

# Baidu (BIDU US)

## Ads headwinds to linger in 4Q21E & 1Q22E

Baidu delivered solid 3Q21 and in-line guidance, with rev/adj. EPS +13% YoY/-28% YoY, 0%/20% above consensus. 4Q21E rev guidance was 2-12% YoY growth, midpoint largely in line. We expect ads headwinds to continue in 4Q21E & 1Q22E (forecasting marketing rev flat YoY in 4Q21E), given soft macro, COVID-19 and tightening regulations. AI Cloud growth might slow down in 4Q21E given high base, but we keep positive on its LT potential. We forecast Baidu Core OPM -5ppts QoQ in 4Q21E, to reflect prudent ads sentiment and non-ads investment. We trimmed its earnings by 11-18% in FY21/22/23E, and lowered SOTP-based TP to US\$218.8. Multiple downside risk is limited, but lack catalysts in the near term.

- 3Q21 margin beat, with largely in-line guidance.** 3Q21 rev was RMB31.9bn, +13% YoY, in line with consensus. Non-GAAP EPS declined 28% YoY, 20% above consensus. Margin beat on higher gross margin. 4Q21E guidance came in at RMB31.0-34.0bn, 2-12% YoY growth, with midpoint 0.7% below consensus.
- Ads pressure to continue in 4Q21E & 1Q22E.** 3Q21 Baidu Core +15% YoY (vs. +27% in 2Q21), 1% above our expectation. Excluding IQ's rev guidance of -5% to -1% YoY, Baidu Core will grow at 5-16% YoY in 4Q21E. We expect ads pressure to continue in 4Q21E & 1Q22E (forecasting marketing rev flat YoY in 4Q21E), given soft macro, COVID-19 and tightening regulations. PIPL impact would be limited, and mgmt. expect ads to benefit from dismantling walled garden (e.g. ecommerce vertical). Non-ads strong momentum continued, as AI Cloud rev accelerated to +73% YoY (vs. +71% in 2Q21), largely above industrial growth. We are positive on its AI Cloud potential (backed by ACE smart transportation expansion), but 4Q21E growth might slow down given high base. We forecast Baidu Core OPM -5ppts QoQ in 4Q21E, to reflect prudent ads sentiment and non-ads investment.
- Maintain BUY.** To reflect ads headwinds and margin dilution from non-ads biz, we trimmed its earnings by 11-18% in FY21-23E, and lowered SOTP-based TP to US\$218.8 from US\$248.

### Earnings Summary

(YE 31 Dec)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue (RMB mn)	107,413	107,074	123,433	136,891	151,370
YoY growth (%)	5.0	(0.3)	15.3	10.9	10.6
Adj. net income (RMB mn)	18,182	22,020	18,371	20,402	23,989
Adj. EPS (RMB)	52.1	63.9	53.2	58.9	69.0
YoY growth (%)	(23.5)	22.6	-16.8	10.7	17.2
Consensus EPS	NA	NA	54.7	66.0	81.2
P/E (x)	20.0	16.3	19.7	17.7	15.1
P/B (x)	1.7	1.5	1.4	1.3	1.2
Yield (%)	0.0	0.0	0.0	0.0	0.0
ROE (%)	21.3	12.2	9.2	9.5	10.1
Net gearing (%)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash

Source: Company data, Bloomberg, CMBIS estimates

### BUY (Maintain)

Target Price	US\$218.8
(Previous TP)	US\$248.0)
Up/Downside	+35.2%
Current Price	US\$161.8

### China Internet Sector

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### Stock Data

Mkt Cap (US\$ mn)	58,707
Avg 3 mths t/o (US\$ mn)	680.45
52w High/Low (US\$)	354.8/ 132.3
Total Issued Shares (mn)	278

Source: Bloomberg

### Shareholding Structure

T Rowe Price Group	1.3%
Goldman Sachs	1.1%
Baillie Gifford	1.0%

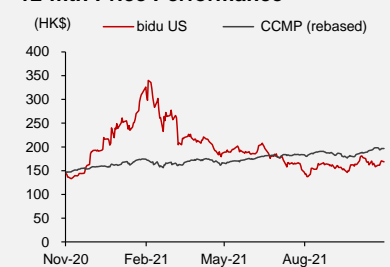
Source: Bloomberg

### Share Performance

	Absolute	Relative
1-mth	3.1%	-3.1%
3-mth	10.6%	3.4%
6-mth	-9.4%	-23.3%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

Auditor: Ernst & Young

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**Figure 1: 3Q21 financial review**

RMB mn	1Q19	2Q19	3Q19	4Q19	1Q20	2Q20	3Q20	4Q20	1Q21	2Q21	3Q21	QoQ	YoY	Consensus	Diff %
Net revenue	24,123	26,326	28,080	28,884	22,545	26,034	28,232	30,263	28,134	31,350	31,921	1.8%	13.1%	31,814	0%
Revenue	24,123	26,326	28,080	28,884	22,545	26,034	28,232	30,263	28,134	31,350	31,921	1.8%	13.1%	31,814	0%
Operating profit	(936)	233	2355	4,655	(437)	3,644	6,156	4,977	2,789	3,463	2,308	-33.4%	-62.5%	2,666	-13%
Adj. net profit	967	3,635	4,387	9,193	3,082	5,082	6,988	6,868	4,297	5,359	5,090	-5.0%	-27.2%	4,297	18%
Adj. EPS (Rmb)	2.77	10.11	12.61	26.54	8.84	14.73	20.35	20.08	12.38	15.41	14.66	-4.9%	-28.0%	12.20	20%
<b>Margin (%)</b>															
Gross margin	38.5%	38.8%	41.7%	46.3%	34.9%	49.6%	54.6%	52.0%	46.7%	49.3%	49.5%			48.0%	
Operating margin	-3.9%	0.9%	8.4%	16.1%	-1.9%	14.0%	21.8%	16.4%	9.9%	11.0%	7.2%			8.4%	
Adj. net margin	4.0%	13.8%	15.6%	31.8%	13.7%	19.5%	24.8%	22.7%	15.3%	17.1%	15.9%			13.5%	
<b>Growth (%)</b>															
Revenue (YoY)	15.4%	1.4%	24.9%	6.2%	-6.5%	-1.1%	0.5%	4.8%	24.8%	20.4%	13.1%			12.7%	
Revenue (QoQ)	-11.3%	9.1%	6.7%	2.9%	-21.9%	15.5%	8.4%	7.2%	-7.0%	11.4%	1.8%			1.5%	
Operating profit	-120.5%	-95.7%	-46.8%	318.6%	-53.3%	1463.9%	161.4%	6.9%	-738.2%	-5.0%	-62.5%			-56.7%	
Adj. net profit	-78.9%	-51.1%	-35.0%	95.5%	218.7%	39.8%	59.3%	-25.3%	39.4%	5.5%	-27.2%			-38.5%	

Source: Company data, Bloomberg

**Figure 2: 3Q21 revenue breakdown**

RMB mn	1Q19	2Q19	3Q19	4Q19	1Q20	2Q20	3Q20	4Q20	1Q21	2Q21	3Q21	QoQ	YoY
<b>Total revenue</b>	<b>24,123</b>	<b>26,326</b>	<b>28,080</b>	<b>28,884</b>	<b>22,545</b>	<b>26,034</b>	<b>28,232</b>	<b>30,263</b>	<b>28,134</b>	<b>31,350</b>	<b>31,921</b>	<b>2%</b>	<b>13%</b>
Online marketing	17,657	19,327	20,434	20,765	14,243	17,688	20,201	20,708	18,094	20,828	21,050	1%	4%
Other services	6,466	7,089	7,646	8,119	8,302	8,346	8,031	9,555	10,040	10,522	10,871	3%	35%

Source: Company data

**Figure 3: CMBIS estimates vs consensus**

RMB mn, Dec-YE	CMBIS			Consensus			Diff (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	123,433	136,891	151,370	125,001	142,544	162,392	-1.3%	-4.0%	-6.8%
Gross Profit	57,549	65,853	73,621	59,922	69,775	81,908	-4.0%	-5.6%	-10.1%
Operating Profit	9,410	11,097	14,586	15,127	18,933	24,955	-37.8%	-41.4%	-41.5%
Adj. net profit	18,371	20,402	23,989	19,180	23,244	29,777	-4.2%	-12.2%	-19.4%
EPS (RMB)	53.17	58.87	69.01	54.70	65.95	81.24	-2.8%	-10.7%	-15.1%
Gross Margin	46.6%	48.1%	48.6%	47.9%	48.9%	50.4%	-1.3ppts	-0.8ppts	-1.8ppts
Operating Margin	7.6%	8.1%	9.6%	12.1%	13.3%	15.4%	-4.5ppts	-5.2ppts	-5.7ppts
Net Margin	14.9%	14.9%	15.8%	15.3%	16.3%	18.3%	-0.5ppts	-1.4ppts	-2.5ppts

Source: Company data, Bloomberg, CMBIS estimates

**Figure 4: Earnings revision**

RMB mn, Dec-YE	New			Old			Diff (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	123,433	136,891	151,370	124,487	142,273	163,320	-0.8%	-3.8%	-7.3%
Gross Profit	57,549	65,853	73,621	59,359	71,457	84,623	-3.0%	-7.8%	-13.0%
Operating Profit	9,410	11,097	14,586	12,054	15,970	20,111	-21.9%	-30.5%	-27.5%
Adj. net profit	18,371	20,402	23,989	20,664	24,779	29,201	-11.1%	-17.7%	-17.8%
EPS (RMB)	53.17	58.87	69.01	59.81	71.51	84.01	-11.1%	-17.7%	-17.9%
Gross Margin	46.6%	48.1%	48.6%	47.7%	50.2%	51.8%	-1.1ppts	-2.1ppts	-3.2ppts
Operating Margin	7.6%	8.1%	9.6%	9.7%	11.2%	12.3%	-2.1ppts	-3.1ppts	-2.7ppts
Net Margin	14.9%	14.9%	15.8%	16.6%	17.4%	17.9%	-1.7ppts	-2.5ppts	-2.0ppts

Source: Company data, CMBIS estimates

**Figure 5: SOTP valuation**

US\$bn	Valuation		Methodology	Multiple Applied/Implied		Metrics		Shareholding %
	US\$bn	Per share(US\$)		FY21E	FY22E	FY21E	FY22E	
Core search + news feed	36.7	106.1	EV/EBIT	10.8	10.0	3.4	3.7	100%
Cloud	8.9	25.7	EV/Sales	5.3	4.0	1.7	2.2	100%
Apollo	5.7	16.6	EV/Sales	5.6	4.0	1.0	1.4	100%
iQiyi	3.2	9.2	Mkt cap					57%
Ctrip	2.2	6.5	Mkt cap					12%
Net (Debt)/Cash	18.9	54.6	Cash forecasted on Balance sheet					
<b>Equity Value</b>	<b>76</b>	<b>218.8</b>						

Source: CMBIS estimates

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Net Revenue</b>	<b>107,413</b>	<b>107,074</b>	<b>123,433</b>	<b>136,891</b>	<b>151,370</b>
Online marketing	78,093	72,840	89,714	96,891	104,642
Other services	29,320	34,234	33,719	40,000	46,728
COSG	(62,850)	(55,158)	(65,884)	(71,037)	(77,750)
<b>Gross profit</b>	<b>44,563</b>	<b>51,916</b>	<b>57,549</b>	<b>65,853</b>	<b>73,621</b>
R&D	(18,346)	(19,513)	(27,155)	(31,485)	(33,302)
S&GA	(19,910)	(18,063)	(20,984)	(23,271)	(25,733)
<b>Operating profit</b>	<b>6,307</b>	<b>14,340</b>	<b>9,410</b>	<b>11,097</b>	<b>14,586</b>
Interest income	6,060	5,358	6,177	6,850	7,575
Interest exp.	(2,960)	(3,103)	(3,382)	(3,382)	(3,382)
Exchange loss	(33)	(660)	0	0	0
Loss from E.M.I	(1,254)	(2,248)	0	0	0
Other income	(8,460)	9,403	9,403	9,403	9,403
<b>Pre-tax profit</b>	<b>(340)</b>	<b>23,090</b>	<b>21,608</b>	<b>23,968</b>	<b>28,182</b>
Tax	(1,948)	(4,064)	(4,754)	(5,752)	(6,764)
MI	4,345	3,446	1,180	1,275	1,499
<b>Net profit</b>	<b>2,057</b>	<b>22,472</b>	<b>18,371</b>	<b>20,402</b>	<b>23,989</b>
Adjustment	19,318	(452)	337	911	1,071
<b>Non GAAP Net profit</b>	<b>21,375</b>	<b>22,020</b>	<b>18,371</b>	<b>20,402</b>	<b>23,989</b>

### Cash flow summary

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Net income</b>	(2,288)	19,026	16,854	18,216	21,418
D&A	19,879	15,090	19,258	23,751	28,854
Change in WC	(1,270)	1,034	(1,485)	1,840	2,587
Others	5,626	(10,950)	0	0	0
<b>Operating CF</b>	<b>21,948</b>	<b>24,200</b>	<b>34,627</b>	<b>43,807</b>	<b>52,859</b>
Capex	(18,993)	(22,792)	(27,350)	(32,820)	(39,384)
Associates	0	0	0	0	0
Others	3,506	(4,760)	0	0	0
<b>Investing CF</b>	<b>(15,488)</b>	<b>(27,552)</b>	<b>(27,350)</b>	<b>(32,820)</b>	<b>(39,384)</b>
Chg in capital	(353)	0	0	0	0
Change of Debts	(4,072)	9,602	0	0	0
Others	3,770	(3,937)	0	0	0
<b>Financing CF</b>	<b>(655)</b>	<b>5,665</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Change in cash</b>	<b>5,805</b>	<b>2,313</b>	<b>7,277</b>	<b>10,987</b>	<b>13,475</b>
Cash (beg of yr)	27,638	33,443	35,544	42,820	53,807
FX	0	(212)	0	0	0
<b>Cash (end of yr)</b>	<b>33,443</b>	<b>35,782</b>	<b>42,820</b>	<b>53,807</b>	<b>67,282</b>
Pledge cash	996	758	758	758	758
Cash at balance sheet	34,439	36,540	43,578	54,565	68,040

### Balance sheet

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Non-current assets</b>	<b>135,754</b>	<b>149,366</b>	<b>165,393</b>	<b>174,462</b>	<b>184,992</b>
Fixed asset	18,311	17,508	25,220	29,912	35,619
Long term investment	69,410	76,233	76,233	76,233	76,233
Intangible assets	26,137	30,705	39,019	43,397	48,220
Others	14,564	15,116	15,116	15,116	15,116
<b>Current assets</b>	<b>165,562</b>	<b>183,342</b>	<b>189,429</b>	<b>201,258</b>	<b>215,638</b>
Cash	34,439	36,540	43,578	54,565	68,040
Account receivable	7,416	8,668	7,717	8,558	9,464
Associates	1,594	726	726	726	726
Others	123,707	138,134	138,134	138,133	138,133
<b>Current liabilities</b>	<b>57,380</b>	<b>68,385</b>	<b>61,197</b>	<b>63,878</b>	<b>67,370</b>
Borrowings	3,355	10,443	10,443	10,443	10,443
Payables	43,763	49,342	46,906	49,587	53,079
Associates	2,231	1,324	1,324	1,324	1,324
Others	8,031	7,276	2,524	2,523	2,523
<b>Non-current liabilities</b>	<b>71,121</b>	<b>72,480</b>	<b>65,265</b>	<b>65,265</b>	<b>65,265</b>
Long term liabilities	45,894	48,408	48,408	48,408	48,408
Deferred taxation	3,273	3,067	3,067	3,067	3,067
Others	21,954	21,005	13,790	13,790	13,790
MI	9,216	9,147	4,865	3,590	2,091
S/H equity	163,599	182,696	203,990	224,392	248,380
<b>Total Equity</b>	<b>172,815</b>	<b>191,843</b>	<b>208,855</b>	<b>227,982</b>	<b>250,471</b>

Source: Company data, CMBIS estimates

### Key ratios

YE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Sales mix (%)</b>					
Online marketing	72.7	68.0	72.7	70.8	69.1
Other services	27.3	32.0	27.3	29.2	30.9
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>P&amp;L ratios (%)</b>					
Gross margin	41.5	48.5	46.6	48.1	48.6
Pre-tax margin	-0.3	21.6	17.5	17.5	18.6
Net margin	-2.1	17.8	13.7	13.3	14.1
Tax rate	-573.5	17.6	22.0	24.0	24.0
<b>Balance sheet ratios</b>					
Current ratio (x)	2.9	2.7	3.1	3.2	3.2
Debtors turnover	22.8	22.8	22.8	22.8	22.8
Creditors turnover	189.9	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
<b>Returns (%)</b>					
ROE	13.1	12.6	9.2	9.5	10.1
ROA	5.7	5.9	4.8	5.1	5.6
<b>Per share</b>					
EPADS (RMB)	61	64	53	59	69
DPS (RMB)	0	0	0	0	0
BVPADS (RMB)	492	548	611	673	746

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