

Zhihu (ZH US)

Strong vocational training with loss narrowing

Zhihu delivered 2Q23 results with in-line rev and upbeat margin. We forecast 3Q23E rev +12% YoY (in line with consensus), with resilient membership and strong vocational training. Membership would see sequential growth in 3Q23E (+42% YoY), backed by richer content and cooperation with Huawei. Vocational training would surge at 119% YoY growth in 3Q23E, driven by both organic and external growth, as well as ramp-up in demand in 2H23E for more examinations. We expect ads to further decline in 3Q23E before sequential recovery in 4Q23E. ZH will prioritize loss-reduction strategy by deepening commercialization and cost reduction in 2H23E/FY24E. To reflect weak ads and cost control, we cut FY23-25E rev by 7%-8%, while earnings barely changed. Our TP was adjusted to US\$2.1.

- **2Q23 slightly beat on margin.** Rev +25% YoY, 1% below consensus. By segment, marketing services continued to decline 14% YoY for macro headwinds and strategy shift toward margin improvement. Paid membership +66% YoY, and vocational training showed strong momentum at 213% YoY growth, mainly on diversified courses and M&A. Non-GAAP net loss narrowed to RMB222mn, vs. consensus of -RMB248mn, thanks to higher GPM (53.8%, 2ppts above consensus) partially offset by increasing S&M expenses. User metrics trended well, with 109.4mn MAU in 2Q23 vs. 102.4mn in 1Q23.
- **Resilient membership and strong vocational training ahead.** We forecast 3Q23E rev +12% YoY (largely in line with consensus), with resilient membership and strong vocational training. Membership would see sequential growth, at 42% YoY in 3Q23E, backed by diversified content and larger user base through cooperating with multiple channels (e.g. Huawei). Vocational training will be on fast trajectory in 3Q23E (+119% YoY), driven by both organic growth and M&A, as well as ramp-up in demand in 2H23E for more examinations to come. Mgmt. expects to see vocational training growth at 100%+YoY in 2H23E. For marketing services, soft macro may linger into 2H23E. We forecast ads to further decline 28% YoY in 3Q23E before sequential recovery in 4Q23E. Mgmt. expects ads to bottom out in 2H23E thanks to ROI-driven products and phasing out of low-margin business.
- **Loss narrowing into 2H23E and FY24E.** ZH will prioritize its loss-reduction strategy by deepening commercialization and cost reduction with prudent investments in 2H23E and FY24E. We expect 3Q23/FY23E GPM to be 53.2%/53.3% and adj.net loss to be RMB234mn/786mn.
- **Maintain BUY.** To reflect weak ads and loss-reduction strategy, we cut FY23-25E rev by 7%-8%, while keep bottom line barely changed. Our DCF-based TP was adjusted to US\$2.1 for currency change and financials adjustment.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	2,959	3,605	4,287	5,269	6,138
YoY growth (%)	118.9	21.8	18.9	22.9	16.5
Adj. net income (RMB mn)	(747)	(1,196)	(786)	(82)	272
Adj. EPS (RMB)	(1.28)	(1.96)	(1.25)	(0.13)	0.42
YoY growth (%)	NA	NA	NA	NA	NA
Consensus EPS (RMB)	NA	NA	(1.4)	(0.5)	0.4
P/E (x)	NA	NA	NA	NA	17.5
P/S (x)	1.4	1.2	1.1	0.9	0.8
Net gearing (%)	0.0	0.0	0.0	0.0	0.0

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	US\$2.1
(Previous TP	US\$2.3)
Up/Downside	+110%
Current Price	US\$1.0

China Entertainment Sector

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Stock Data

Mkt Cap (US\$ mn)	683
Avg 3 mths t/o (US\$ mn)	2.94
52w High/Low (US\$)	2.11/ 0.89
Total Issued Shares (mn)	589

Source: Bloomberg

Shareholding Structure

Qiming Corporate GP	4.04%
Point 72	2.47%
Goldman Sachs	2.33%

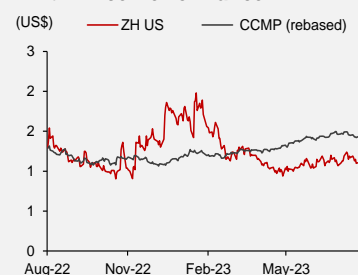
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	1.9%	5.8%
3-mth	4.8%	-1.3%
6-mth	-29.7%	-40.1%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Ernst & Young

Figure 1: 2Q23 financial review

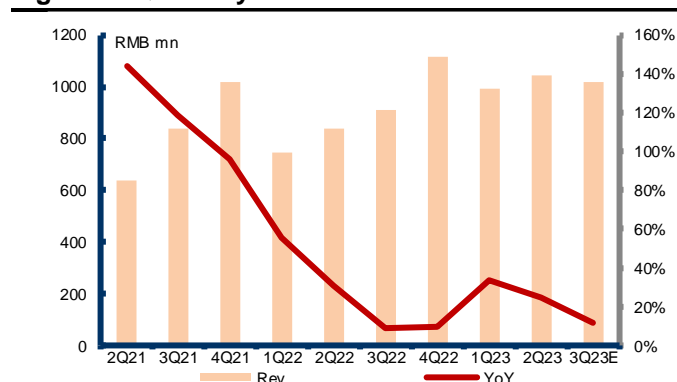
RMB mn, Dec-YE	3Q21	4Q21	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23	QoQ	YoY	Consensus	Diff %
Revenue	823	1,019	743	836	912	1,114	994	1,044	5.0%	24.9%	1,050	-1%
Operating Profit	(363)	(460)	(500)	(526)	(472)	(504)	(437)	(534)	NA	NA	(338)	NA
Net profit	(270)	(383)	(614)	(487)	(300)	(180)	(181)	(280)	NA	NA	(312)	NA
Adj. net profit	(112)	(241)	(367)	(444)	(251)	(134)	(120)	(222)	NA	NA	(248)	NA
Adj. EPS (RMB)	(0.19)	(0.41)	(0.61)	(0.72)	(0.41)	(0.22)	(0.20)	(0.37)	NA	NA	(0.42)	NA
Margin (%)												
Gross margin	51.6%	47.1%	45.1%	47.8%	48.7%	56.4%	51.5%	53.8%			51.6%	
Operating margin	-44.0%	-45.1%	-67.3%	-62.9%	-51.7%	-45.3%	-43.9%	-51.2%			-32.2%	
Adj. net margin	-13.7%	-23.6%	-49.4%	-53.1%	-27.5%	-12.0%	-12.1%	-21.3%			-23.7%	
Growth (%)												
Revenue (YoY)	115.1%	96.1%	55.4%	31.0%	10.7%	9.3%	33.8%	24.9%			25.6%	
Revenue (QoQ)	29.0%	23.8%	-27.1%	12.5%	9.1%	22.2%	-10.7%	5.0%			5.6%	
Operating Profit	NA	NA	NA	NA	NA	NA	NA	NA			NA	
Adj. net profit	NA	NA	NA	NA	NA	NA	NA	NA			NA	

Source: Company data, Bloomberg

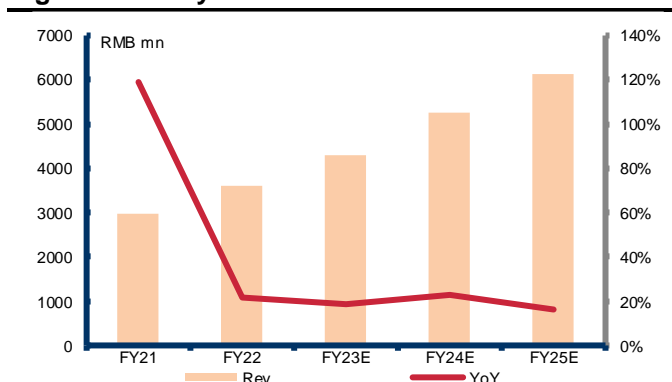
Figure 2: 2Q23 revenue breakdown

RMB mn, Dec-YE	3Q21	4Q21	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23	QoQ	YoY
Total revenue	823	1,019	743	836	912	1,114	994	1,044	5%	25%
Marketing services	599	745	444	478	462	572	392	413	5%	-14%
Paid membership	178	209	222	271	335	403	455	449	-1%	66%
Vocational Training	14	22	40	46	78	85	107	145	35%	213%
Others	32	43	38	41	36	54	40	38	-6%	-7%

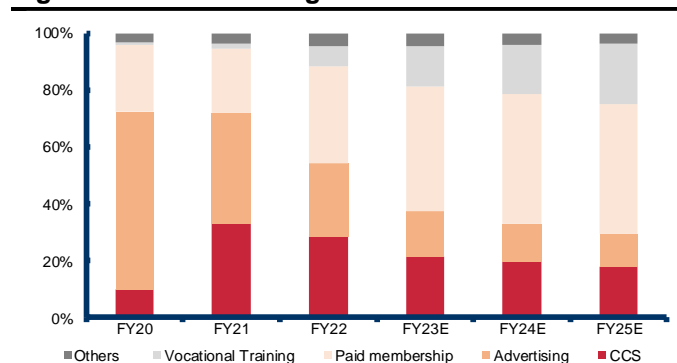
Source: Company data

Figure 3: Quarterly rev estimates

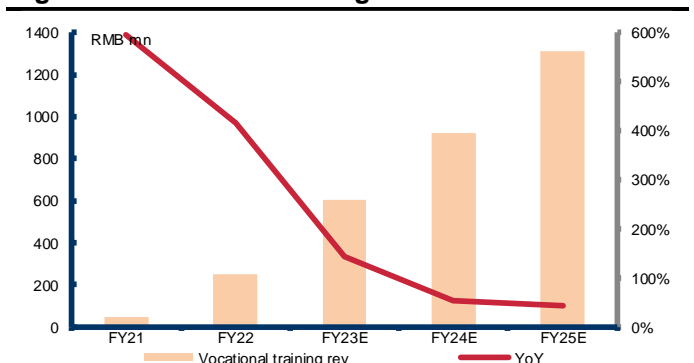
Source: Company data

Figure 4: Yearly rev estimates

Source: Company data, CMBIGM estimates

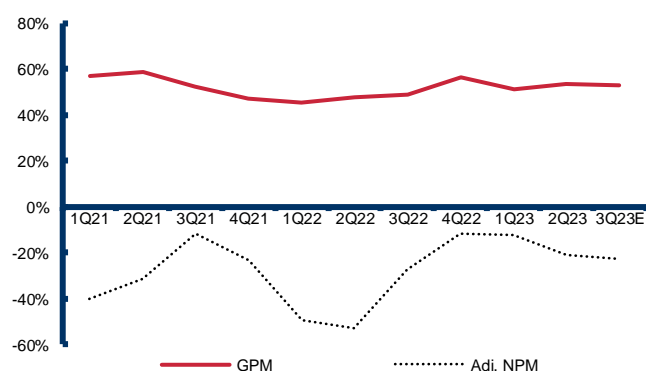
Figure 5: Rev mix change

Source: Company data, CMBIGM estimates

Figure 6: Vocational training rev estimates

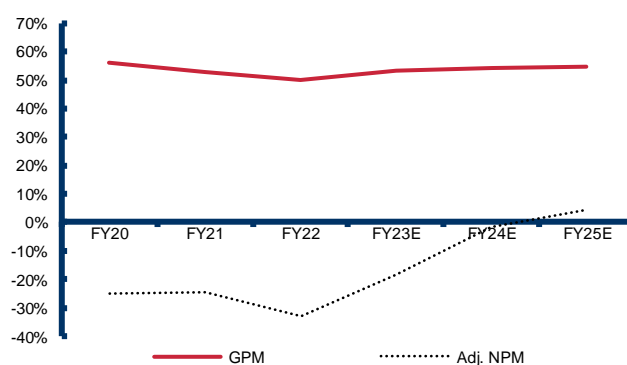
Source: Company data, CMBIGM estimates

Figure 7: Quarterly margin



Source: Company data, CMBIGM

Figure 8: Yearly margin estimates



Source: Company data, CMBIGM estimates

Figure 9: CMBIGM estimates vs consensus

RMB mn, Dec-YE	CMBIGM			Consensus			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	4,287	5,269	6,138	4,628	5,670	6,628	-7.4%	-7.1%	-7.4%
Gross profit	2,283	2,865	3,368	2,387	3,075	3,709	-4.4%	-6.9%	-9.2%
Operating profit	(1,074)	(386)	(40)	(1,229)	(687)	(238)	NA	NA	NA
Adj. net profit	(786)	(82)	272	(833)	(285)	266	NA	NA	2.2%
EPS (RMB)	(1.25)	(0.13)	0.42	(1.41)	(0.49)	0.36	NA	NA	16.5%
Gross margin	53.3%	54.4%	54.9%	51.6%	54.2%	56.0%	+1.7ppts	+0.1ppts	-1.1ppts
Operating margin	-25.1%	-7.3%	-0.6%	-26.6%	-12.1%	-3.6%	+1.5ppts	+4.8ppts	+2.9ppts
Net margin	-18.3%	-1.6%	4.4%	-18.0%	-5.0%	4.0%	-0.3ppts	+3.5ppts	+0.4ppts

Source: Company data, Bloomberg, CMBIGM estimates

Figure 10: Earnings revision

RMB mn, Dec-YE	New			Old			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	4,287	5,269	6,138	4,608	5,669	6,652	-7.0%	-7.1%	-7.7%
Gross profit	2,283	2,865	3,368	2,396	3,044	3,642	-4.7%	-5.9%	-7.5%
Operating profit	(1,074)	(386)	(40)	(1,220)	(404)	(62)	NA	NA	NA
Adj. net profit	(786)	(82)	272	(892)	(80)	273	NA	NA	-0.3%
EPS (RMB)	(1.25)	(0.13)	0.42	(1.42)	(0.12)	0	NA	NA	-0.3%
Gross margin	53.3%	54.4%	54.9%	52.0%	53.7%	54.7%	+1.3ppts	+0.7ppts	+0.1ppts
Operating margin	-25.1%	-7.3%	-0.6%	-26.5%	-7.1%	-0.9%	+1.4ppts	-0.2ppts	+0.3ppts
Net margin	-18.3%	-1.6%	4.4%	-19.4%	-1.4%	4.1%	+1.0ppts	-0.2ppts	+0.3ppts

Source: Company data, CMBIGM estimates

Figure 11: DCF Valuation

DCF valuation (RMB mn)										
	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E	2031E	2032E
EBIT	(814)	(119)	197	272	626	720	806	883	951	1,010
Tax	(7)	0	(6)	(21)	(75)	(108)	(121)	(132)	(143)	(151)
D&A	22	26	28	35	41	46	51	55	60	66
Working capital	(252)	(80)	664	69	59	50	42	36	31	26
CAPEX	(21)	(26)	(31)	(34)	(37)	(40)	(44)	(49)	(54)	(59)
FCF	(1,072)	(199)	851	322	614	667	734	793	846	891
FCF Growth		NA	NA	-62%	91%	9%	10%	8%	7%	5%
Terminal Value										9,836
PV (FCF+ Terminal Value)	(1,072)	(177)	675	227	385	373	365	351	333	3,766

Assumptions

WACC	12.3%
Tax rate	15.0%
Risk free rate	3.2%
Beta	1.10
Market risk return	11.5%
Cost of equity	12.3%
WACC	12.3%
Terminal growth rate	3.0%

Equity Value

PV	5,228
minus: Net cash	4,371
minus: Minority Interest	0
Equity Value	9,599
Shares (mn)	612
Target Price (US\$) based on DCF	2.1

		WACC					
Growth		10.3%	11.3%	12.3%	13.3%	14.3%	
	1.5%	2.4	2.2	2.0	1.9	1.8	
	2.0%	2.4	2.2	2.1	1.9	1.8	
	2.5%	2.5	2.3	2.1	2.0	1.8	
	3.0%	2.6	2.3	2.1	2.0	1.9	
	3.5%	2.7	2.4	2.2	2.0	1.9	
	4.0%	2.8	2.5	2.2	2.1	1.9	
	4.5%	2.9	2.6	2.3	2.1	2.0	

Source: Company data, BBG, CMBIGM estimates

Figure 12: Valuation comps

Company	Ticker	Mkt cap (USD mn)	Currency	Price	CMBI Rating	CMBI TP	PE			PS			FY23-25 EPS CAGR
Zhihu	ZH US	683	USD	1	BUY	2	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	NA
Online Community													
Bilibili	BILI US	6,063	USD	15	BUY	27	NA	NA	52.9	1.9	1.6	1.4	NA
Kuaishou	1024 HK	35,745	HKD	65	BUY	97	41.8	20.6	13.5	2.3	2.0	1.8	78%
Average							41.8	20.6	13.5	2.1	1.8	1.6	78%
VAS													
China Literature	772 HK	4,011	HKD	31	NA	NA	19.6	17.1	15.2	3.7	3.4	3.1	14%
Tencent	700 HK	387,912	HKD	318	BUY	458	19.0	16.1	14.1	4.6	4.1	3.7	15%
JOYY	YY US	2,222	USD	32	BUY	46	15.6	13.2	10.9	1.0	0.9	0.8	21%
Huya	HUYA US	563	USD	2	BUY	6	NA	48.2	12.8	0.6	0.6	0.5	NA
Douyu	DOYU US	327	USD	1	NA	NA	36.5	31.7	24.4	0.4	0.4	0.4	36%
TME	TME US	10,966	USD	6	BUY	9	13.7	12.9	11.6	3.0	2.9	2.6	6%
Mango	300413 CH	7,380	CNY	29	NA	NA	22.8	19.3	16.9	3.4	3.0	2.8	17%
IQIYI	IQ US	4,676	USD	5	BUY	9	14.5	10.1	8.2	1.1	1.0	0.9	32%
Average							17.5	14.8	12.8	1.9	1.7	1.6	20%
Ad													
Baidu	BIDU US	44,874	USD	128	BUY	201	13.1	12.0	10.5	2.4	2.2	2.0	5%
Weibo	WB US	3,096	USD	13	BUY	27	5.9	5.3	4.8	1.7	1.5	1.4	10%
Average							9.5	8.7	7.7	2.0	1.9	1.7	7%
Average							17.9	14.1	11.9	1.9	1.8	1.6	23%

Source: BBG, CMBIGM estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenues	2,959	3,605	4,287	5,269	6,138
CCS	974	1,030	926	1,037	1,106
Advertising	1,161	926	670	692	706
Paid membership	669	1,231	1,894	2,403	2,785
Vocational Training	156	418	797	1,136	1,542
Others					
COGS	(1,405)	(1,797)	(2,004)	(2,404)	(2,770)
Gross profit	1,554	1,808	2,283	2,865	3,368
S&M	(1,635)	(2,026)	(2,048)	(2,015)	(2,154)
R&D	(620)	(763)	(736)	(652)	(661)
G&A	(690)	(622)	(574)	(583)	(593)
Operating profit	(1,391)	(1,604)	(1,074)	(386)	(40)
Other income	97	40	28	37	81
Pre-tax Income	(1,293)	(1,564)	(1,047)	(349)	41
Income Tax	(5)	(14)	(7)	0	(6)
Net profit	(1,299)	(1,578)	(1,054)	(349)	35
Net profit to shareholder	(1,469)	(1,581)	(1,057)	(349)	35
Adj. net profit	(747)	(1,196)	(786)	(82)	272

Cash flow summary

YE 31 Dec (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Net income	(1,299)	(1,578)	(1,054)	(349)	35
D&A	21	25	22	26	28
Change in WC	291	(134)	(252)	(80)	664
Others	546	572	257	263	233
Operating CF	(440)	(1,115)	(1,026)	(139)	960
CAPEX	(7)	(1)	(21)	(26)	(31)
Others	(3,129)	3,491	991	(11)	(12)
Investing CF	(3,137)	3,490	970	(37)	(43)
Issuance of shares	0	0	0	0	0
IPO proceeds	4,853	0	0	0	0
Others	23	(108)	(1,580)	0	0
Financing CF	4,876	(108)	(1,580)	0	0
Net change in cash	1,300	2,267	(1,636)	(176)	917
Cash (beg of yr)	958	2,157	4,526	2,890	2,714
Fx effect					
Cash (end of yr)	2,157	4,526	2,890	2,714	3,631

Balance sheet

YE 31 Dec (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Non-current assets	471	336	248	258	273
PP&E	10	7	28	39	48
Intangible assets, net	68	80	67	66	72
Right-of-use assets	126	126	126	126	126
Others	266	123	26	26	26
Current assets	8,334	7,320	6,692	6,890	7,426
Cash, cash equivalents	2,157	4,526	2,890	2,714	3,631
Term deposits	2,816	948	948	948	948
Short-term investments	2,240	787	1,240	1,240	1,240
Other current asset	1,122	1,058	1,614	1,988	1,607
Current liabilities	1,898	1,825	2,032	2,327	2,610
AP and accruals	1,027	916	961	1,143	1,313
Salary welfare payables	314	284	373	366	382
Contract liabilities	240	356	473	601	696
Others	318	270	225	217	219
Non-current liabilities	169	137	137	137	137
Lease liabilities	73	82	82	82	82
Mezzanine equity and shareholders' equity	6,738	5,694	4,770	4,684	4,953

Key ratios

YE 31 Dec	FY21A	FY22A	FY23E	FY24E	FY25E
Sales mix (%)					
CCS	32.9	28.6	21.6	19.7	18.0
Advertising	39.2	25.7	15.6	13.1	11.5
Paid membership	22.6	34.1	44.2	45.6	45.4
Vocational Training	5.3	11.6	18.6	21.6	25.1
Others	0.0	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	100.0
Growth rate (%)					
Revenue	118.9	21.8	18.9	22.9	16.5
Gross profit	105.1	16.4	26.3	25.5	17.6
EBIT	NA	NA	NA	NA	NA
Adj. net profit	NA	NA	NA	NA	NA
P&L ratios (%)					
Operating margin	(47.0)	(44.5)	(25.1)	(7.3)	(0.6)
Pre-tax margin	(43.7)	(43.4)	(24.4)	(6.6)	0.7
Adj. net margin	(25.2)	(33.2)	(18.3)	(1.6)	4.4
Effective tax rate	0.4	0.9	0.7	0.0	(15.0)
Returns (%)					
ROE	(11.1)	(21.0)	(16.5)	(1.8)	5.5
ROA	(8.5)	(15.6)	(11.3)	(1.2)	3.5
Per share					
EPS (RMB)	(1.3)	(2.0)	(1.3)	(0.1)	0.4
DPS (RMB)	0.0	0.0	0.0	0.0	0.0
BVPS (RMB)	23.0	18.7	15.2	14.6	15.2

Source: Company data, CMBIGM estimates

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