Algory Capital

Alibaba (NYSE: BABA)

Fundamental Investments – Generalist Group

Current price (2/27/24): $74.62 | Target Price: $88.00 | Implied Upside: 17.92%

Alibaba.com

February 2024

Agenda

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Company Overview

Ecommerce, AIDC (AliExpress) international ecommerce, and cloud computing.

Business Description & Strategy

Overview: Alibaba is a multinational technology and ecommerce conglomerate that has multiple segments under ecommerce, logistics, and cloud computing. There are six main groups under Alibaba: Taobao and Tmall Group (TTG), Alibaba International Digital Commerce (AIDC) Group, Local Services Group, Cainao Smart Logistics Network Limited, Cloud Intelligence Group, and Digital Media and Entertainment Group. Alibaba makes most of its revenue through its Taobao and Tmall group, accounting for almost 50% of total revenue.

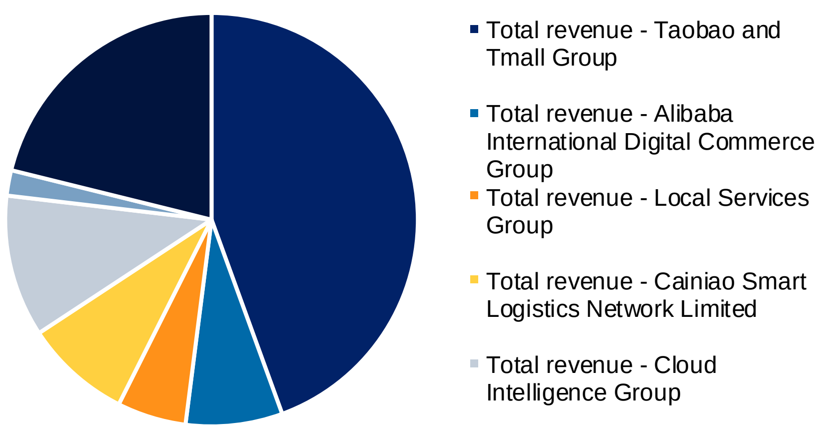
Strategy: Alibaba is focused on **1) Product Supply** through increasing product selection on TTG platforms and through the new AE *Choice* model for the AIDC Group. AE *Choice* model connects the marketplace platform model with an efficient supply chain; propels user and transaction growth. **2) Competitive pricing** in the TTG through increasing investment in product sourcing and optimizing connecting merchants to the platform. Offering quality products at attractive prices, resulting in increased purchase frequency as well. **3) Prioritizing public cloud** by continuing to reduce revenue from project-based contracts and increasing focus on public cloud products. Improving customer coverage and service to increase growth rate.

Valuation: DCF and comparable company analysis show Alibaba is trading at a discounted valuation with significant operational and financial turnaround opportunities driving a target share price of $88.00.

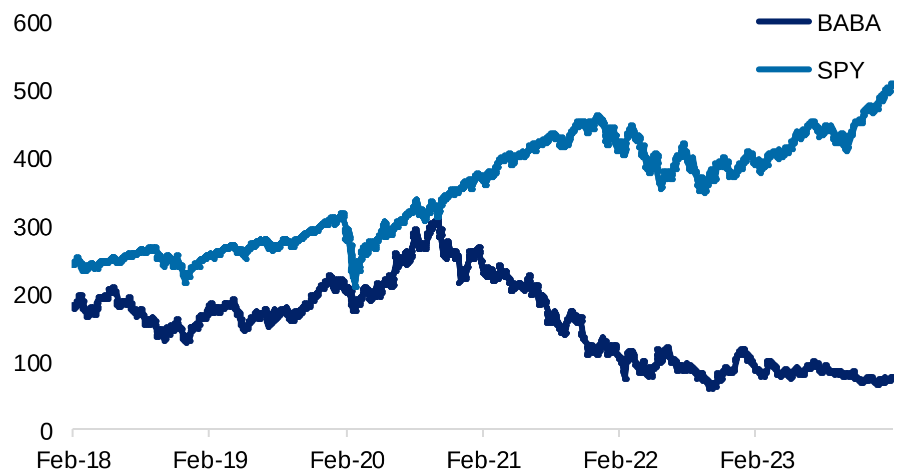
Current Market Data (Feb 27)

Mkt Cap (billion)	$197.57	**EV (billion)**	$126.50
Price	$ 77.68	**FY23 Revenue**	$868,687,000
52 Week High	$105.05	**FY23 EBITDA Margin**	13.4%
52 Week Low	$66.63	**FY23 Debt (M)**	$176,597,000
Div. Yield % (LTM)	1.31%	**EV/EBITDA (LTM)**	0.90x
Float %	82.3%	**P/E (LTM)**	14.28x

Alibaba Segment Revenue Breakdown

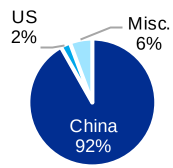
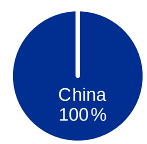
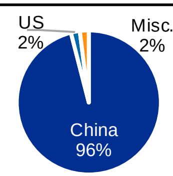
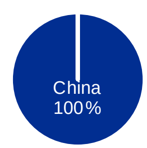
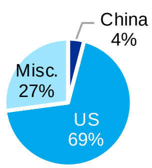


Historic Share Price vs. Benchmark



Competitive Landscape

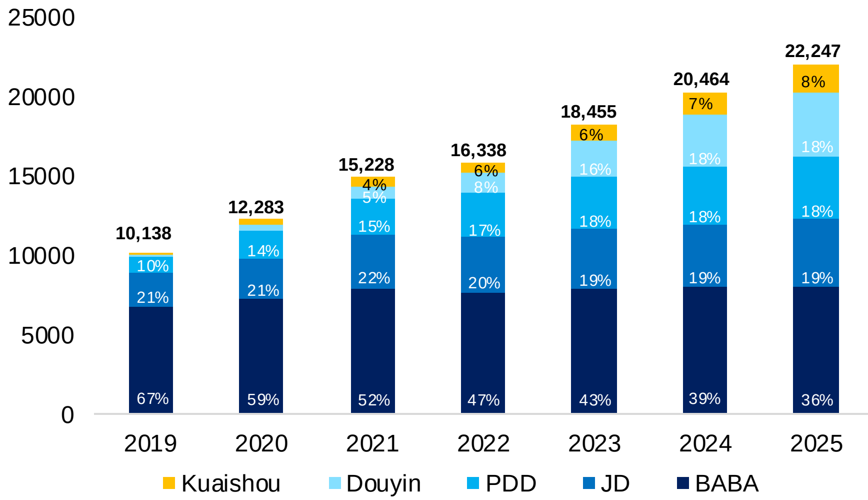
Alibaba is a leading e-commerce platform with Taobao and Tmall making up 50% of revenue

Company	Key Products	Revenue Breakdown by Product Segment	Revenue by Region	Cloud and Logistics Revenue / Total Rev	Ecommerce Revenue / Total Rev	Global Ecommerce Market Share (%)	Ad Expenses as a % of SG&A
Alibaba.com	• Taobao/Tmall • AIDC • Local Services • Cainiao • Cloud • Digital Media	• **TTG: 44%** • AIDC: 8% • Local: 5% • Cainiao: 8% • Cloud: 11% • DMEG: 2%		• 19.44% of total revenue • 11.11% cloud • 8.34% logistics	• Ecommerce makes up **50.02%** of total revenue	• **23%** global market share	• **71.04%** of SG&A is from Sales and Marketing
JD.COM	• Online Retail • JD Logistics • JD Retail Cloud • JD Health • JD Property	• **Retail: 83%** • Logistics: 14.62% • Dada: 1.01% • New: 1.42%		• 14.62% of total revenue is from JD Logistics	• Ecommerce makes up **82.95%** of total revenue	• **9%** global market share	• **77.02%** of SG&A is from Sales and Marketing
Pinduoduo	• Transaction services • Merchandise sales • Online marketing	• **Marketing: 78.7%** • Transaction: 21.2% • Sales: 0.1%		• Does not make revenue from cloud or logistics	• Ecommerce makes up **99.84%** of total revenue	• **8%** global market share	• **93.20%** of SG&A is from Sales and Marketing
美团 美团点评 Meituan Dianping	• Core local commerce • Food delivery • Hotel & In store • New initiatives	• **Delivery: 33%** • Commission: 24.84% • Market: 13% • Other: 29.36%		• No longer makes revenue from cloud service as of 2020	• Ecommerce makes up **56.92%** of total revenue	• **0.5%** global market share	• **80.27%** of SG&A is from Sales and Marketing
amazon	• Ecommerce • Amazon Web Services (AWS) • Amazon Prime • Digital Ads	• **Online: 42.8%** • Physical: 4% • Third-party: 22.9% • Subs: 6.85% • Advertising: 7.34% • AWS: 15.58%		• 15.58% of total revenue is made up by Amazon Web Services	• Ecommerce makes up **40.45%** of total revenue	• **12%** global market share	• **78.97%** of SG&A is from Sales and Marketing

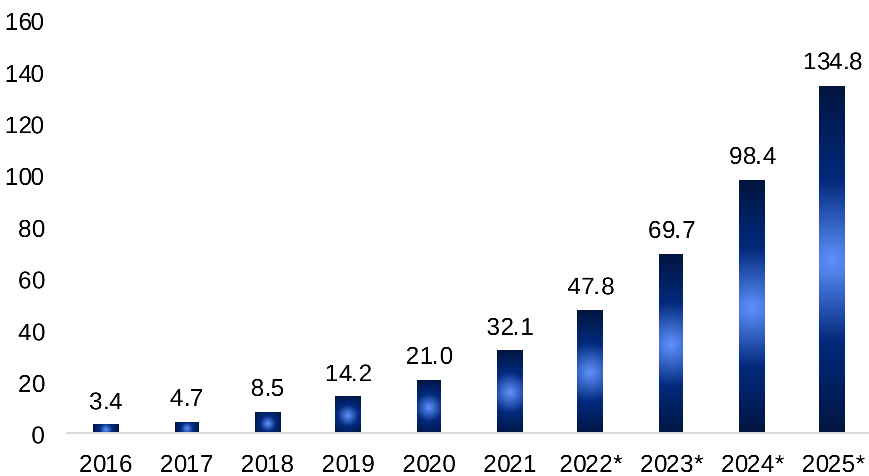
Investment Thesis

BABA presents a strong opportunity stemming from a dominant competitive position and strong initiatives towards ecommerce and cloud.

Major Chinese EC Player GMV share trend



Forecasted Market Size of Public Cloud Service ($B)



Market Share Stabilization	Take-Rate Expansion	Cloud Computing & Logistics Segment Growth
Prolonged Market Dominance: In 2019 they had a GMV share of 67% which has declined by declining. We believe BABA will gain stabillze market share at 40%, contrary to the Streets view at 36% in 2025. **New Management:** We believe that the new management's four initiatives for 2024 will bring reaccelerated growth to Alibaba. Investments in product supply, competitive advantages, quality service, and purchase frequency along with cloud investing will lead to TTG returning to growth. Baba plans to achieve this by focusing on the acquisition and retention of high-quality users.	**Mix Shift Benefit:** Taobao and Tmall Group (TTG) are Alibaba's core e-commerce business and are experiencing a mix-shift towards Taobao. Taobao has a lower take rate than Tmall due to their merchants paying only for spending on advertising, no commissions. **Merchant Acquisition Impact:** Alibaba has/is acquiring new merchants that will drive the Taobao take rate due to more ad spending. The street has not considered this or the continued DAU YoY growth and investments in the Taobao app. We expect Taobao's take rate to be 1.26%, which gives an 38.5% upside compared to street expectations.	**Public Recognition:** AliCloud's public cloud services received digital transformation and generative AI capabilities owing recognition for performance against competitors. **AliCloud's LTP:** Public cloud spending in China is projected to grow 13% on average for the next 4 years. The public cloud revenue accounts for ~70% of the revenue share for AliCloud, which is only expected to triple in the next two years from 32B$ in 2023 to 90B$ in 2025.

Catalyst I: GMV Market Share

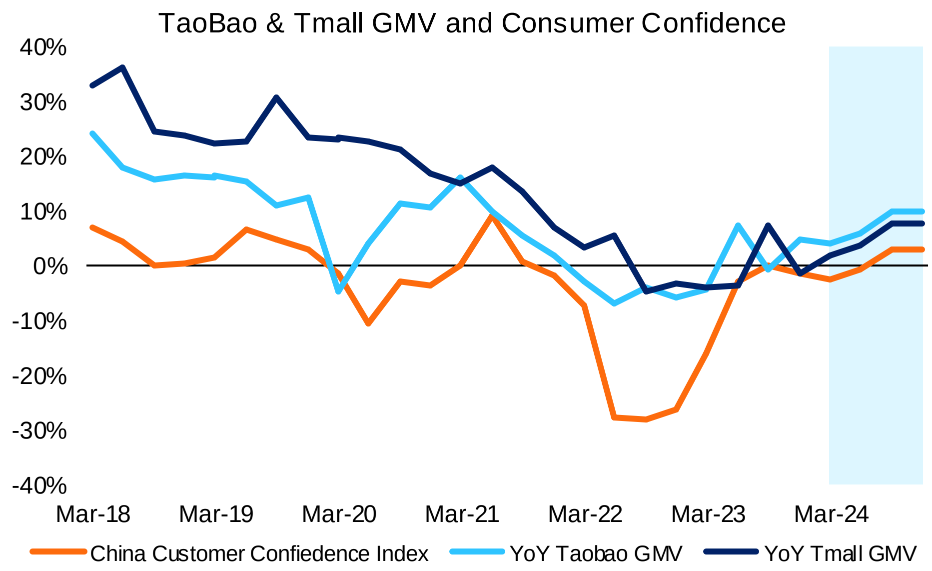
Baba has been losing market share for years, however we expect market share to stabilize due to management initiatives.

Forecast of Key Drivers of GMV Market Share

Key Drivers of Market Share: We differ from the street's perspective that GMV Market Share will decline and forecast Alibaba's GMV market share to stabilize at 40% due to renewed investment in product experiences. We arrived at this by forecasting an upside for Total Retail Consumer spending compared to the street. We have this variant view due to our optimistic look on China's Disposable Income YoY growth and China's Consumer Confidence YoY growth. In addition, we hold the opinion that domestic ecommerce will steadily grow, despite the negative outlook on the overall Chinese economy. Due to these key drivers, we expect Taobao market share YoY grow at 7.41% over next two years with Tmall not far behind at 5.48%. This provides an upside to the streets value of 3.10% and .08%, respectively.

Stabilization of Market Share: This is due to Taobao and Tmall's initiatives of putting users first, building a prosperous ecosystem, and realizing technology-driven innovation. Examples include Taobao currently increasing their front-page exposure to channels for livestreaming, price-competitive products, and neighborhood shopping categories to satisfy users' diverse needs, through testing new interfaces on their app. Tmall is also doing something similar by using AI initiatives to help merchants improve their services and attract new customers.

Expected Rise in Consumer Confidence to Drive GMV

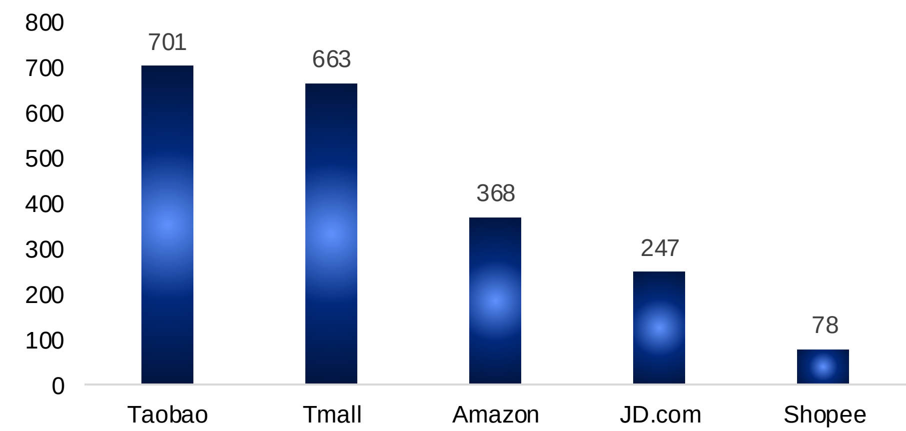


Alibaba's Initiatives to Drive GMV Market Share

Early Success of Initiatives: Alibaba's management has outlined four new initiative to drive GMV Market share of Taobao and Tmall Group. In this past quarter they focused on their user-first and competitive pricing strategies in Taobao and Tmall Group was effective as they had GMV growth. This was driven by a robust increase in numbers of active buyers and order volume. We expect this to continue in 2024, as management keeps divesting and reinvesting into the above areas.

Initiatives for Regrowth: To reaccelerate growth of Taobao and Tmall Commerce Group in 2024, investments in the following four fields will propel TTG's market share driving Alibaba to capture more GMV market share. Investments in product supply, competitive advantages, quality service, and purchase frequency along with cloud investing will lead to TTG returning to growth. Baba plans to achieve this by focusing on acquisition and retention of high-quality users.

Leading Global Online Marketplaces (Billions)



Catalyst II: Take-Rate Expansion

Alibaba, specifically TTG's take rate has been low, however we expect it to grow due to management initiatives.

Take-Rate Key Driver Forecasts

Take Rate Breakdown: Alibaba's take rate is broken down into two segments containing Taobao and Tmall's take rate. Taobao has a lower take rate than Tmall, due to not charging commission.

Taobao Forecast: Street expects Taobao's take rate to be .91% YoY, however we disagree and expect Taobao's take rate to have significant upside due to them not charging commission and a significant increase in merchants. We forecasted Taobao's take rate to be 1.26% YoY, which give us an upside of 38.5%.

Tmall Forecast: On the other hand, Tmall focuses on strict quality control and the authentication process. Tmall's take rate is influenced by commission and has been negatively affected by consumption downgrade. This results in the street expecting Tmall's take rate to be 5.15% YoY, again we disagree due to a less negative outlook on the Chinese economy and due to our expectation of steady growth in Chinese ecommerce resulting in higher consumption than expected. However, we were conservative and hold with street expectations.

Management Take-Rate Upside Initiatives

Management Initiatives: Alibaba has had significant changes in management, and they came ready with specific initiatives. Management is focused on driving take-rate due to their increased user engagement, continued DAU YoY growth, investments in the Taobao app, and increased investments in merchants.

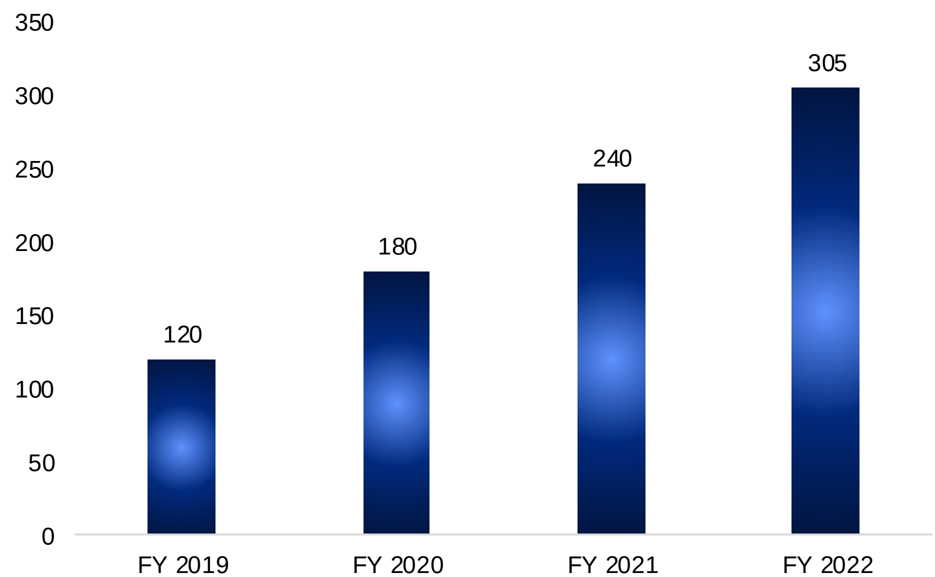
Taobao App: The company has scaled back spending on Taobao Deals and Taocacai, and reallocated the investment into the Taobao app by investing in traffic and content acquisition. A new feature Taobao has used that has improved customer services is starting to support 'Refund Only', which is allowing consumers to apply for a refund without returning the item with quality issue. In addition, we see an increase in Taobao's take rate due to management's initiative of increasing consumers' demand of price competitive products offered on the platform.

Merchant Growth: In addition, they also had their number of merchants continue to grow at a double-digit rate and have been able to do so while onboarding a wide range of brands and merchants. This drives GMV market share and take-rate as Taobao and Tmall are able to provide consumers the most comprehensive selection of products among its peers. Specifically, for Taobao we believe the increased number of merchants is increasing their take-rate and we can see with Taobao's take rate exceeding street expectations.

Take Rate Competitive Landscape

Competitors	Take Rates by Percentage
Alibaba	**4%**
eBay	9%
Amazon Market-Place	15%
Etsy	17%
JD.com	20%
PDD	3%

Number of Annual Active Users on Alibaba's Platforms



Catalyst III: Cloud Computing and Logistics Segment

AliCloud's recapture of market share and Cainiao's rapid expansion will increase revenue growth

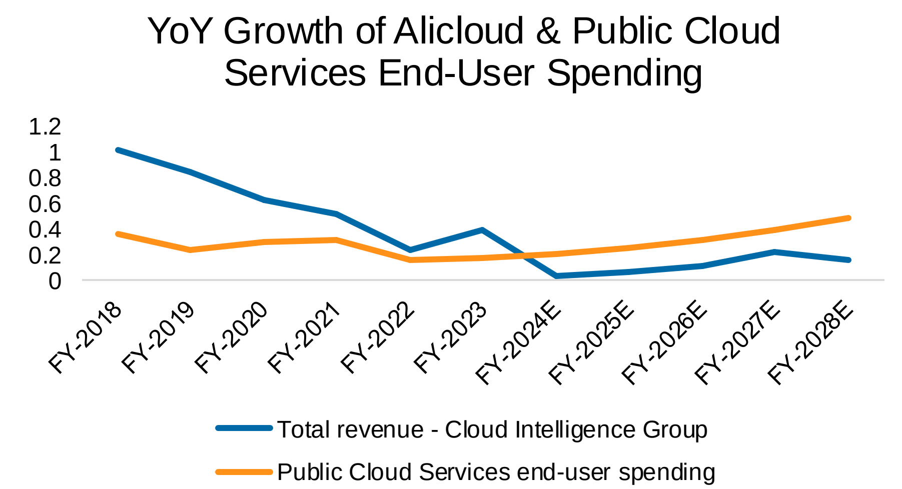
Increase in Cloud Growth

Top Player in Public Cloud: Alibaba Cloud was recognized as a leader among the eleven Chinese public cloud providers. Public Cloud revenue accounts for approximately 70% of revenue for Alicloud. The street is pessimistic due to the pause on the anticipated spin off however due to the synergies between Alicloud, TGG, and Dingtalk, we do not believe that this assessment is not a true Alicloud's performance

Aggressive Market Share Growth: Alicloud has been shifting their strategy to recapture market share in the cloud services. This has been reflected by their price cuts in core products once in April last year and again in the next week. This will lead to an increase in market share and total paying customer count.

Increase in End-User Spending: There is a correlation between the YoY growth of revenue for Alicloud and the YoY growth of end-user spending for public cloud services. There is a projected increase in growth for the next 4 years however the street believes that there will be a decrease for Alicloud.

Growth Comparison between Total Revenue & Spending



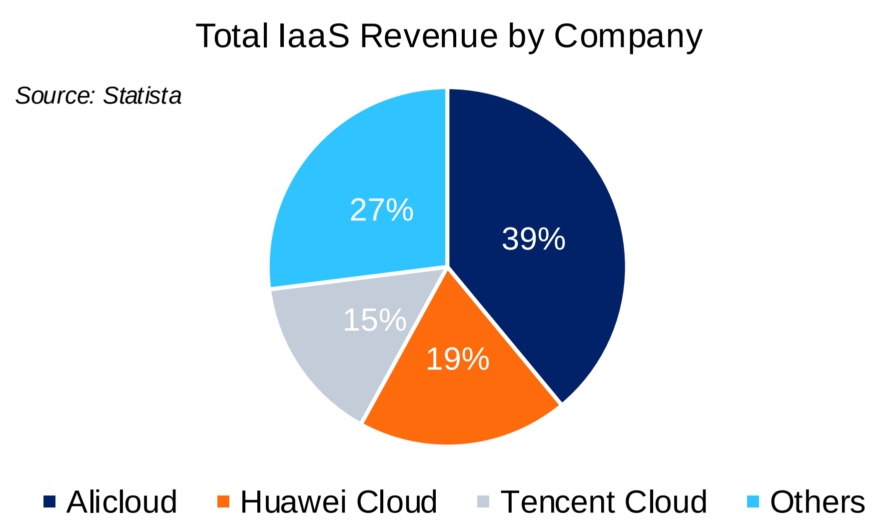
AI and Cainiao accelerating growth

Rise of DingTalk and AI Integration: DingTalk reached 700 million individual users by the end of 2023 and 25 million organizations. 120,000 of those clients are paying users. Underpinning the performance of DingTalk is AliCloud's new large language model (LLM) Tongyi Gianwen and will enable the push of AI agents.

Cainiao's Impressive Growth: Cainiao is the logistics and supply chain branch of Alibaba. They have been seeing strong growth (27% in first 9 months of FY2023) and there is still ample room for growth. They are expected to be one of the fastest growing branches of Alibaba and are seeing more independence in management.

International Revenue Potential: With the increase in international E-commerce growth for Alibaba and its subsidiaries, Cainiao's growth can be amplified significantly. Additionally, Alibaba was ranked as the world's third largest IaaS provider and is still in a "land grab" mode. They are priced cheaper to gain market share.

Alicloud's Dominance in Cloud Services



Valuation

BABA Presents Significant Upside Based on An Expected Recover in E-Commerce and Cloud Market Share

Alibaba Valuation Based on FY2025E	Taobao	Tmall	AIDC	Cloud Services	Cainiao	All Others
GMV	4,141,110.02	4,180,432.68	3,698,611.11	5,041.88	N/A	N/A
Monetization Rate	1.59%	5.43%	3.51%	23,615.63	N/A	N/A
Total Revenue	**182,229.49**	**343,204.21**	**129,716.59**	**119,067.25**	**115,676.44**	**281,254.31**
Y/Y Growth Rate	8.91%	7.78%	28%	3.75%	19%	4%
Expected Price/Sales Ratio	1.80x	1.60x	1.60x	1.50x	1.60x	1.20x
Implied Equity Value	328,013.08	549,126.74	207546.5457	178,600.88	185,082.30	337,505.17
Shares Outstanding	20,293.00	20,293.00	20,293.00	20,293.00	20,293.00	20,293.00
Implied Segment Share Price	$16.16	$27.06	$10.23	$8.80	$9.12	$16.63
Implied Share Price	**$88.00**					
Current Share Price	$74.63					
Implied Upside	*17.92%*					

Comparable Companies Analysis				**EV/EBITDA Multiple**			**P/E Multiple**		
Company Name	**Ticker**	**Equity Value**	**Enterprise Value**	**2022A EV/EBITDA**	**2023E EV/EBITDA**	**2024E EV/EBITDA**	**2022A P/E**	**2023E P/E**	**2024E P/E**
Pindoduo	PDD	173,230	143,010	15.9x	17.6x	11.8x	25.6x	24.5x	19.8x
JD.com	JD	36,190	12,420	29.4x	4.5x	3.7x	60.3x	10.2x	9.6x
Meituan Dianping	MPNGF	142,149	474,210	191.8x	14.4x	8.6x	(142x)	40.9x	25.8x
Vipshop Holdings	VIPS	10,499	8,030	5.7x	4.5x	4.0x	9.6x	8.7x	9.1x
Alibaba	**BABA**	**187,837**	**124,240**	**15.4x**	**14.4x**	**5.5x**	**30.3x**	**25.6x**	**13.4x**
Upper Quartile					11.9x	7.8x		25.3x	18.2x
Median					14.4x	5.5x		24.5x	13.4x
Mean					11.1x	6.7x		22.7x	15.5x
High					17.6x	11.8x		40.9x	25.8x
Low					4.5x	3.7x		8.7x	9.1x

Risks and Mitigations

Global government regulations, market share loss, and higher than expected costs are major risk factors for Alibaba

Risk 1: Further market share loss

- Competitors such as PDD may take more market share than current
- This can be mitigated by BABA's global expansion and shift in focus to international ecommerce
- Larger Chinese internet companies (e.g. Baidu and Tencent) can be threatening to Alibaba's Local Services and Cloud Group
- Can be mitigated by cloud expansion and BABA's strategy to focus on public cloud over private cloud.

Risk 2: Current investments may be a long-lasting effort

- Implementation of new models (e.g. the AE *Choice* model) may take longer than expected
- Higher-than-expected costs to integrate new retail initiatives, resulting in potential earnings drag
- BABA is currently undergoing various major structural changes within the company, (such as the 1+6+N), some of which may require a greater effort and to fully implement than currently projected, which will also increase the costs associated as well.

Risk 3: Limitations by Chinese government

- US-China tension may hinder global expansion of Alibaba into the US, which will be detrimental due to projected market share loss
- Chinese government political risk, as well as potential steeper than expected economic slowdown in China – impact revenue
- BABA's revenue and net income are significantly impacted by the economic conditions in China and globally
- Due to being based in and primarily operating in China, BABA's operations are mostly governed by PRC laws, rules, and regulations
- US government restrictions are limitations preventing Alibaba's Cloud Computing Segment from spinning off – as long as the current restrictions hold, Cloud will not be spun out (in the near future)

High Impact

3 — Heightened US-China geopolitical tensions may result in the slowing of BABA's plan of expanding to a more global landscape. Furthermore, as long as US regulations on the amount of chips that can be sent to China remain limited, BABA will not be able to spin out its Cloud Intelligence Group in the near future. Furthermore, domestic government regulations and China's economic conditions may pose risks to BABA's revenue and operations.

2 — Underscored by the recent change in CEO, BABA is currently undergoing many drastic shifts in company structure, including implementations of new models and retail initiatives such as the AE *Choice* model. Another example is the 1+6+N, where BABA is individualizing each of the 6 branches of the company by providing each segment with its own board of directors. These structural shifts are prone to take a larger than expected effort and cost which may result in a potential earnings drag for BABA.

1 — We expect market share to stabilize in the near future, but there is a risk that new dominant ecommerce companies such as PDD and JD will continue to eat up market share. This can be mitigated by BABA's global expansion and shift in focus to international ecommerce and public over private cloud. However, if BABA continues to experience market loss, revenue may be impacted heavily.

Low Impact

Low Probability | **High Probability**