

PDD Holdings (PDD US)

Rapid overseas business expansion

We remain positive on PDD Holdings' (PDD) long-term growth prospect, mainly given: 1) domestic business could maintain healthy revenue and earnings growth in 2023, aided by the incorporation of more branded products and high ASP products, as well as the increase in monetization, aided by the increase in percentage of paid traffic volume; 2) Temu, the overseas e-commerce business operated under the "fully-entrusted" model, leveraging strong domestic supply chain and PDD's strong execution capability, has seen robust GMV and revenue growth, which is on track to support PDD's long-term revenue and earnings growth, and will likely propel a further valuation rerating, in our view. We lift our DCF-based TP by 21% to US\$131.8 (was US\$109.0), to factor in potentially stronger-than-expected domestic business monetization expansion, and better-than-expected development of Temu business. Maintain BUY.

- **Temu is seeing rapid business expansion.** According to Temu's official website, Temu had commenced operation in 47 countries around the globe as of October 2023. Leveraging strong domestic supply and PDD's strong execution capability, and being operated under the "fully-entrusted" business model, Temu can better manage product supply and quality, as well as provide better logistic and fulfilment services, thereby enhancing consumer experience. Temu's pace of overseas expansion and GMV growth has been faster than our previous expectation, and we think greater visibility on Temu's financials will propel further rerating. We forecast Temu to generate US\$16.9bn GMV and RMB25.4bn operating loss in 2023E.
- **Core domestic business sustained robust development although facing intensified competition.** PDD, in our view has more proactive room to drive GMV growth through targeting bigger consumer wallet share, and further increasing monetization rate aided by the increase in percentage of paid traffic volume. Although facing intensifying industry competition, PDD in our view, still enjoys relative higher traffic allocation efficiency compared to its peers, which enables the platform to provide better ROI for advertising merchants. We forecast PDD's online marketing services and others revenue to grow 42% YoY in 2023E to RMB146.4bn. Aided by the ramp-up of monetization for "Ten-billion subsidy" section, solid revenue growth of Duoduo Grocery, and incremental revenue generation from Temu, we forecast PDD's transaction services to grow 123% YoY in 2023E to RMB61.6bn.
- **Stable domestic business profit generation buffers overseas expansion.** PDD's strong profit generation capability in domestic business could aid further overseas expansion, in our view. We forecast PDD to post a 24.8% non-GAAP operating margin in 2023E (2022: 29.2%) due to incremental investment to support overseas business expansion, but to recover to 27.9% in 2024E, driven by operating efficiency improvement of overseas business.

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	93,950	130,558	208,026	265,939	325,104
YoY growth (%)	57.9	39.0	59.3	27.8	22.2
Net profit (RMB mn)	7,768.7	31,538.1	43,604.5	58,881.2	76,184.8
Adjusted net profit (RMB mn)	13,829.5	39,529.7	52,300.2	69,038.6	88,590.4
EPS (Adjusted) (RMB)	9.56	27.45	35.96	47.47	60.92
Consensus EPS (RMB)	9.56	27.45	33.88	42.24	54.32
P/E (x)	123.0	15.4	23.8	17.7	13.6
ROE (%)	11.5	32.7	30.0	28.4	26.7

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price US\$131.80
(Previous TP US\$109.00)
Up/Downside 20.7%
Current Price US\$109.23

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Stock Data

Mkt Cap (US\$ mn)	157,326.5
Avg 3 mths t/o (US\$ mn)	280.2
52w High/Low (US\$)	110.07/60.02
Total Issued Shares (mn)	1440.3

Source: FactSet

Shareholding Structure

Entities affiliated with Zheng Huang	27.9%
Entities affiliated with Tencent	15.5%

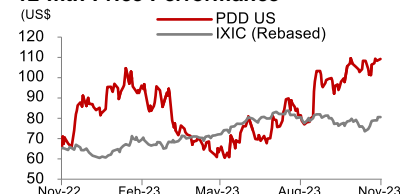
Source: Nasdaq

Share Performance

	Absolute	Relative
1-mth	3.0%	0.0%
3-mth	34.1%	34.0%
6-mth	72.5%	53.6%

Source: FactSet

12-month Price Performance



Source: FactSet

Changes in forecast and valuation

Figure 1: PDD: forecast revision

RMB bn	Current			Previous			Change (%)		
	2023E	2024E	2025E	2023E	2024E	2025E	2023E	2024E	2025E
Revenue	208.0	265.9	325.1	175.4	213.9	247.8	18.6%	24.3%	31.2%
Gross Profit	136.7	174.8	213.3	133.0	164.1	189.9	2.8%	6.5%	12.3%
Operating Profit	43.6	64.1	84.8	42.1	60.7	77.4	3.5%	5.5%	9.5%
Non-GAAP net profit	52.3	69.0	88.6	49.2	65.7	79.1	6.3%	5.1%	12.0%
Gross Margin	65.7%	65.7%	65.6%	75.8%	76.7%	76.6%	-10.1 ppt	-11.0 ppt	-11.0 ppt
Operating Margin	21.0%	24.1%	26.1%	24.0%	28.4%	31.2%	-3.0 ppt	-4.3 ppt	-5.1 ppt
Non-GAAP net margin	25.1%	26.0%	27.2%	28.1%	30.7%	31.9%	-3.0 ppt	-4.7 ppt	-4.7 ppt

Source: CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

RMB bn	Current			Consensus			Diff (%)		
	2023E	2024E	2025E	2023E	2024E	2025E	2023E	2024E	2025E
Revenue	208.0	265.9	325.1	204.9	264.1	326.5	1.5%	0.7%	-0.4%
Gross Profit	136.7	174.8	213.3	137.2	175.7	216.8	-0.3%	-0.5%	-1.6%
Operating Profit	43.6	64.1	84.8	43.8	62.7	85.1	-0.6%	2.2%	-0.3%
Non-GAAP net profit	52.3	69.0	88.6	52.9	68.5	88.8	-1.1%	0.8%	-0.2%
Gross Margin	65.7%	65.7%	65.6%	66.9%	66.5%	66.4%	-1.2 ppt	-0.8 ppt	-0.8 ppt
Operating Margin	21.0%	24.1%	26.1%	21.4%	23.7%	26.1%	-0.4 ppt	0.4 ppt	0.0 ppt
Non-GAAP net margin	25.1%	26.0%	27.2%	25.8%	25.9%	27.2%	-0.7 ppt	0.0 ppt	0.1 ppt

Source: Bloomberg, CMBIGM estimates

Our target price is US\$131.8, based on the DCF valuation methodology (WACC of 12.0% and terminal growth of 2.0%; both unchanged). Our target price translates into 25.0x 2023E PE and 19.0x 2024E PE (non-GAAP). Our previous DCF-based target price of US\$109.0 translates into 22.0x 2023E PE (non-GAAP).

Figure 3: PDD: DCF valuation (WACC of 12.0%; terminal growth of 2.0%; both unchanged)

(RMBbn)	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E
Total revenue	208,026	265,939	325,104	370,399	400,519	419,273	432,323	444,241
NPV of FCF	493,947	495,487						
Discounted terminal value	554,587	621,138						
Total PDD equity valuation	1,259,557	1,403,938						
No. of shares (diluted, mn)	1,454	1,454						
Valuation per share (US\$)	120.3	134.1						
Target valuation per share (US\$)	131.8							

Source: CMBIGM estimates

Note: 1) our DCF valuation is based on weighted average valuation of 2 months in 2023 and 10 months in 2024; 2) we fine-tuned exchange rate assumption from RMB:USD = 1:6.925 to RMB:USD = 1:7.2

Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Revenue	59,492	93,950	130,558	208,026	265,939	325,104
Cost of goods sold	(19,279)	(31,718)	(31,462)	(71,309)	(91,170)	(111,821)
Gross profit	40,213	62,232	99,095	136,716	174,769	213,283
Operating expenses	(49,594)	(55,335)	(68,693)	(93,124)	(110,710)	(128,514)
Selling expense	(41,195)	(44,802)	(54,344)	(78,634)	(92,281)	(106,309)
Admin expense	(1,507)	(1,541)	(3,965)	(4,235)	(4,787)	(5,852)
R&D expense	(6,892)	(8,993)	(10,385)	(10,256)	(13,643)	(16,353)
Others	0	0	0	0	0	0
Operating profit	(9,380)	6,897	30,402	43,592	64,058	84,770
Interest income	2,455	3,062	3,997	7,472	8,863	10,343
Interest expense	(757)	(1,231)	(52)	(24)	(24)	(24)
Foreign exchange gain/loss	225	72	(150)	140	140	140
Others	194	656	2,221	2,334	2,334	2,334
Pre-tax profit	(7,263)	9,455	36,419	53,513	75,371	97,562
Income tax	0	(1,934)	(4,726)	(10,025)	(16,605)	(21,493)
Others	84	247	(155)	116	116	116
After tax profit	(7,180)	7,769	31,538	43,604	58,881	76,185
Minority interest	0	0	0	0	0	0
Net profit	(7,180)	7,769	31,538	43,604	58,881	76,185
Adjusted net profit	(2,965)	13,830	39,530	52,300	69,039	88,590

BALANCE SHEET	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Current assets	149,524	160,909	216,618	279,915	357,485	458,262
Cash & equivalents	22,421	6,427	34,326	95,911	172,201	271,670
Restricted cash	52,422	59,617	57,974	57,974	57,974	57,974
Account receivables	730	674	588	936	1,197	1,463
Prepayment	5,160	3,425	2,298	3,662	4,682	5,723
Other current assets	68,791	90,767	121,431	121,431	121,431	121,431
Non-current assets	9,385	20,301	20,502	24,215	24,494	24,461
PP&E	203	2,203	1,045	2,115	2,694	2,961
Right-of-use assets	630	939	1,416	1,416	1,416	1,416
Intangibles	1,277	701	134	2,777	2,477	2,177
Other non-current assets	7,275	16,457	17,907	17,907	17,907	17,907
Total assets	158,909	181,210	237,120	304,130	381,980	482,723
Current liabilities	83,882	93,730	116,889	129,152	138,014	150,219
Short-term borrowings	1,866	0	13,886	13,886	13,886	13,886
Account payables	53,834	62,510	63,317	67,826	68,049	72,442
Other current liabilities	16,735	16,707	18,124	24,995	28,884	32,405
Lease liabilities	253	427	602	602	602	602
Accrued expenses	11,193	14,086	20,961	21,843	26,594	30,885
Non-current liabilities	14,851	12,365	2,460	2,460	2,460	2,460
Convertible bonds	14,433	11,789	1,576	1,576	1,576	1,576
Other non-current liabilities	418	577	884	884	884	884
Total liabilities	98,733	106,095	119,349	131,612	140,474	152,679
Share capital	0	0	0	0	0	0
Capital surplus	86,699	95,341	99,255	99,255	99,255	99,255
Retained earnings	(25,475)	(17,707)	15,193	69,941	138,928	227,466
Other reserves	(1,048)	(2,520)	3,322	3,322	3,322	3,322
Total shareholders equity	60,176	75,115	117,771	172,519	241,506	330,044
Total equity and liabilities	158,909	181,210	237,120	304,130	381,980	482,723

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	(7,263)	9,455	36,419	53,513	75,371	97,562
Depreciation & amortization	652	1,495	1,948	3,686	5,040	5,885
Tax paid	0	(1,934)	(4,726)	(10,025)	(16,605)	(21,493)
Change in working capital	31,050	13,562	9,886	10,550	7,582	10,897
Others	3,759	6,204	4,980	8,021	10,222	12,470
Net cash from operations	28,197	28,783	48,508	65,745	81,609	105,321
Investing						
Capital expenditure	(43)	(3,287)	(2,611)	(4,161)	(5,319)	(5,852)
Acquisition of subsidiaries/ investments	(93,160)	(130,268)	(28,596)	0	0	0
Net proceeds from disposal of short-term investments	55,083	97,547	0	0	0	0
Others	(238)	445	8,845	0	0	0
Net cash from investing	(38,358)	(35,562)	(22,362)	(4,161)	(5,319)	(5,852)
Financing						
Net borrowings	906	(1,875)	0	0	0	0
Proceeds from share issues	50,893	0	3,915	(0)	0	0
Share repurchases	0	0	0	0	0	0
Others	(0)	0	(3,905)	0	0	0
Net cash from financing	51,799	(1,875)	10	(0)	0	0
Net change in cash						
Cash at the beginning of the year	33,346	74,844	66,044	34,326	95,911	172,201
Exchange difference	(140)	(145)	100	0	0	0
Others	0	0	57,974	0	0	0
Cash at the end of the year	74,844	66,044	150,275	95,911	172,201	271,670
GROWTH	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Revenue	97.4%	57.9%	39.0%	59.3%	27.8%	22.2%
Gross profit	68.9%	54.8%	59.2%	38.0%	27.8%	22.0%
Operating profit	na	na	340.8%	43.4%	47.0%	32.3%
Net profit	na	na	306.0%	38.3%	35.0%	29.4%
Adj. net profit	na	na	185.8%	32.3%	32.0%	28.3%
PROFITABILITY	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Gross profit margin	67.6%	66.2%	75.9%	65.7%	65.7%	65.6%
Operating margin	(15.8%)	7.3%	23.3%	21.0%	24.1%	26.1%
Adj. net profit margin	(5.0%)	14.7%	30.3%	25.1%	26.0%	27.2%
Return on equity (ROE)	(16.9%)	11.5%	32.7%	30.0%	28.4%	26.7%
GEARING/LIQUIDITY/ACTIVITIES	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Current ratio (x)	1.8	1.7	1.9	2.2	2.6	3.1
Receivable turnover days	5.5	2.7	1.8	1.3	1.5	1.5
Payable turnover days	(792.9)	(669.4)	(729.9)	(335.6)	(272.0)	(229.3)
VALUATION	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
P/E	na	123.0	15.4	23.8	17.7	13.6
P/E (diluted)	na	79.7	14.0	22.2	16.8	13.1
P/B	10.2	12.7	4.1	6.0	4.3	3.1

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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