



Alibaba Group Holdings Limited (NYSE: BABA/SEHK: 9988)

The casualty of era... Downgrade to SELL

- BABA reported C3Q23 revenue, non-GAAP operating profit and GAAP net income in-line, 6% and (7%) vs. our est., and in-line, in-line and (14%);
- Instead of appointing capable management to oversee key subsidiaries, BABA backpedalled to call off its spin-off plans;
- We cut TP from US\$ 127 to US\$ 72, and downgrade to SELL.

The malaise today is an aftermath of overexpansion since IPO

Following BABA's IPO in 2014, with no competitors in sight, BABA embarked on an overexpansion that saw it to expand to (1) control of money flow (AntFin) and information flow (AliCloud) on top of merchandise flow (Taobao/Tmall), (2) buy up offline retailers, (3) buy up downstream (logistics), (4) buy up upstream (Youku/AutoNavi). The resulting conglomerate not only raises alert with CPC and runs afoul with trustbusters, but also piles up deteriorating assets.

Managing by committee won't work

Inviting founders back is a wrong move. Most co-founders (the 18 Arhats), like Roman Senators, are capable of defending Rome's tradition but not addressing its problems. BABA today is a rare Internet platform with diminishing interest from its spiritual leader. Jack Ma's sale of shares bodes ill for its participation of BABA's future reforms, at a time when we notice a general dearth of capable management across the board, which is not surprising given BABA's excessive footprint but is a problem if demonstrated talent is not promoted.

TikTok/ByteDance threatens BABA more than Tencent

Monetizing traffic has been the corner stone of the TikTok/ByteDance platform while creating traffic is not, which makes it more threatening to BABA.

What can turn us positive?

First, Taobao/Tmall need capable management to defend against TikTok/ByteDance, PDD and JD. Further, BABA needs to resolve with government on businesses which (1) pose security uncertainties, (2) invite antitrust actions. Lastly, BABA, separate or as a whole, must be managed by people with high aspiration for success and corresponding incentives. (TBC)

Summary financial data

Highlights	FY2022A	FY2023A	FY2024E	FY2025E	FY2026E
Revenues (US\$ mn)	853.1	868.8	950.2	999.3	1,094.1
Non-GAAP operating profit (US\$)	130.4	147.5	166.7	170.8	171.8
Non-GAAP EPADS (US\$)	52.7	54.3	70.9	78.3	78.2
GAAP EPADS (US\$)	20.1	27.5	47.9	51.1	47.6
Adjusted EBITA margin	15.3%	15.0%	13.7%	13.0%	11.9%
P/E (non-GAAP)	10.9	10.6	8.1	7.3	7.3
Free cash flow yield (%)	4.1%	6.8%	8.5%	8.6%	9.5%

Source: Alibaba Group Holdings Limited, Bloomberg, Blue Lotus (as of November 17, 2023); Note: P/E based on last close and USD/RMB = 7.25.

See the last page of the report for important disclosures.

Blue Lotus Capital Advisors Limited

BUY
UR
SELL

Target Price: US\$ 72	Current Price: US\$ 79.11
RIC: (NYSE: BABA/SEHK: 9988)	BBG: (BABA US/9988 HK)
Market cap (US\$ mn)	201,210.3
Average daily volume (US\$ mn)	1,815.0
Shares out/float (m)	2,543.4/NA

Source: Bloomberg, Blue Lotus (as of November 17, 2023)

Key Changes

	New	Old	Diff
BLRI Recommendation	SELL	BUY	
BLRI Target Price (US\$)	72	127	(43.3%)
FY2024E EPADS (US\$)	9.8	10.4	(6.2%)
FY2025E EPADS (US\$)	10.8	12.0	(9.7%)
FY2026E EPADS (US\$)	10.8	12.4	(12.9%)

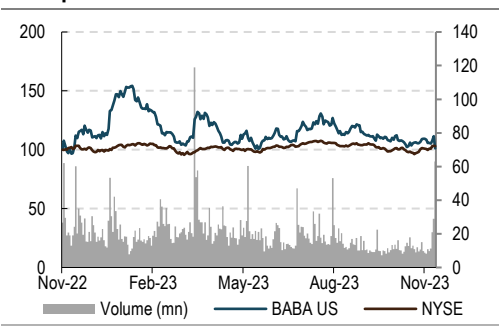
Source: Blue Lotus (as of November 17, 2023); Note: Prior EPS estimates rebased for FX rate of USD/RMB = 7.25.

BLRI vs. The Street

No. of Bloomberg Recommendations	41
Target price vs. Bloomberg mean	(44.4%)
1-year-fwd EPS vs. Bloomberg mean	(2.8%)
Bloomberg recommendation	4.78

Source: Bloomberg Recommendation, Blue Lotus (1=SELL,5=BUY) (as of November 17, 2023)

Price performance and volume data



Source: Bloomberg, Blue Lotus (as of November 17, 2023)

Research team



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Alibaba Group Holdings Limited: Financial Summary

Fiscal year ends-31-Mar

Exhibit 1. Income statement

(RMB bn)	FY2023A	FY2024E	FY2025E
China retail marketplace GMV	7,417	7,363	7,264
Net revenues	868.8	950.2	999.3
Cost of revenues	(549.7)	(597.0)	(633.7)
Gross profit	319.1	353.2	365.6
Operating expenses, GAAP	(218.6)	(219.6)	(237.2)
R&D cost	(56.7)	(52.2)	(57.0)
Sales marketing cost	(103.5)	(114.3)	(122.6)
General administrative	(42.2)	(41.0)	(47.2)
Operating profit, GAAP	100.4	133.7	128.4
Share based compensation	30.8	20.9	32.0
Operating profit, non-GAAP	147.5	166.7	170.8
Interest income and investment income, net	(17.0)	1.9	12.6
Pre-tax profit, GAAP	89.3	141.7	147.2
Income tax	(15.5)	(24.6)	(28.0)
Net income, GAAP	65.6	117.1	119.3
Net income, non-GAAP	143.4	180.4	190.3
Number of ADS, diluted	2.6	2.5	2.4
EPADS, GAAP, diluted (RMB)	27.5	47.9	51.1
EPADS, non-GAAP, diluted (RMB)	54.3	70.9	78.3
Gross margin	36.7%	37.2%	36.6%
Operating margin, non-GAAP	17.0%	17.5%	17.1%
Net margin, GAAP	7.6%	12.3%	11.9%
Net margin, non-GAAP	16.5%	19.0%	19.0%

Source: Alibaba Group Holdings Limited, Blue Lotus (as of November 17, 2023)

Exhibit 2. Balance sheet

(RMB bn)	FY2023A	FY2024E	FY2025E
Cash and restricted cash	229.5	271.4	285.0
Short-term invest. And inv in sec.	331.4	391.1	474.9
Prepayments and others	137.1	137.1	137.1
Total current asset	698.0	799.5	896.9
Property and equipment	176.0	195.9	208.5
Investment in securities, non-current	453.1	488.6	523.0
Intangibles, goodwill and others	315.0	364.3	366.7
Prepayments, non-current	110.9	162.5	178.3
Total assets	1,753.0	2,010.8	2,173.3
Bank borrowings	7.5	7.5	7.5
Income tax payable	12.5	29.9	32.2
Accrued expense	276.0	310.6	330.3
Deferred revenue	71.3	92.9	101.9
Merchant deposits	13.3	29.4	34.7
Total current liabilities	380.6	470.3	506.5
Long term debt	52.0	38.3	38.3
Deferred tax liabilities	95.7	133.1	142.6
Total non-current liabilities	147.7	171.4	181.0
Additional paid in capital	416.9	416.9	416.9
Retained earnings	599.0	720.0	856.7
Total equity	989.7	1,110.6	1,247.3
Total liabilities and equity	1,753.0	2,010.8	2,173.3

Source: Alibaba Group Holdings Limited, Blue Lotus (as of November 17, 2023)

Company Description

Since 2013, Alibaba Group has become the largest online mobile e-business company by GMV in the world. Alibaba operates several subsidiaries. The GMV of Taobao and Tmall accounts for ~49% of China's market share in 2022. AliCloud Computing, the largest public cloud computing company in China, occupied 34% of China's market share in 2022, and owns one-third of Ant Finance, including Alipay, which is the largest online payment platform in the world occupying over 50% of China's market share in 2022.

Industry View

We estimate China's e-commerce market to grow by 11%~ in 2023, after growing 7%~ in 2022. Between 2022 and 2024, we estimate the total online ecommerce market to grow at CAGR of 13%, and traditional e-commerce and social e-commerce sub-sectors to grow at CAGR of 9% and 36%, respectively.

Exhibit 3. Cash flow statement

(RMB bn)	FY2023A	FY2024E	FY2025E
Net income	65.6	117.1	119.3
Adjusted for	-	-	-
Depreciation & amortization	49.7	61.1	69.1
Share based compensation	30.8	20.9	32.0
Amortization of intangible assets	18.4	20.6	17.9
Changes in	-	-	-
Prepayments and others	(32.9)	(38.3)	(33.8)
Income tax payables	3.3	2.7	2.3
Merchant deposits	5.0	5.1	5.3
Accrued liabilities and deferred rev.	37.3	27.3	28.7
Cash from operations	176.9	217.2	241.3
Capex, PPE	(53.3)	(66.5)	(74.0)
Purchase of intangibles	(8.8)	17.2	14.7
Cash paid for equity investment	(40.0)	(48.0)	(57.6)
Acquisitions of AFS and HTM investment securities	(22.1)	8.5	-
Other cash paid in investing	(4.1)	(78.1)	(110.9)
Cash from Investing activities	(128.4)	(166.9)	(227.8)
Cash from financing activities	(59.9)	0.1	0.1
Change in cash	(6.3)	50.4	13.6
Cash at beginning	227.4	229.5	271.4
Cash at end	229.5	271.4	285.0

Source: Alibaba Group Holdings Limited, Blue Lotus (as of November 17, 2023)

See the last page of the report for important disclosures.

Taobao and Cloud are vulnerable

- **BABA was by far the weakest ecommerce platform by GMV:** Taobao/Tmall's GMV recorded a "modest decline" in GMV during CY3Q23 compared to our estimate and consensus of low-single digit GMV increase. It significantly underperformed peers, such as JD (JD US, BUY, TP US\$ 34) which grew low single-digit, Vipshop (VIPS US, BUY, TP US\$16) which 13%, Kuaishou (1024 HK, BUY, HK\$ 62) which we estimate grew 30-35%, Douyin (Private) which we estimate grew 60%~, and PDD (PDD US, BUY, TP US\$ 128) which we estimate grew 25-30%. Despite negative GMV, growth BABA's sales and marketing spending grew 14% yoy, beating our estimate by 10%, and significantly outpacing the 3% growth to Taobao/Tmall CMR, which we believe is indicative of the ineffectiveness of its current strategy.
- **Cloud computing begins to shed customers:** BABA's cloud business continues to shed private cloud customers, and we believe management commentary seems to indicate that customer shedding could accelerate in coming quarters. Thus, we currently expect cloud revenues growth to turn negative in the following quarters. A spate of severe service disruptions, such as a recent server shutdown that hampered cloud services for several hours, is likely accelerating customer loss. Meanwhile, the company said it was unprepared for the recent restrictions on AI chip exports.
- **Reduced expectations for Taobao/Tmall and Cloud computing:** Our main model changes are (1) decreased Taobao/Tmall GMV FY2024-2027 CAGR to (2%) from prior +2.5%, as Taobao/Tmall is increasingly uncompetitive against PDD/Douyin, in our view, (2) decreased Cloud computing revenue FY2024-2027 CAGR to +4% from prior +12%, as the recent service disruptions could expediate customer loss, and the company's lack of preparedness for the AI chip restrictions suggest that customers could migrate to Cloud providers with better resources, and (3) increased operating expense estimates, as we expect BABA will continue to spend ineffectively to achieve growth.

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Exhibit 4. Alibaba Holdings FY2Q24/CY3Q23 Earnings Review Table

(RMB mn)	F2Q24A	F2Q24E	F2Q24C	%Diff vs Est.	%Diff vs Cons.	F1Q24A	QoQ	F2Q23A	YoY	F3Q24E New	F3Q24E Old	F3Q24C
Total revenue	224,790	221,732	227,104	1.4%	(1.0%)	250,735	(10.3%)	221,662	1.4%	266,503	267,931	272,580
-China Commerce	97,654	98,143		(0.5%)		114,953	(15.0%)	93,735	4.2%	129,469	133,852	
-International Commerce	24,511	21,158		15.8%		22,123	10.8%	16,046	52.8%	26,697	24,260	
-Local Services Group	15,564	16,061		(3.1%)		14,450	7.7%	13,381	16.3%	16,334	16,174	
-Cainiao Smart Logistics	22,823	22,121		3.2%		23,164	(1.5%)	18,282	24.8%	28,912	28,549	
-Cloud Intelligence	27,648	27,498		0.5%		25,123	10.1%	27,035	2.3%	26,525	27,602	
-Digital Media	5,779	6,012		(3.9%)		5,381	7.4%	5,228	10.5%	5,326	5,113	
-All others	48,052	47,475		1.2%		45,541	5.5%	47,955	0.2%	51,624	50,621	
-Consolidation adj.	(17,241)	(16,736)		3.0%		(16,579)	4.0%	(14,410)	19.6%	(18,382)	(18,241)	
Cost of revenue	(139,664)	(139,872)	(141,145)	(0.1%)	(1.0%)	(142,347)	(1.9%)	(131,210)	6.4%	(164,788)	(166,987)	
Gross profit	85,126	81,860	85,959	4.0%	(1.0%)	108,388	(21.5%)	90,452	(5.9%)	101,715	100,944	109,250
Gross margin	37.9%	36.9%	37.9%	1.0ppt	0.0ppt	43.2%	(5.4ppt)	40.8%	(2.9ppt)	38.2%	37.7%	40.1%
-R&D	(14,218)	(13,716)		3.7%		(10,465)	35.9%	(15,150)	(6.2%)	(13,192)	(13,036)	
-S&M	(25,485)	(23,190)		9.9%		(27,047)	(5.8%)	(22,359)	14.0%	(34,177)	(32,185)	
-G&A	(9,408)	(12,057)		(22.0%)		(7,297)	28.9%	(10,591)	(11.2%)	(11,086)	(12,010)	
Other items	(2,431)	(2,600)		(6.5%)		(4,510)	(46.1%)	(2,729)	(10.9%)	(2,600)	(2,600)	
Intangibles amortization	(2,431)	(2,600)		(6.5%)		(2,479)	(1.9%)	(2,729)	(10.9%)	(2,600)	(2,600)	
OPEX, GAAP	(51,542)	(51,563)		(0.0%)		(49,319)	4.5%	(50,829)	1.4%	(61,055)	(59,831)	
OPEX, non-GAAP	(42,281)	(41,424)		2.1%		(48,469)	(12.8%)	(40,313)	4.9%	(49,927)	(48,121)	
SBC	(6,830)	(7,539)		(9.4%)		1,629	NM	(7,787)	(12.3%)	(8,528)	(9,110)	
GAAP op. income	33,584	30,297	33,030	10.8%	1.7%	42,490	(21.0%)	25,213	33.2%	40,661	41,113	45,863
GAAP op. margin	14.9%	13.7%	14.5%	1.3ppt	0.4ppt	16.9%	(2.0ppt)	11.4%	3.6ppt	15.3%	15.3%	16.8%
Non-GAAP op. income	42,845	40,436	41,902	6.0%	2.3%	45,371	(5.6%)	35,729	19.9%	51,789	52,823	
Non-GAAP op. margin	19.1%	18.2%	18.5%	0.8ppt	0.6ppt	18.1%	1.0ppt	16.1%	2.9ppt	19.4%	19.7%	
Interest income	5,136	5,000		2.7%		(5,898)	NM	(42,452)	NM	5,000	5,000	
Interest expense	(1,854)	(1,784)		3.9%		(1,784)	3.9%	(1,388)	33.6%	(1,854)	(1,784)	
Other income, net	1,391	1,944		(28.5%)		1,364	2.0%	2,944	(52.8%)	1,910	1,979	
Pretax inc., GAAP	38,257	35,457	35,601	7.9%	7.5%	36,172	5.8%	(15,683)	NM	45,717	46,308	49,209
Tax expense	(5,797)	(6,737)		(14.0%)		(6,022)	(3.7%)	(2,572)	125.4%	(8,686)	(8,799)	
Share res. of equity inv.	(5,764)	-		NM		2,850	NM	(4,136)	39%	-	-	
GAAP net income	26,696	28,721	31,311	(7.0%)	(14.7%)	33,000	(19.1%)	(22,391)	NM	37,031	37,510	43,337
Net margin, GAAP	11.9%	13.0%	13.8%	(1.1ppt)	(1.9ppt)	13.2%	(1.3ppt)	(10.1%)	22.0ppt	13.9%	14.0%	15.9%
Non-GAAP net income	40,188	42,895	40,215	(6.3%)	(0.1%)	44,922	(10.5%)	33,385	20.4%	54,043	52,713	53,409
Net margin, non-GAAP	17.9%	19.3%	17.7%	(1.5ppt)	0.2ppt	17.9%	(0.0ppt)	15.1%	2.8ppt	20.3%	19.7%	19.6%

Source: Alibaba Holdings, Blue Lotus (as of November 17, 2023)

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