

COMPANY RESULTS

Baidu Inc (9888 HK)

1Q23: Solid Ad And Cloud Recovery; Strong Earnings Beat; Generative AI As Key Focus

Baidu's 1Q23 earnings came in better than expectations. Revenue grew 10% yoy to Rmb31b, 3.8% above the street's estimate. Gross margin expanded 6ppt yoy to 51%, beating consensus expectation. Non-GAAP operating profit was Rmb6.4b, up 61% yoy, while non-GAAP operating profit margin came in at 21%, better than our estimate. Non-GAAP net profit improved by 48% yoy to Rmb5.7b through operating leverage, 32% above consensus estimate. Maintain BUY. Target price: HK\$187.00 (US\$193.00).

1Q23 RESULTS

Year to 31 Dec (Rmbm)	1Q22	4Q22	1Q23	QoQ	YoY	UOBKH	Var	Cons	Var
Total Net revenue	28,411	33,077	31,144	-6%	10%	30,090	3.5%	30,008	3.8%
Online marketing services	16,929	19,571	17,972	-8%	6%	17,330	3.7%		
Others	11,482	13,506	13,172	-2%	15%	12,760	3.2%		
COGS	15,546	16,945	15,152	-11%	-3%	15,781	-4.0%		
Gross profits	12,865	16,132	15,992	-1%	24%	14,309	11.8%	14,181	12.8%
GPM	45.3%	48.8%	51.3%	2.6 ppts	6.1 ppts	47.6%	3.8 ppts	47.3%	4.1 ppts
Operating expenses	10,346	11,697	11,110	-5%	7%	11,239	-1.2%		
Non-GAAP operating income	3,996	8,245	6,428	-22%	61%	4,931	30.4%		
Non-GAAP OPM	14%	25%	21%	-4.3 ppts	6.6 ppts	16.39%	4.3 ppts		
Non-GAAP net income	3,879	5,371	5,727	7%	48%	4,489	27.6%	4,340	32.0%
Non-GAAP EPS (RMB)	1.37	1.89	2.02	7%	48%	1.60	26.0%	1.62	24.9%
Non-GAAP Net Margin	13.7%	16.2%	18.4%	2.2 ppts	4.7 ppts	14.9%	3.5 ppts	14.5%	3.9 ppts

Source: Baidu Inc, UOB Kay Hian

RESULTS

- Ad revenue growth entered positive trajectory.** In 1Q23, Baidu Inc's (Baidu) core search revenue climbed 7.6% yoy to Rmb23b. Core online marketing revenue grew 6% yoy and came in 3.7% better than our expectations, primarily contributed by the rapid recovery in verticals with high offline exposure such as travel, healthcare, business services and local services but e-commerce and games remain under pressure. Gross merchandise value facilitated by Baidu grew 55% yoy in 1Q23. In Mar 23, Baidu App's monthly active users reached 657m, up 4% yoy. Managed Page accounted for 49% of Baidu Core's online marketing revenue in 1Q23. iQiyi delivered an accelerated revenue growth of 14.7% yoy to Rmb8.3b (1Q22: -8.7%; 4Q22: +2.8%), driven by subscription revenue growth of 24% yoy, and 5% yoy growth from advertising revenue. In 1Q23, Baidu continued to return value to shareholders and has repurchased US\$195m shares.
- Margin overview.** Gross margin edged up 6ppt to 51% yoy. 1Q23 non-GAAP operating income came in at Rmb6.4b with non-GAAP operating margin expanding by 6.6ppt yoy to 21%, mainly driven by a sequential decline in headcount, channel spending and promotional marketing expenses. Baidu Core also delivered 23% core operating profit margin in 1Q23, improving from 1Q22's 17.2%. Non-GAAP net profit was Rmb5.7b, which is 32% above the street's estimates, translating to non-GAAP net profit margin of 18.4%.

KEY FINANCIALS

Year to 31 Dec (Rmbm)	2021	2022	2023F	2024F	2025F
Net turnover	124,493	123,675	137,185	152,219	166,409
EBITDA	16,402	22,388	26,728	26,571	31,750
Operating profit	10,518	15,911	19,920	19,678	24,963
Net profit (rep./act.)	7,591	7,534	20,438	19,710	24,539
Net profit (adj.)	18,830	20,680	26,348	28,925	34,788
EPS (Fen)	676.7	733.4	907.2	966.9	1,140.1
PE (x)	16.3	15.1	12.2	11.4	9.7
P/B (x)	1.4	1.4	1.3	1.2	1.0
EV/EBITDA (x)	12.7	9.3	7.8	7.8	6.5
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Net margin (%)	6.1	6.1	14.9	12.9	14.7
Net debt/(cash) to equity (%)	(20.6)	(26.5)	(43.4)	(47.3)	(50.8)
ROE (%)	3.9	3.5	8.6	7.3	8.1
Consensus net profit	-	-	22,467	25,840	29,581
UOBKH/Consensus (x)	-	-	1.17	1.12	1.18

Source: Baidu Inc, Bloomberg, UOB Kay Hian

BUY

(Maintained)

Share Price	HK\$124.30
Target Price	HK\$187.00
Upside	+50.4%

COMPANY DESCRIPTION

Baidu Inc is a leading internet company that offers algorithmic search, enterprise search, news, voice assistance, online storage and navigation services.

STOCK DATA

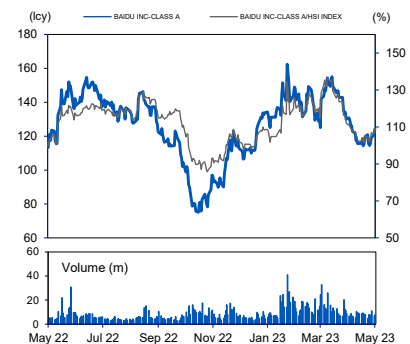
GICS sector	Communication Services
Bloomberg ticker:	9888 HK
Shares issued (m):	2,255.4
Market cap (US\$m):	347,639.5
Market cap (US\$m):	44,353.1
3-mth avg daily t'over (US\$m):	201.3
Price Performance (%)	

52-week high/low HK\$162.50/HK\$75.10

1mth	3mth	6mth	1yr	YTD
(4.4)	(16.1)	28.7	9.7	11.3

Major Shareholders	%
BlackRock Inc	6.7
BBH & CO	4.9
Vanguard Group Inc	3.9
FY23 NAV/Share (Rmb)	88.00
FY23 Net Cash/Share (Rmb)	38.16

PRICE CHART



Source: Bloomberg

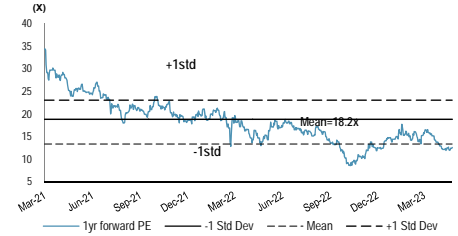
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STOCK IMPACT

- AI Cloud achieved profitability in 1Q23.** Other revenue delivered 14.7% yoy growth, improving from 9.2% yoy in 4Q22, mainly contributed from the resilient AI-powered businesses and cloud business. AI Cloud delivered a decelerated growth of 8% yoy to Rmb4.4b, adversely impacted by the delay in fee collection and cloud project completion. In addition, AI Cloud achieved profitability on a non-GAAP operating level this quarter by improving standardisation and phasing out low quality projects.
- Strategically created an ecosystem centred around Ernie bot,** to foster the widespread adoption of AI-generated solutions across various scenarios. Baidu launched Ernie bot on 16 March and embedded generative AI with Cloud on 27 March. By strengthening user traction, this will facilitate the accumulation of large-scale human feedback as well as stimulate rapid model iteration and customisation to meet evolving market needs. In addition, Baidu has been working with prominent industry players in financial services, software, education and enterprise resource planning companies. As of 9 May, over 300 companies have participated in the testing of Ernie in 400 internal scenarios. Leveraging the power-packed foundation models, Baidu continues to explore new techniques to seamlessly integrate the unique four-stack AI capabilities.
- Significant progress in Apollo Go to supplement growth.** Baidu's intelligent driving division saw tremendous growth in 1Q23, with the number of rides provided on Apollo Go soaring 236% yoy and reaching nearly 660,000. Apollo Go, a ride-hailing service, obtained Beijing's first approval on 17 March to operate fully driverless without a driver and safety operator. Currently, Apollo Go is operating in three cities while Baidu is focused on expanding its fleet and passenger adoption in regions to conduct seamless commercialisation. With over 135 autonomous vehicles and one-third of paid Apollo Go rides being fully driverless, Baidu is confident in expanding the number of rides to optimise cost to establish a sustainable and profitable business model.

12-MONTH FORWARD PE BAND



Source: Bloomberg, UOB Kay Hian

EARNINGS REVISION/RISK

- Our 2023 revenue estimates are largely unchanged in view of the positive ad recovery sentiment and possibility of AI Cloud regaining momentum.** We raise non-GAAP net profit forecasts by 11%/16% for 2Q23/2023 respectively seeing the higher-than-expected margin improvement in 1Q23. We expect Baidu to deliver adjusted net profit of Rmb6.2m in 2Q23, which should translate into net margin of 18.8%.
- Risks:** a) Weaker advertising business due to the macro slowdown and fierce competition in China's advertising industry, b) uncertainties facing the Autonomous Driving segment and robotaxi launch, c) shrinking government budget, and d) the US ban on the supply of high-end chips to Chinese tech giants.

VALUATION/RECOMMENDATION

- Maintain BUY with a target price of HK\$187.00 (US\$193.00).** We remain optimistic on Baidu's growth trajectory given its strong recovery in ad revenue and the ongoing investment in growth initiatives which it believes its leading AI technology can empower. Our target price implies 2.2x 2023F P/S and 15x 2023F PE. The company is currently trading at 12.6x 12-month forward PE, below its historical mean of 18.2x.

SHARE PRICE CATALYST

- a) Market share expansion in the AI Cloud segment and AD segment, b) higher monetisation rates across all business units, c) increase in synergies between Baidu's core business and new initiatives.

SOTP VALUATION

Segment (US\$m)	Rev 23E	NOPAT 23E	NOPAT 23E	P/E (x) 2023E	EV/S (x) 2023E	Valuation (Rmb mn)	Valuation (US\$ mn)	Baidu's stake	To Baidu	\$/share	% of
Core, Advertising	74,531	23,254	3,854	8.4	0	220,136	32,373	100%	32,373	91.3	47%
Cloud (ex ACE)	2,106				8	114,541	16,844	100%	16,844	47.5	25%
iQiyi, long form video	4,641	136	294		1	21,419	3,150	56%	1,770	5.0	3%
Autos	1,600				4	93,946	13,816	82%	11,277	31.8	16%
Xiaodu	867				2	13,600	2,000	60%	1,200	3.4	2%
Subtotal									63,464	179	93%
Total investments									4,595	13.0	7%
Core op. + investments									68,059	191.9	99%
Net cash									23,171	65.3	34%
NAV	22,213	2,912	3,622	23.0x	3.5x				91,230	257.3	133%
less holdco discount								25%	(22,807)	(64.3)	-33%
Total, in US\$m	22,213			17.3x	2.6x				68,422	193	
Total, in HK\$m									530,272	187	

Source: Baidu, UOB Kay Hian

PROFIT & LOSS

Year to 31 Dec (Rmbm)	2022	2023F	2024F	2025F
Net turnover	123,675	137,185	152,219	166,409
EBITDA	22,388	26,728	26,571	31,750
Deprec. & amort.	6,477	6,807	6,893	6,787
EBIT	15,911	19,920	19,678	24,963
Total other non-operating income	(6,981)	1,360	(427)	(603)
Associate contributions	(2,150)	(1,057)	(576)	(251)
Net interest income/(expense)	3,332	5,316	7,660	8,344
Pre-tax profit	10,112	25,539	26,335	32,453
Tax	(2,578)	(5,102)	(6,625)	(7,914)
Minorities	(25)	1,410	970	970
Net profit	7,534	20,438	19,710	24,539
Net profit (adj.)	20,680	26,348	28,925	34,788

BALANCE SHEET

Year to 31 Dec (Rmbm)	2022	2023F	2024F	2025F
Fixed assets	23,973	23,373	23,275	22,928
Other LT assets	154,150	156,694	161,371	166,105
LT debt	n.a.	n.a.	n.a.	n.a.
Cash/ST investment	64,486	112,725	137,503	166,631
Other current assets	148,364	151,196	154,232	157,171
Total assets	390,973	443,988	476,381	512,836
ST debt	5,343	3,016	3,016	3,016
Other current liabilities	74,287	70,968	71,922	70,961
Other LT liabilities	73,538	73,538	73,538	73,538
Shareholders' equity	223,478	252,970	284,409	321,825
Minority interest	8,393	8,393	8,393	8,393
Total liabilities & equity	390,973	443,988	476,381	512,836

CASH FLOW

Year to 31 Dec (Rmbm)	2022	2023F	2024F	2025F
Operating	22,218	43,925	41,318	47,705
Pre-tax profit	10,112	25,539	26,335	32,453
Tax	(2,578)	(5,102)	(6,625)	(7,914)
Deprec. & amort.	6,477	6,807	6,893	6,787
Working capital changes	(10,893)	(8,815)	(12,129)	(14,348)
Other operating cashflows	19,100	25,495	26,843	30,727
Investing	6,085	(16,089)	(16,874)	(18,912)
Capex (growth)	(9,915)	(11,403)	(13,113)	(15,080)
Others	16,000	(4,686)	(3,761)	(3,832)
Financing	10,906	(1,992)	335	335
Dividend payments	335	335	335	335
Issue of shares	0	335	335	335
Loan repayment	0	0	0	0
Others/interest paid	10,571	(2,662)	(335)	(335)
Net cash inflow (outflow)	39,209	25,845	24,779	29,128
Beginning cash & cash equivalent	47,671	86,880	112,725	137,503
Changes due to forex impact	0	0	0	0
Ending cash & cash equivalent	64,486	112,725	137,503	166,631

KEY METRICS

Year to 31 Dec (%)	2022	2023F	2024F	2025F
Profitability				
EBITDA margin	18.1	19.5	17.5	19.1
Pre-tax margin	8.2	18.6	17.3	19.5
Net margin	6.1	14.9	12.9	14.7
ROA	2.0	4.9	4.3	5.0
ROE	3.5	8.6	7.3	8.1
Growth				
Turnover	(0.7)	10.9	11.0	9.3
EBITDA	36.5	19.4	(0.6)	19.5
Pre-tax profit	(6.2)	152.6	3.1	23.2
Net profit	(0.8)	171.3	(3.6)	24.5
Net profit (adj.)	9.8	27.4	9.8	20.3
EPS	8.4	23.7	6.6	17.9
Leverage				
Debt to total capital	2.3	1.1	1.0	0.9
Debt to equity	2.4	1.2	1.1	0.9
Net debt/(cash) to equity	(26.5)	(43.4)	(47.3)	(50.8)

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