

# China Youzan (8083 HK)

## 21Q1 result missed expectation, while the structure mix of new paying merchants optimized

Hong Kong | TMT sector | Company Update

### Investment Summary

#### The company's 1Q21 result missed market expectation

The company announced its 1Q21 result on May 10, and the result missed market expectations. The 21Q1 GMV was RMB 23.6 billion (+13.5% YoY), which was lower than market expectations. The GMV growth in the past few quarters have maintained at a high level (the average YoY growth rate of GMV in the past four quarters is roughly 75.9% YoY). Therefore, compared with the past data, the deceleration of the 21Q1 GMV growth was relatively obvious. The slowdown in GMV growth was mainly due to the drop in GMV from Kuaishou. The GMV from Kuaishou fell by 43.4% YoY to RMB 4.7 billion. We expect the GMV growth will resume rapid growth in 21H2. The company's management maintains their previous target YoY GMV growth rate of 50% in 2021 and expects that the GMV contribution from Kuaishou will drop to 10% by the end of 2021 (Kuaishou GMV accounted for 40% of total GMV in 2020).

In terms of revenue, the company's 21Q1 revenue was RMB 417 million (+11.9% YoY), which was also below market's expectation. In terms of breakdown, the subscription solution revenue was RMB 257 million (+20.7% YoY) and the merchant solution revenue was RMB 157 million (-0.2% YoY). Excluding the transaction fee revenue, the revenue from merchant solutions increased by over 20% YoY. The revenue from other business was RMB 3.55 million (+12.4% YoY).

In terms of GP, the 21Q1 GP was RMB 245 million (+15.7% YoY), with GPM at 58.7% (1.9ppts YoY). The GP from subscription solution was RMB 190 million (+21.1% YoY), with respective GPM at 73.8% (+0.2ppts YoY). The GP from merchant solution was RMB 55 million (+0.9% YoY), with respective GPM at 35.1% (+0.4ppts YoY).

In terms of the expenses, the company's S&M expense in 21Q1 was RMB 209 million (+29.9% YoY), with respective expense ratio at 50.3% (+7.0ppts YoY). The increase in both S&M expense and expense ratio was mainly due to the fact that the company has expanded its direct sales team and established operation service centers in both Wuhan and Nanjing in 21Q1. The newly hired sales team tend to have lower revenue conversion efficiency. The admin expense in 21Q1 was RMB 71 million (+56.4% YoY), with respective expense ratio at 16.9% (+4.8ppts YoY). The rise in both admin expense and expense ratio was because the 21Q1 admin expense has included one-off expenses such as the related expenses of the take private and main board listing proposal. The 21Q1 other operating expense was RMB 137 million (+34.7% YoY), with respective expense ratio at 32.7% (+5.5ppts YoY). The increase in both the expense and expense ratio was due the fact that the company has increased investment in R&D for Youzan PaaS platform and other new products.

In terms of profit, the company's 21Q1 net loss attributable to the parent was approximately RMB 91 million. The net loss was further increased by 21.7% YoY. The NPM was -21.8% (-1.8 ppts YoY).

3 June 2021

### Buy (Maintain)

CMP HKD 1.71

(Closing price as of 1 June)

TARGET HKD 3.04 (+78%)

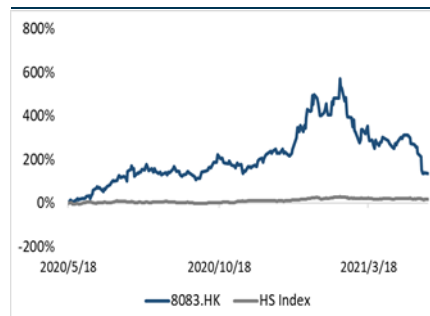
#### COMPANY DATA

O/S SHARES (MN) :	17,260
MARKET CAP (HKD MN) :	29,515
52 - WK HI/LO (HKD):	4.52/0.69

#### SHARE HOLDING PATTERN, %

Whitecrow Investment Ltd	8.35%
Poyang Lake Investment Limited	6.01%
Ward Ferry Management (BVI) Limited	6.91%

#### PRICE VS. HSI



Source: Wind, Phillip Securities

#### KEY FINANCIALS

CNY mn	FY20	FY21E	FY22E	FY23E
Net Sales	1821	2678	3993	5640
Net income	-295	-276	-205	-1
EPS	-0.018	-0.016	-0.012	-0.000
P/E, x	N/A	N/A	N/A	N/A
ROE, Adj (%)	-6.4	-6.7	-5.4	0.1
ROA, Adj (%)	-2.4	-2.3	-1.6	0.0

Market closing price as of 1 June

Source: Company Data, Phillip Securities Est.

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### The structure mix of new paying merchants optimized

The number of new paying merchants in 21Q1 was 7,961 (-43.1% YoY). The main reason for the YoY decline in the number of new paying merchants was that there were many small merchants set up online stores through company's SaaS products in 20Q1, due to the pandemic and hence the corresponding base in 21Q1 was high. Further, Q1 is typically the sales offseason. Although the number of new merchants in 21Q1 dropped sharply YoY, the structure mix of new merchants has been significantly optimized. Among the new paying merchants, the proportion of merchants subscribing to the high end products was close to 50%. The optimization of the merchant structure mix will affect positively to the future key operating indicators such as renewal rate, ACV, ARPU, LTV etc. The number of paying merchants as of the end of 1Q21 was 95,692, which reflects a decrease of 1.5% comparing to the 97,158 at the end of 20Q4. The decrease in the number of the paying merchants was mainly due to the loss in Kuaishou and other small merchants during the period. On the other hand, the company's 21Q1 ACV reached RMB 13,060 (+9.9% QoQ).

The company's offline commerce SaaS business has been developing well. The number of paying merchants from Youzan Retail, Youzan Chain, Youzan Beauty and Youzan Education have all increased QoQ. The number of paying merchants from Youzan Chain, Youzan Beauty and Youzan Education increased by over 100% YoY respectively.

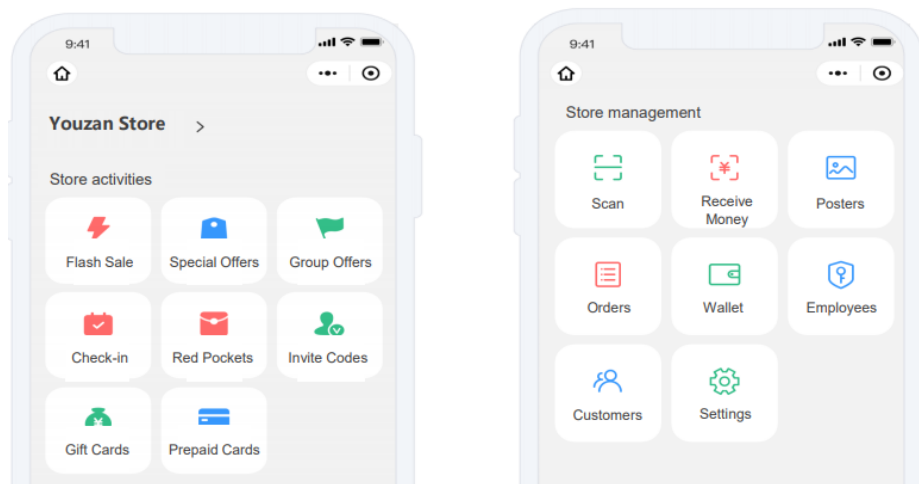
### The launch of new products enriches the company's product matrix

The company has recently launched a few new products, including Youzan WeCom Assistant and WowShop.

1) Youzan WeCom Assistant is an individually selling product, that empowers merchants in customer acquisition, activation and operation. Merchants can accumulate customer assets in WeCom and drive the activity and conversion rate of its customers. Youzan WeCom Assistant is usable with Youzan WeiMall, Youzan Retail, Youzan Chain, Youzan Beauty and Youzan Education. WeCom Assistant is currently the only office tool that is linked with Wechat, and can solve many of the shortcomings of operating a business through personal WeChat accounts. At present, the product is divided into basic version (charging RMB 3,800/year) and professional version (charging RMB 6,800 year).

2) Wowshop is an all-in-one marketing and store management toolkit focusing on physical stores in lower-tier cities. It mainly provides store activities function (including flash sales and special offers to attract customers to physical stores offline) and store management services (including order and employee's management). The user interface of Wowshop is relatively simple, which greatly reduces the threshold for merchants in low-tier cities to use digital marketing tools. Since the product is positioned to serve merchants in the lower-tier cities, hence the subscription fee is relatively low, with an annual subscription fee of RMB 1,888/year.

Figure 1: the user interface of Wowshop



Source: company, PSHK

### Valuation and Investment Thesis

The company's 1Q21 result missed expectation, but we expect it to gradually picking up strong growth momentum in 2Q21 and 2H21. Considered that the number of the paying merchants in 21Q1 was lower than we expected, we trim the company's 2021/2022/2023 revenue forecast to RMB 2.68/3.99/5.64 billion from RMB 2.81/4.15/5.86 billion. We lower the SaaS and extended services target P/S to 25x and the transaction and other business P/S to 5x, in order to reflect the current market's more cautious view on high valuation companies. We cut our TP to HKD 3.04 (-23%). We maintain BUY rating. (Market closing price as of 1st June) (exchange rate: RMB 0.85/HKD)

### Risk

1) The delay in Youzan Technology listing and take private of China Youzan 2) The expansion of SaaS customers is worse than expected 3) The increased industry competition 4) GMV increase less than expected 5) Merchants renewal rate less than expected

## Financial Statements

### Consolidated Statement of Profit or Loss

Dec Y/E, RMB mn	FY19	FY20	FY21E	FY22E	FY23E
Revenue	1169	1821	2678	3993	5640
Gross Profit	593	1082	1596	2440	3513
S&M expense	-543	-782	-1071	-1517	-2087
Admin expense	-197	-241	-348	-479	-564
Amortisation of IA	-193	-193	-186	-162	-141
Other expense	-486	-507	-571	-661	-739
Other operating gain/(loss)	-179	43	0	0	0
Operating Profit	-1006	-599	-579	-380	-17
Net finance income	-12	8	5	5	15
Other non-operating gain/(loss)	5	-1	0	0	0
Profit before tax	-1012	-592	-574	-375	-2
Tax	97	47	47	29	0
NCI	324	251	252	140	1
Profit for the year	-592	-295	-276	-205	-1
EPS (RMB)	-0.040	-0.018	-0.016	-0.012	0.000

### Key Financial Data

Dec Y/E	FY19	FY20	FY21E	FY22E	FY23E
Valuation Ratio					
P/E ratio, x	N/A	N/A	N/A	N/A	N/A

### Per share data (RMB)

EPS	-0.040	-0.018	-0.016	-0.012	0.000
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### Growth & Margin

Revenue Growth	99.4%	55.8%	47.1%	49.1%	41.2%
Operating income growth	N/A	N/A	N/A	N/A	N/A
Net income Growth	N/A	N/A	N/A	N/A	N/A
Gross Profit Margin	50.8%	59.4%	59.6%	61.1%	62.3%
Operating profit Margin	-86.1%	-32.9%	-21.6%	-9.5%	-0.3%
Net Profit Margin	-50.6%	-16.2%	-10.3%	-5.1%	0.0%

### Key Ratios

ROE	-15.2%	-6.4%	-6.7%	-5.5%	0.0%
ROA	-5.6%	-2.4%	-2.3%	-1.7%	0.0%

Source: Company, PSHK Estimate

Market closing price as of 1 June

### Consolidated Statement of Financial Position

Dec Y/E, RMB mn	FY19	FY20	FY21E	FY22E	FY23E
<b>Non Current Asset</b>					
PPE	61	65	91	129	181
ROU assets	205	241	261	283	307
Intangible assets	1632	1440	1254	1092	951
Capitalised contract costs	10	24	36	50	68
Others	2253	2335	2335	2335	2335
<b>Total Non Current Assets</b>	<b>4161</b>	<b>4105</b>	<b>3978</b>	<b>3889</b>	<b>3843</b>
<b>Current Asset</b>					
Capitalised contract costs	119	171	201	326	399
Inventories	2	1	1	1	1
Prepayments	924	806	927	1066	1226
Cash and cash equivalents	746	1727	1590	1595	2087
Others	4547	5402	5402	5402	5402
<b>Total Current Assets</b>	<b>6337</b>	<b>8108</b>	<b>8123</b>	<b>8391</b>	<b>9116</b>
<b>Total Assets</b>	<b>10499</b>	<b>12212</b>	<b>12101</b>	<b>12280</b>	<b>12959</b>
<b>Non Current Liabilities</b>					
Contract liabilities	48	56	101	149	211
Lease liabilities	184	223	244	265	289
Others	261	244	244	244	244
<b>Total Non Current Liabilities</b>	<b>493</b>	<b>524</b>	<b>589</b>	<b>658</b>	<b>744</b>
<b>Current Liabilities</b>					
Trade payables	4	4	11	11	20
Settlement obligations	5070	5802	5802	5802	5802
Contract liabilities	407	611	955	1410	1997
Others	627	641	641	641	641
<b>Total Current Liabilities</b>	<b>6107</b>	<b>7059</b>	<b>7410</b>	<b>7865</b>	<b>8460</b>
<b>Equity</b>					
Share capital	129	145	145	145	145
Reserve	3530	3714	3438	3233	3232
Non controlling interest	241	771	519	379	378
<b>Total Equity</b>	<b>3899</b>	<b>4630</b>	<b>4102</b>	<b>3757</b>	<b>3756</b>
<b>Total Liabilities and Equity</b>	<b>10499</b>	<b>12212</b>	<b>12101</b>	<b>12280</b>	<b>12959</b>

### Cashflow Statement

Dec Y/E, RMB mn	FY19	FY20	FY21E	FY22E	FY23E
<b>Profit (loss) before tax</b>	<b>-1,012</b>	<b>-592</b>	<b>-574</b>	<b>-375</b>	<b>-2</b>
Depreciation and amortization	419	473	261	252	249
change in working capital	-354	214	232	226	405
Others	331	50	42	24	-15
<b>CFO</b>	<b>-616</b>	<b>144</b>	<b>-39</b>	<b>127</b>	<b>637</b>
Capex	-43	-24	-53	-74	-105
Others	-9	-50	3	4	6
<b>CFI</b>	<b>-52</b>	<b>-74</b>	<b>-50</b>	<b>-70</b>	<b>-99</b>
<b>CFF</b>	<b>954</b>	<b>1,031</b>	<b>-48</b>	<b>-52</b>	<b>-46</b>
<b>Net Change in Cash</b>	<b>285</b>	<b>1,101</b>	<b>-137</b>	<b>5</b>	<b>492</b>
Foreign exchange	31	-96	0	0	0
cash equivalents for sales	0	0	0	0	0
<b>Cash at year end</b>	<b>746</b>	<b>1,752</b>	<b>1,590</b>	<b>1,595</b>	<b>2,087</b>

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Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within $\pm 5\%$ from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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