$315.00	Buy
2:	19-Feb-21	HK\$260.40	HK\$354.00	Buy
3:	13-Apr-21	HK\$232.20	HK\$348.00	Buy
4:	14-May-21	HK\$213.20	HK\$293.00	Buy
5:	4-Aug-21	HK\$193.50	HK\$293.00	Buy
6:	19-Nov-21	HK\$156.00	HK\$228.00	Buy

Source: DBS HK

Analyst: Tsz-Wang TAM, CFA  
Lilian LV

**US Share - Target Price & Ratings History**



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	3-Feb-21	US\$254.50	US\$324.00	Buy
2:	19-Feb-21	US\$264.51	US\$364.00	Buy
3:	13-Apr-21	US\$244.01	US\$358.00	Buy
4:	14-May-21	US\$206.08	US\$301.00	Buy
5:	4-Aug-21	US\$197.38	US\$301.00	Buy
6:	19-Nov-21	US\$143.60	US\$234.00	Buy

Source: DBS HK

Analyst: Tsz-Wang TAM, CFA  
Lilian LV

# China/Hong Kong Company Update

## Pinduoduo Inc

Bloomberg: PDD US Equity | Reuters: PDD.O

Refer to important disclosures at the end of this report.

DBS Group Research . Equity

13 Jan 2022

**BUY** (Upgrade from HOLD)

Last Traded Price (12 Jan 2022): US\$60.38 (NASDAQ : 15,188)

Price Target 12-mth: US\$96.00 (59% upside) (Prev US\$93.00)

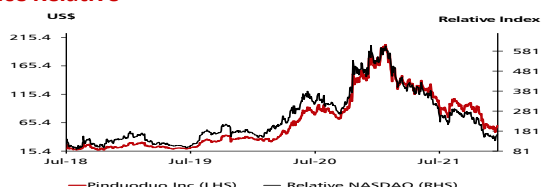
### Analyst

Tsz-Wang TAM, CFA +852 36684195 tszwangtam@dbs.com  
Lilian LV lilianlv@dbs.com

### What's New

- Revenue growth remains higher than the industry with 69%, 30%, and 28% for FY21F, FY22F, and FY23F
- Growth drivers are e-grocery expansion and high monetisation potential with 700m+ MAU
- Share price correction has been overdone given solid revenue growth and improving earnings
- Upgrade to BUY from HOLD with revised TP of US\$96, due to higher revenue growth led by e-grocery expansion

### Price Relative



### Forecasts and Valuation

FY Dec (RMBm)	2020A	2021F	2022F	2023F
Turnover	59,492	100,377	130,282	167,166
EBITDA	(8,226)	449	4,338	18,554
Pre-tax Profit	(7,180)	1,349	5,238	19,454
Net Profit	(7,180)	1,349	5,238	19,454
Non-GAAP net profit	(2,965)	5,549	9,438	23,654
Non-GAAP profit(gth%)	(30.5)	N/A	70	151
EPS (RMB)	(6.02)	1.08	4.18	15.52
EPS (US\$)	(0.95)	0.17	0.66	2.44
EPS Gth (%)	0.0	N/A	288.4	271.4
Diluted EPS (US\$)	(0.95)	0.17	0.66	2.44
DPS (US\$)	0.00	0.00	0.00	0.00
BV Per Share (US\$)	7.64	8.16	9.26	12.14
PE (X)	nm	356.7	91.9	24.7
P/Cash Flow (X)	16.2	11.8	7.6	4.6
P/Free CF (X)	16.3	12.0	7.7	4.6
EV/EBITDA (X)	nm	705.2	58.2	7.9
Net Div Yield (%)	0.0	0.0	0.0	0.0
P/Book Value (X)	7.9	7.4	6.5	5.0
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE(%)	(16.9)	2.2	7.5	22.8
Earnings Rev (%)		40	nm	194
Consensus EPS (RMB)		4.44	8.42	15.22
Other Broker Recs:		B:41	S:1	H:11

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

## Key e-grocery player with huge user base

### Investment Thesis

**Monetisation potential from 700m+ user base.** Pinduoduo's MAU of 700m+ surpassed Alibaba in 2020. This should continuously attract 3P merchants and expand product categories and SKUs, which will drive advertising revenue. We expect higher earnings thanks to improving operating efficiency and more focus on high-margin marketplace business.

**E-grocery a key growth driver.** Duouo grocery is a leading player in Community Group BUY (CGB) with focus on fresh grocery. The online fresh grocery market size is expected to grow at a CAGR of 38% over FY20-23, from its currently low penetration of 12%.

**Stronger revenue growth than leading players.** We expect Pinduoduo's revenue to grow at c.41% CAGR during FY20-FY23F, faster than leading competitors, driven by its steady user growth in lower-tier cities and rising purchase frequency in new categories.

### Valuation:

We have a BUY rating on the counter. We set our TP at US\$96, based on a 6x FY22F price-to-sales (P/S), largely in line with the historical average of leading players.

### Where we differ:

**Higher than consensus GMV growth.** We forecast Pinduoduo's GMV growth at 46% and 34% for FY21F and FY22F, slightly higher than market consensus. We believe its e-grocery expansion is faster than expected, supported by the first-mover advantage and wide user base in lower-tier cities.

### Key Risks to Our View:

(1) Changes in government regulations; (2) Intensifying market competition in e-commerce and CGB; (3) Failure to retain existing users.

### At A Glance

Issued Capital (m shrs)	1,239
Mkt Cap (US\$m)	74,811
Major Shareholders (%)	
Free Float (%)	100.0
3m Avg. Daily Val. (US\$m)	559.08
GICS Industry: Consumer Discretionary / Retailing	



Watchlist the stock on Insights Direct to receive prompt updates



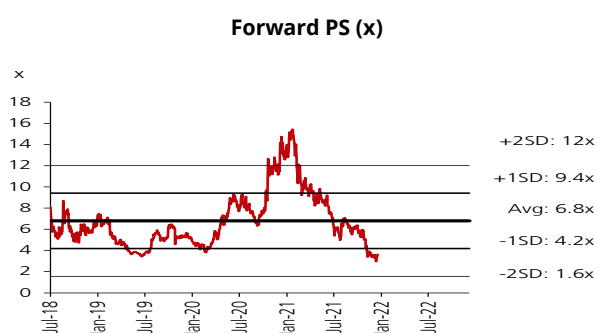
Live more, Bank less

## Pinduoduo Inc

### Company Background

Established in 2014 and listed in 2018, Pinduoduo is the third-largest e-commerce platform in China with a 10% market share in 2019 (any latest number say 2020) in terms of gross merchandise value. The company focuses on agricultural products. Online marketplace services and commission fees accounted for 81% and 10% of its FY20 revenue respectively. HUANG Zheng, its former Chairman and CEO, is the company's largest shareholder. Tencent is the second-largest shareholder.

### Historical PS and PB band



Source: Thomson Reuters, DBS HK

## Pinduoduo Inc

### Key Assumptions

FY Dec	2019A	2020A	2021F	2022F	2023F
GMV (Rmb bn)	1,006.6	1,667.6	2,438.9	3,273.0	4,065.0
No. of active buyers (m)	585.2	788.4	922.4	1,014.7	1,095.8

Source: Company, DBS HK

### Segmental Breakdown (RMB m)

FY Dec	2019A	2020A	2021F	2022F	2023F
<b>Revenues (RMB m)</b>					
Online market place	26,814	47,954	78,044	109,644	142,275
Transaction	3,328	5,787	14,633	19,638	24,390
Merchandise	0	5,751	7,700	1,000	500
<b>Total</b>	<b>30,142</b>	<b>59,492</b>	<b>100,377</b>	<b>130,282</b>	<b>167,166</b>

Source: Company, DBS HK

### Income Statement (RMB m)

FY Dec	2019A	2020A	2021F	2022F	2023F
Revenue	30,142	59,492	100,377	130,282	167,166
Cost of Goods Sold	(6,339)	(19,279)	(37,357)	(43,663)	(55,500)
<b>Gross Profit</b>	<b>23,803</b>	<b>40,213</b>	<b>63,020</b>	<b>86,619</b>	<b>111,666</b>
Other Opng (Exp)/Inc	(32,341)	(49,594)	(63,172)	(82,880)	(93,712)
<b>Operating Profit</b>	<b>(8,538)</b>	<b>(9,380)</b>	<b>(151)</b>	<b>3,738</b>	<b>17,954</b>
Other Non Opg (Exp)/Inc	146	419	0	0	0
Associates & JV Inc	29	84	0	0	0
Net Interest (Exp)/Inc	1,396	1,698	1,500	1,500	1,500
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>(6,968)</b>	<b>(7,180)</b>	<b>1,349</b>	<b>5,238</b>	<b>19,454</b>
Tax	0	0	0	0	0
Minority Interest	0	0	0	0	0
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>(6,968)</b>	<b>(7,180)</b>	<b>1,349</b>	<b>5,238</b>	<b>19,454</b>
Net Profit before Except.	(6,968)	(7,180)	1,349	5,238	19,454
EBITDA	(7,726)	(8,226)	449	4,338	18,554
<b>Growth</b>					
Revenue Gth (%)	129.7	97.4	68.7	29.8	28.3
EBITDA Gth (%)	25.0	(6.5)	N/A	866.7	327.7
Opg Profit Gth (%)	(20.9)	9.9	(98.4)	(2,572.0)	380.2
Net Profit Gth (%)	32.3	(3.0)	N/A	288.4	271.4
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	79.0	67.6	62.8	66.5	66.8
Opg Profit Margin (%)	(28.3)	(15.8)	(0.2)	2.9	10.7
Net Profit Margin (%)	(23.1)	(12.1)	1.3	4.0	11.6
ROAE (%)	(32.1)	(16.9)	2.2	7.5	22.8
ROA (%)	(11.7)	(6.1)	0.7	2.2	6.0
ROCE (%)	(34.1)	(17.4)	(0.2)	4.3	17.6
Div Payout Ratio (%)	N/A	N/A	0.0	0.0	0.0
Net Interest Cover (x)	NM	NM	NM	NM	NM

Source: Company, DBS HK

## Pinduoduo Inc

**Balance Sheet (RMB m)**

FY Dec	2019A	2020A	2021F	2022F	2023F
Net Fixed Assets	558	833	683	533	383
Invt in Associates & JVs	0	0	0	0	0
Other LT Assets	2,497	8,552	8,552	8,552	8,552
Cash & ST Invt	68,635	139,395	181,002	244,804	350,277
Inventory	0	0	0	0	0
Debtors	0	0	0	0	0
Other Current Assets	4,367	10,129	12,709	16,579	22,383
<b>Total Assets</b>	<b>76,057</b>	<b>158,909</b>	<b>202,946</b>	<b>270,467</b>	<b>381,595</b>
ST Debt	899	1,866	1,866	1,866	1,866
Creditors	29,926	53,834	80,751	121,126	181,690
Other Current Liab	14,943	28,182	40,453	58,860	86,471
LT Debt	5,207	14,433	14,433	14,433	14,433
Other LT Liabilities	436	418	418	418	418
Shareholder's Equity	24,647	60,176	65,025	73,763	96,717
Minority Interests	0	0	0	0	0
<b>Total Cap. &amp; Liab.</b>	<b>76,057</b>	<b>158,909</b>	<b>202,946</b>	<b>270,467</b>	<b>381,595</b>
Non-Cash Wkg. Capital	(40,502)	(71,887)	(108,495)	(163,408)	(245,778)
Net Cash/(Debt)	62,529	123,096	164,703	228,505	333,978
Debtors Turn (avg days)	N/A	N/A	N/A	N/A	N/A
Creditors Turn (avg days)	1,511.1	820.6	668.2	855.6	1,006.6
Inventory Turn (avg days)	N/A	N/A	N/A	N/A	N/A
Asset Turnover (x)	0.5	0.5	0.6	0.6	0.5
Current Ratio (x)	1.6	1.8	1.6	1.4	1.4
Quick Ratio (x)	1.5	1.7	1.5	1.3	1.3
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	0.4	0.3	3.7	3.7	3.7
Z-Score (X)	NA	NA	NA	NA	NA

Source: Company, DBS HK

**Cash Flow Statement (RMB m)**

FY Dec	2019A	2020A	2021F	2022F	2023F
Pre-Tax Profit	(6,968)	(7,180)	1,349	5,238	19,454
Dep. & Amort.	638	652	600	600	600
Tax Paid	0	0	0	0	0
Assoc. & JV Inc/(loss)	(29)	(84)	0	0	0
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	14,821	28,197	40,707	62,901	104,573
Other Operating CF	6,358	6,612	(1,949)	(5,838)	(20,054)
<b>Net Operating CF</b>	<b>14,821</b>	<b>28,197</b>	<b>40,707</b>	<b>62,901</b>	<b>104,573</b>
Capital Exp.(net)	(27)	(43)	(600)	(600)	(600)
Other Invt.(net)	(27,868)	(38,077)	0	0	0
Invt in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(424)	(238)	0	0	0
<b>Net Investing CF</b>	<b>(28,320)</b>	<b>(38,358)</b>	<b>(600)</b>	<b>(600)</b>	<b>(600)</b>
Div Paid	0	0	0	0	0
Chg in Gross Debt	7,861	13,930	0	0	0
Capital Issues	7,994	37,869	0	0	0
Other Financing CF	0	0	(1,000)	(1,000)	(1,000)
<b>Net Financing CF</b>	<b>15,855</b>	<b>51,799</b>	<b>(1,000)</b>	<b>(1,000)</b>	<b>(1,000)</b>
Currency Adjustments	450	(140)	0	0	0
Chg in Cash	2,806	41,498	39,107	61,301	102,973
Opg CFPS (RMB)	0.00	0.00	0.00	0.00	0.00
Free CFPS (RMB)	12.79	23.62	32.00	49.71	82.96

Source: Company, DBS HK



**Pinduoduo Inc**

**Target Price & Ratings History**

USD



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	19-Feb-21	US\$195.78	US\$131.00	Fully Valued
2:	18-Mar-21	US\$149.46	US\$131.00	Fully Valued
3:	25-Aug-21	US\$99.12	US\$95.40	Hold
4:	29-Nov-21	US\$68.46	US\$93.00	Hold

Source: DBS HK

Analyst: Tsz-Wang TAM, CFA  
Lilian LV

### China Internet Sector

DBS HK recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**FULLY VALUED** (negative total return, i.e., > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

\*Share price appreciation + dividends

Completed Date: 13 Jan 2022 16:29:38 (HKT)

Dissemination Date: 13 Jan 2022 19:47:44 (HKT)

Sources for all charts and tables are DBS HK unless otherwise specified.

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**DBS Bank (Hong Kong) Limited**13<sup>th</sup> Floor One Island East, 18 Westlands Road, Quarry Bay, Hong Kong

Tel: (852) 3668-4181, Fax: (852) 2521-1812

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DBS Regional Research Offices

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**HONG KONG**

DBS Bank (Hong Kong) Ltd

Contact: Carol Wu

13th Floor One Island East,

18 Westlands Road, Quarry Bay, Hong Kong

Tel: 852 3668 4181

Fax: 852 2521 1812

e-mail: dbsvhk@dbs.com

**MALAYSIA**

AllianceDBS Research Sdn Bhd

Contact: Wong Ming Tek (128540 U)

19th Floor, Menara Multi-Purpose, Capital Square,

8 Jalan Munshi Abdullah 50100, Kuala Lumpur, Malaysia.

Tel.: 603 2604 3333

Fax: 603 2604 3921

e-mail: general@alliancedbs.com

Co. Regn No. 198401015984 (128540-U)

**SINGAPORE**

DBS Bank Ltd

Contact: Janice Chua

12 Marina Boulevard,

Marina Bay Financial Centre Tower 3

Singapore 018982

Tel: 65 6878 8888

e-mail: groupresearch@dbs.com

Company Regn. No. 196800306E

**INDONESIA**

PT DBS Vickers Sekuritas (Indonesia)

Contact: Maynard Priajaya Arif

DBS Bank Tower

Ciputra World 1, 32/F

Jl. Prof. Dr. Satrio Kav. 3-5

Jakarta 12940, Indonesia

Tel: 62 21 3003 4900

Fax: 6221 3003 4943

e-mail: indonesiaesearch@dbs.com

**THAILAND**

DBS Vickers Securities (Thailand) Co Ltd

Contact: Chanpen Sirithanarattanakul

989 Siam Piwat Tower Building,

9th, 14th-15th Floor

Rama 1 Road, Pathumwan,

Bangkok Thailand 10330

Tel. 66 2 857 7831

Fax: 66 2 658 1269

e-mail: research@th.dbs.com

Company Regn. No 0105539127012

Securities and Exchange Commission, Thailand