

Baidu (BIDU US)

Ads recovery on track

Baidu delivered strong 1Q20 results, with topline/bottom line -7%/+219% YoY, 3%/113% above consensus. 2Q20E guidance beat 2%. We are impressed by its effective cost control, and turn more positive on Baidu ads recovery for its strong traffic and well-executed managed page initiatives. We keep our financial forecast unchanged. Maintain BUY with TP US\$151.2.

- 1Q20 beat on margin surprise.** 1Q20 revenue was RMB22.5bn, down 7% YoY, 3% above consensus/ at high-end of guidance, mainly on better-than-expected Baidu Core. Non-GAAP EPS surged 219% YoY, 113% above consensus. Margin surprised on higher-than-expected gross margin (lower TAC) and lighter R&D. 2Q20E revenue guidance came at RMB25-27.3bn, -5% YoY to +4% YoY, with midpoint 2% above consensus. Excluding iQiqi's guidance, Baidu Core was guided at -8% YoY to +2% YoY. We view 1Q20 as a strong quarter, for its effective cost control and solid guidance in 2Q20E.
- Ads recovery on track.** 1Q20 Baidu Core declined 13% YoY, better than our expectation. Baidu App DAU +28% YoY in 1Q20 (vs. +21% YoY in 4Q19), with in-app search queries +45% YoY and feed time spent +51% YoY. Given weak hospital ads demand, healthcare revenue contribution was below 10% YoY in 1Q20, and medical ads monetization was pending for full re-opening. Mgmt mentioned that eCPM would continue to improve after domestic market stabilization, suggesting positive signal for ads sentiment. We turn more positive on its ads recovery, mainly on: 1) strong traffic and user engagement; 2) well-executed managed page initiatives; and 3) resilient online advertisers (e.g. online games, education), coupled with recovery from offline advertisers.
- Disciplined cost control to continue.** 1Q20 Baidu Core's non-GAAP operating margin came in at 22%, above our estimate of 16%. Looking ahead, mgmt guided cost+opex up 10% or teens QoQ in 2Q20E. In the long run, mgmt. expect potential margin expansion with higher productivity, effective cost control and narrowing loss of AI initiatives.
- Maintain BUY.** We keep our financial forecast unchanged, with SOTP-based TP of US\$151.2 (16x FY21E P/E). The stock is trading at 18x/13x FY20/21E P/E, valuation is attractive in our view. Backed by solid results and guidance, we suggest to watch its ads recovery and upside from medical transition and ecosystem monetization.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	102,277	107,413	113,569	129,597	142,039
YoY growth (%)	27.7	5.0	5.7	14.1	9.6
Adj. net income (RMB mn)	23,323	21,375	15,586	21,760	27,189
Adj. EPS (RMB)	66.3	61.8	45.0	62.9	78.5
YoY growth (%)	4.1	-6.9	-27.1	39.6	25.0
Consensus EPS	NA	NA	43.2	60.3	71.5
P/E (x)	12.2	13.1	18.0	12.9	10.3
P/B (x)	1.6	1.6	1.5	1.4	1.3
Yield (%)	0.0	0.0	0.0	0.0	0.0
ROE (%)	16.9	1.3	8.5	10.2	11.2
Net gearing (%)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price	US\$151.2
(Previous TP	US\$151.2)
Up/Downside	+37.5%
Current Price	US\$109.8

China Internet Sector

Sophie Huang
 (852) 3900 0889
 sophiehuang@cmbi.com.hk

Stock Data

Mkt Cap (US\$ mn)	34,549
Avg 3 mths t/o (US\$ mn)	481.9
52w High/Low (US\$)	147/82
Total Issued Shares (mn)	274

Source: Bloomberg

Shareholding Structure

BlackRock	4.8%
Vanguard Group	3.8%
Harding Loevner	3.1%

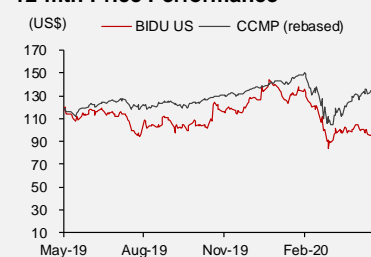
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	-4.9%	-8.7%
3-mth	-25.8%	-19.9%
6-mth	-14.7%	-19.2%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Ernst & Young

Related Reports

- Moving into long-term recovery - 2 Mar 2020
- 3Q19 strong beat on cost efficiency - 8 Nov 2019
- Margin surprise on disciplined cost control - 21 Aug 2019
- 1Q19 miss; A challenging year - 20 May 2019

Figure 1: 1Q20 financial review

Rmb mn	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19	1Q20	QoQ	YoY	Consensus	Diff %
Net revenue	20,907	25,972	28,203	27,195	24,123	26,326	28,080	28,884	22,545	-21.9%	-6.5%	21,920	3%
Revenue	20,907	25,972	22,481	27,195	24,123	26,326	28,080	28,884	22,545	-21.9%	-6.5%	21,920	3%
Operating profit	4,568	5,422	4,428	1,112	(936)	233	2355	4,655	(437)	-109.4%	-53.3%	(1,312)	-67%
Net profit	6,694	6,402	12,396	2,081	(327)	2,412	(6,373)	6,345	41	-99.4%	-112.5%	284	-86%
Adj. net profit	4,585	7,433	6,751	4,703	967	3,635	4,387	9,193	3,082	-66.5%	218.7%	148	1977%
Adj. EPS (Rmb)	16.30	21.06	19.01	13.42	2.77	10.11	12.61	26.54	8.84	-66.7%	219.1%	4.16	113%
Margin (%)													
Gross margin	52.6%	53.8%	49.6%	42.6%	38.5%	38.8%	41.7%	46.3%	34.9%			32.0%	
Operating margin	21.8%	20.9%	19.7%	4.1%	-3.9%	0.9%	8.4%	16.1%	-1.9%			-6.0%	
Adj. net margin	16.4%	28.6%	30.0%	17.3%	4.0%	13.8%	15.6%	31.8%	13.7%			0.7%	
Growth (%)													
Revenue (YoY)	23.8%	24.4%	-4.3%	15.4%	15.4%	1.4%	24.9%	6.2%	-6.5%			-9.1%	
Revenue (QoQ)	-11.2%	24.2%	-13.4%	21.0%	-11.3%	9.1%	6.7%	2.9%	-21.9%			-24.1%	
Operating profit	127.8%	28.8%	-5.8%	-76.7%	-120.5%	-95.7%	-46.8%	318.6%	-53.3%			40.2%	
Adj. net profit	91.4%	33.4%	-25.6%	-15.5%	-78.9%	-51.1%	-35.0%	95.5%	218.7%			-84.7%	

Source: Company data, Bloomberg

Figure 2: 1Q20 revenue breakdown

Rmb mn	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19	1Q20	QoQ	YoY
Total revenue	20,907	25,972	28,203	27,195	24,123	26,326	28,080	28,884	22,545	-22%	-7%
Online marketing services	17,169	21,065	22,481	21,197	17,657	19,327	20,434	20,765	14,243	-31%	-19%
Other services	3,738	4,907	5,722	5,998	6,466	7,089	7,646	8,119	8,302	2%	28%

Source: Company data

Figure 3: CMBIS estimates vs consensus

RMB mn, Dec-YE	CMBIS			Consensus			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	113,569	129,597	142,039	110,505	126,967	141,615	2.8%	2.1%	0.3%
Gross Profit	47,416	56,853	65,321	44,528	55,662	65,632	6.5%	2.1%	-0.5%
Operating Profit	10,733	16,937	23,419	6,902	14,957	21,742	55.5%	13.2%	7.7%
Net profit	15,586	21,760	27,189	14,791	21,650	25,898	5.4%	0.5%	5.0%
EPS (RMB)	45.03	62.86	78.55	43.15	60.26	71.46	4.4%	4.3%	9.9%
Gross Margin	41.8%	43.9%	46.0%	40.3%	43.8%	46.3%	+1.5ppt	+0.0ppts	-0.4ppts
Operating Margin	9.5%	13.1%	16.5%	6.2%	11.8%	15.4%	+3.2ppts	+1.3ppts	+1.1ppts
Net Margin	13.7%	16.8%	19.1%	13.4%	17.1%	18.3%	+0.3ppts	-0.3ppts	+0.9ppts

Source: Company data, Bloomberg, CMBIS estimates

Figure 4: SOTP valuation

US\$bn	Valuation		Methodology	Multiple Applied/Implied		Metrics		Shareholding %
	US\$bn	Per share(US\$)		FY20E	FY21E	FY20E	FY21E	
Baidu Core	25.5	73.8	EV/EBIT	9.0	8.5	2.8	3.0	100%
iQiyi	9.3	26.8	Mkt cap					57%
Ctrip	2.1	6.2	Mkt cap					12%
Net (Debt)/Cash	15.4	44.4	Cash forecasted on Balance sheet					
Equity Value	52	151.2						

Source: CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net Revenue	102,277	107,413	113,569	129,597	142,039
Online marketing	81,913	78,093	81,521	86,412	92,461
Other services	20,365	29,320	32,048	43,185	49,578
COSG	(51,744)	(62,850)	(66,153)	(72,744)	(76,718)
Gross profit	50,533	44,563	47,416	56,853	65,321
R&D	(15,772)	(18,346)	(17,035)	(18,144)	(19,175)
S&GA	(19,231)	(19,910)	(19,647)	(21,772)	(22,726)
Operating profit	15,530	6,307	10,733	16,937	23,419
Interest income	4,451	6,060	6,407	7,312	8,014
Interest exp.	(1,883)	(2,960)	(2,849)	(2,849)	(2,849)
Exchange loss	(122)	(33)	0	0	0
Loss from E.M.I	(79)	(1,254)	0	0	0
Other income	9,428	(8,460)	0	0	0
Pre-tax profit	27,325	(340)	14,291	21,400	28,584
Tax	(4,743)	(1,948)	(2,572)	(3,852)	(5,145)
MI	4,991	4,345	3,516	2,808	1,641
Net profit	27,573	2,057	15,235	20,356	25,080
Adjustment	742	19,318	352	1,404	2,110
Non GAAP Net profit	23,323	21,375	15,586	21,760	27,189

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income	22,582	(2,288)	11,719	17,548	23,439
D&A	9,102	19,879	15,090	19,258	23,751
Change in WC	(5,007)	(1,270)	2,035	2,427	1,290
Others	4,676	5,626	0	0	0
Operating CF	31,353	21,948	28,844	39,233	48,480
Capex	(18,089)	(18,993)	(22,792)	(27,350)	(32,820)
Associates	0	0	0	0	0
Others	(19,336)	3,506	0	0	0
Investing CF	(37,425)	(15,488)	(22,792)	(27,350)	(32,820)
Chg in capital	16,677	(353)	0	0	0
Change of Debts	16,255	(4,072)	0	0	0
Others	(10,306)	3,770	0	0	0
Financing CF	22,626	(655)	0	0	0
Change in cash	16,554	5,805	6,052	11,883	15,660
Cash (beg of yr)	11,084	27,638	33,443	39,495	51,378
FX	0	0	0	0	0
Cash (end of yr)	27,638	33,443	39,495	51,378	67,038
Pledge cash	2,189	996	996	996	996
Cash at balance sheet	29,827	34,439	40,491	52,374	68,034

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	142,472	135,754	143,456	151,548	160,617
Fixed asset	17,903	18,311	21,393	25,220	29,912
Long term investment	80,454	69,410	69,410	69,410	69,410
Intangible assets	27,717	26,137	30,756	35,021	39,399
Others	16,398	14,564	14,564	14,564	14,564
Current assets	155,094	165,562	171,298	184,184	200,622
Cash	29,827	34,439	40,491	52,374	68,034
Account receivable	6,015	7,416	7,100	8,102	8,880
Associates	785	1,594	1,594	1,594	1,594
Others	119,252	123,707	123,707	123,707	123,706
Current liabilities	56,853	57,380	59,099	62,528	64,596
Borrowings	3,130	3,355	3,355	3,355	3,355
Payables	42,719	43,763	45,482	48,911	50,979
Associates	1,727	2,231	2,231	2,231	2,231
Others	9,277	8,031	8,031	8,031	8,030
Non-current liabilities	65,677	72,230	72,230	72,230	72,230
Long term liabilities	50,191	45,894	45,894	45,894	45,894
Deferred taxation	4,099	3,273	3,273	3,273	3,273
Others	11,387	23,063	23,063	23,063	23,063
MI	12,139	8,107	4,591	1,784	143
S/H equity	162,897	163,599	178,834	199,190	224,269
Total Equity	175,036	171,706	183,425	200,973	224,412

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Online marketing	80.1	72.7	71.8	66.7	65.1
Other services	19.9	27.3	28.2	33.3	34.9
Total	100.0	100.0	100.0	100.0	100.0
P&L ratios (%)					
Gross margin	49.4	41.5	41.8	43.9	46.0
Pre-tax margin	26.7	-0.3	12.6	16.5	20.1
Net margin	22.1	-2.1	10.3	13.5	16.5
Tax rate	17.4	-573.5	18.0	18.0	18.0
Balance sheet ratios					
Current ratio (x)	2.7	2.9	2.9	2.9	3.1
Debtors turnover	18.9	22.8	22.8	22.8	22.8
Creditors turnover	249.6	189.9	189.9	189.9	189.9
Inventory turnover	0.0	0.0	0.0	0.0	0.0
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Returns (%)					
ROE	17.4	13.1	8.7	10.9	12.1
ROA	7.8	5.7	3.8	5.6	7.1
Per share					
EPS (RMB)	66	62	45	63	79
DPS (RMB)	0	0	0	0	0
BVPS (RMB)	4,977	4,961	5,299	5,806	6,483

Source: Company data, CMBIS estimates

Disclosures & Disclaimers

Analyst Certification

The research analyst who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

CMBIS Ratings

BUY	: Stock with potential return of over 15% over next 12 months
HOLD	: Stock with potential return of +15% to -10% over next 12 months
SELL	: Stock with potential loss of over 10% over next 12 months
NOT RATED	: Stock is not rated by CMBIS

OUTPERFORM	: Industry expected to outperform the relevant broad market benchmark over next 12 months
MARKET-PERFORM	: Industry expected to perform in-line with the relevant broad market benchmark over next 12 months
UNDERPERFORM	: Industry expected to underperform the relevant broad market benchmark over next 12 months

CMB International Securities Limited

Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

CMB International Securities Limited ("CMBIS") is a wholly owned subsidiary of CMB International Capital Corporation Limited (a wholly owned subsidiary of China Merchants Bank)

Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIS does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIS recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIS, solely for the purpose of supplying information to the clients of CMBIS or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIS nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIS has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIS provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIS may issue other publications having information and/or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIS may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIS may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIS does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIS may have a conflict of interest that could affect the objectivity of this report and CMBIS will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIS.

Additional information on recommended securities is available upon request.

For recipients of this document in the United Kingdom

This report has been provided only to persons (I) falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time) ("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.") of the Order, and may not be provided to any other person without the prior written consent of CMBIS.

For recipients of this document in the United States

This report is intended for distribution in the United States to "major US institutional investors", as defined in Rule 15a-6 under the US, Securities Exchange Act of 1934, and may not be furnished to any other person in the United States. Each major US institutional investor that receives a copy of this research report by its acceptance hereof represents and agrees that it shall not distribute or provide this research report to any other person.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBISG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBISG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBISG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBISG at +65 6350 4400 for matters arising from, or in connection with the report.