SECTOR UPDATE

Internet – China

Potential Implications Of De Minimis Tax Exemption

On 5 February, the USPS temporarily suspended the receipt of parcels from mainland China and Hong Kong. However, on 7 February, Trump signed an order delaying the cancellation of the de minimis trade exemption. We think PDD's valuation will be partially overshadowed by the potential tariff pressures on Temu but supported by ongoing strategic mitigation efforts. As such, we believe that the uncertainties in policy changes will remain as the key concern throughout 2025.

WHAT'S NEW

- **Overview of recent tariff policy development.** On 1 Feb 25, Trump signed an order imposing a 10% tariff on goods imported from China. The order eliminated the de minimis exemption for small packages valued under US$800 from China. On 5 Feb 25, the US Postal Service (USPS) announced a temporary suspension of international inbound parcels from China Post and Hong Kong Post to the US. Meanwhile, other express carriers stated that shipments from China, which previously fell under the US$800 de-minimis threshold, will require Importer of Record (IOR) documentation. The IOR is the entity or individual responsible for ensuring compliance with legal import and customs clearance procedures. In addition, on 5 Feb 25, the US government stated that it is considering adding Chinese e-commerce retailers, including Temu, to the Department of Homeland Security's "forced labour" list. However, on 7 Feb 25, Trump announced an Executive Order to temporarily resume the de-minimis treatment under 19 U.S.C. 1321, overturning certain provisions of his decision from 1 Feb 25 to impose additional tariffs on Chinese imports.

- **Sensitivity analysis: Potential implications on Temu.** Given the recurring geopolitical uncertainty, we believe the impact from the aggregate 36%, which comprises 10% tariff and 26% tax (consisting of both import tax duty and section 301 tariffs after removing the de minimis exemption) will be applied to its fully entrusted products. We expect the incremental costs to be partially passed on to end consumers, while merchants and Temu are expected to absorb part of the extra tariff and tax costs. With a 36% hike in costs for fully entrusted products, we assume consumers will bear 60-70% of US gross merchandise value (GMV), while Temu will absorb 40% of the aggregate incremental cost, leading to a 15% increase in overall average order value (AOV). Based on our sensitivity analysis, we assume that 65% of US GMV under the fully-entrusted model will be impacted by the incremental tariff. With this, we estimate a demand elasticity of -8% to 8%, which leads to a 0.3-5.7% decline in 2025 EPS, as well as a 0.1-1.5% dip in 2025 revenue. All in, we opine that the impact on Pinduoduo's (PDD) 2025 performance will be manageable on the back of the company's strong domestic business profit base.

- **Temu's price advantages still exist,** as compared with US local offline and US players, like Amazon. While Temu's price advantage over offline retailers will narrow, it will remain competitive at 58% of offline retail pricing, dropping from the previous 44%. This projection accounts for the impact of: a) the additional 10% tariff; b) applicable import duties and tariffs based on the estimated Temu category mix; and c) Section 301 tariffs, where we assume Temu will fully pass through the incremental 36% tariff to consumers, while US local retailers will absorb only a partial increase, given that roughly one-third of their products are sourced from China. Despite tariff-related uncertainties, we believe e-commerce platforms will maintain a cost advantage over US offline retailers due to their structurally lower operating costs, with fewer intermediaries between manufacturers and end consumers. In addition, we expect Chinese platforms to continue diversifying their merchant bases beyond China by expanding partnerships with local merchants.

MARKET WEIGHT

(Maintained)

STOCK PICKS

Company	Ticker	Rec	Share Price (LC$)	Target Price (LC$)
Pinduoduo	PDD US	BUY	117.5	155
Alibaba	9988 HK	BUY	113.8	135

Source: Bloomberg, UOB Kay Hian

ANALYST(S)

Julia Pan Meng Yao
+8621 5404 7225 ext 808
juliapan@uobkayhian.com

Soong Ming San
+603 21471912
mingsan@uobkayhian.com

PEER COMPARISON

Company	Tickers	Rec	Price @ 12-Feb-24 (LC$)	Target Price (LC$)	Upside/(Downside) To TP (%)	Market Cap (LC$m)	PE 2025F (x)	PE 2026F (x)	PE 2027F (x)	EV/EBITDA 2025F (x)	EV/EBITDA 2026F (x)	EV/EBITDA 2027F (x)	EV/Sales 2025F (x)	EV/Sales 2026F (x)	EV/Sales 2027F (x)	ROE 2025F (%)
Pinduoduo	PDD US	BUY	117.5	155	32	163,153	9.2	7.7	7.2	6.4	5.1	5.1	1.8	1.5	1.3	49.2
Alibaba	9988 HK	BUY	113.8	135	19	2,163,067	12.4	11.0	9.5	7.5	6.9	6.2	1.5	1.4	1.3	8.6

Source: Bloomberg, UOB Kay Hian

- **Temu's strategic efforts to mitigate tariff pressures:**

  a) Shifts towards semi-trust business model from fully trusted model in the US. Temu has been transitioning from a fully entrusted model, which relied on direct air freight shipments benefitting from de minimis exemptions, to a rapidly expanding semi-entrusted model. As of Sep 24, the semi-entrusted model, where merchants ship products via sea freight under traditional trade channels, accounted for 25% of Temu's US GMV. We expect short-term supply chain disruptions, extended customs clearance times by 3-5 additional days, and increased documentation costs. These factors may further drive Temu's ongoing transition towards a diversified business model, particularly the expansion of its semi-entrusted model (utilising traditional trade and sea freight) and expedite the development of its third-party (3P) marketplace by onboarding more US-based sellers.

  b) Geographical diversification and broader business model expansion. Temu's US share of global monthly average users (MAU) had declined significantly, from 100% at launch in early-23 to just 15% as of Dec 24, driven by rapid growth in South America and the Middle East. Beyond air freight direct shipments, Temu had introduced semi-entrusted models across 19 countries as of Jan 25, reducing its dependence on de minimis exemptions.

- **Temu's expansion into the South Korean market with 8.23m users.** On 10 February, Temu stated that it is actively preparing for direct entry into the South Korean market. Since late-24, the company has been recruiting employees in key departments such as human resources, administration, marketing, and logistics in South Korea, while also planning to establish an integrated logistics system to support its business expansion. Temu had already launched its website in South Korea and quickly amassed a significant user base. As of Jan 25, Temu's active user count in South Korea reached 8.23m, ranking third after Coupang (33.02m) and Alibaba's AliExpress (9.12m). This rapid growth highlights Temu's increasing foothold and competitiveness in the South Korean market.

- **Potential adverse impact deemed to be limited and manageable.** Alibaba's international business has minimal exposure to the US market. For PDD, 40% of Temu's GMV originates from the US, though in 2024, Temu contributed a 10% drag on PDD's overall group profit and carries minimal implied valuation based on PDD's current market capitalisation. The market has ascribed limited value to Temu's business in PDD's current market cap, as investors await regulatory clarity on US tariffs, de-minimis rules in multiple countries, personal data concerns, and other factors before assigning any meaningful value to Temu's business.

VALUATION/RECOMMENDATION

- **Maintain BUY on Pinduoduo (PDD US) with a lower target price of US$155.00.** Our target price implies 12x 2025F PE based on 2025 SOTP valuation with 10x PE on its core business and 36x PE on Temu. PDD is now trading at 8.4x 2025F PE against an 18% EPS CAGR over 2025-28.

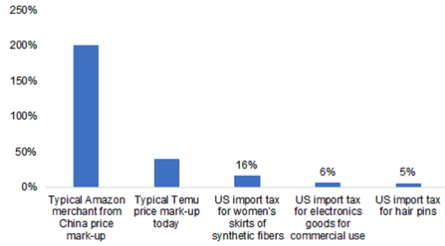
- **Maintain BUY on Alibaba (9988 HK) with a target price of HK$135.00 (US$135.00)** as we roll forward our SOTP valuation to FY26, which implies 13.5x FY26F PE. Alibaba is trading at 11x FY26F PE, 1SD below its historical mean of 24x on the back of an 11% EPS CAGR from FY26-29.

SECTOR CATALYST AND RISK

- **Catalysts:** a) Fast overseas expansion; b) continued gain in consumer mindshare on higher purchase frequency and value-for-money products; c) strong sales of agricultural products driven by higher growth in online grocery categories; and d) improved monetisation rates.

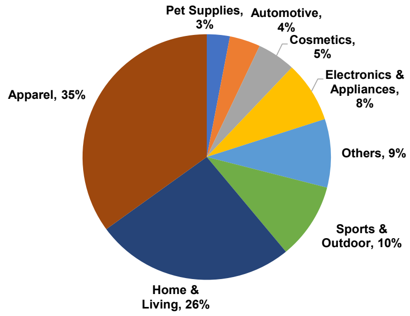
- **Risks:** a) Geopolitical risks from local retailer protection regulations; b) potential heavy investment and increasing logistic costs which may weigh on margins; c) increasing competition in the e-commerce sector; and d) intensified regulatory scrutiny by the US government.

US IMPORT TAX COMPARED WITH THE TYPICAL MARK-UP OF AMAZON AND TEMU



Source: Amazon, Pinduoduo, UOB Kay Hian

TEMU'S CATEGORY MIX



Source: Temu, UOB Kay Hian

SENSITIVITY ANALYSIS OF REMOVAL OF DE MINIMIS EXEMPTION

2025F EPS (Rmb)		------------------ % portion of incremental tariff ------------------				
		60%	63%	65%	68%	70%
Demand Elasticity	-8%	86.34	86.12	85.97	85.75	85.60
	-4%	87.37	87.21	87.09	86.92	86.81
	0%	88.41	88.29	88.21	88.10	88.02
	4%	89.44	89.38	89.34	89.27	89.23
	8%	90.48	90.47	90.46	90.45	90.44

% impact on EPS		---------------- % portion of incremental tariff ----------------				
		60%	63%	65%	68%	70%
Demand Elasticity	-8%	-4.8%	-5.1%	-5.3%	-5.5%	-5.7%
	-4%	-3.7%	-3.9%	-4.0%	-4.2%	-4.3%
	0%	-2.6%	-2.7%	-2.8%	-2.9%	-3.0%
	4%	-1.4%	-1.5%	-1.5%	-1.6%	-1.7%
	8%	-0.3%	-0.3%	-0.3%	-0.3%	-0.3%

Source: PDD, UOB Kay Hian

2025F Revenue (Rmb mn)		------------------ % portion of incremental tariff ------------------				
		60%	63%	65%	68%	70%
Demand Elasticity	-8%	499,025	498,690	498,467	498,132	497,909
	-4%	500,600	500,344	500,173	499,917	499,747
	0%	502,175	501,998	501,880	501,702	501,584
	4%	503,750	503,652	503,586	503,488	503,422
	8%	505,325	505,306	505,292	505,273	505,260

% impact on Revenue		---------------- % portion of incremental tariff ----------------				
		60%	63%	65%	68%	70%
Demand Elasticity	-8%	-1.3%	-1.4%	-1.4%	-1.5%	-1.5%
	-4%	-1.0%	-1.1%	-1.1%	-1.1%	-1.2%
	0%	-0.7%	-0.7%	-0.8%	-0.8%	-0.8%
	4%	-0.4%	-0.4%	-0.4%	-0.4%	-0.5%
	8%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%

Source: PDD, UOB Kay Hian

POTENTIAL REGULATORY RISK ON CHINA CROSS-BORDER PLATFORMS

Potential regulatory risk	Details	Progress/Recent updates	Potential impacts on China cross border platforms
10% tariff tax and de minimis tax exemption	On 5 Feb 25, the USPS announced a temporary suspension of international inbound parcels from China Post and Hong Kong Post to the US. Meanwhile, other express carriers have stated that shipments from China, which previously fell under the US$800 de minimis threshold, will now require IOR documentation. The IOR is the entity or individual responsible for ensuring compliance with legal import and customs clearance procedures.	Removed on 7 Feb 25, under the new executive order announced by the White House, Chinese goods will continue to benefit from the de minimis exemption.	Impact all merchants/suppliers based in China
De minimis tax exemption	In 2023, the US Senate and congressional committees called multiple times to eliminate de minimis treatment (current threshold of US$800) for goods originating from China and Russia.	In "Introduction" phase and the acts must undergo approval by the House and the Senate and receive the President's signature to be enacted into law.	Impact all merchants/suppliers based in China
	De Minimis Working Group (Sep 23) analyses different facets of the small package/de minimis landscape to enhance compliance and enable CBP to detect and intercept high-risk shipments potentially posing a threat to public safety.	Enhancing the supply chain and reducing risks within the low-value package sector.	
	Recent update: CBP launched the Update Timing of Entry Type 86 Release Messages in Air Environment (Non-Express) system on 27 Jan 24, to better evaluate risk with de minimis package shipments to ensure that hold requests from CBP are promptly communicated to the trade community for timely responses.	Effected on 27 Jan 24	
Personal data	Announcement of the drafting of an executive order designed to limit foreign governments' access to sensitive personal data of Americans, potentially compromising national security, on 23 Jan 24.	The executive order could be completed and released in the upcoming month.	Impact China cross-border platforms
	The proposed RESTRICT Act, introduced in Mar 23, would grant the US President the authority to close down e-commerce applications considered a national security threat, particularly those handling sensitive personal data of over 1,000,000 individuals in the US.	User data storage: Since 2022, TikTok has been directing the data of American users to servers based in the US owned by Oracle.	
Elevation of import tariffs	Potential increase of US tariffs to 60% on Chinese imports, Trump said on 27 Jan 24	No progress	Impact all merchants based in China
SME/Local retailer protection measures	In Sep 23, Indonesia implemented a ban on TikTok Shop, prompting discussions among regulators in other ASEAN markets.	In Sep 23, Indonesia implemented a ban on TikTok Shop. Bytedance subsequently formed a strategic partnership with Tokopedia, a local player, and has been undergoing a trial period of 3-4 months since Dec 23.	Impact all merchants/suppliers based in China
Operation restrictions	In Apr 23, the US China Economic and Security Review Commission released an "Issue Brief On China E-Commerce Platforms," which raised concerns regarding forced labour, intellectual property rights violations, product quality, and other related issues.	US congressional committee finds compliance issues in Temu regarding UFLPA and forced labour products, echoing concerns from the Apr 23 "Issue Brief On China E-Commerce Platforms." Ongoing investigation is planned.	Impact China cross-border platforms
		Uniqlo suing Shein over the alleged sale of imitation products.	
	Montana sought to ban TikTok across the state, delivering a blow to an unprecedented attempt to completely restrict a single app within a state's borders.	Montana's TikTok ban, scheduled for 1 January, has been temporarily halted by Federal judge, who deemed it an overreach of state authority and likely a violation of the First Amendment.	
	US Lawmakers introduced a bill in Congress on 6 Mar 24 that would require China's ByteDance to divest TikTok within 165 days to avoid a ban of the video app in the US. The bill states that TikTok is controlled by a foreign adversary and poses a threat to US national security.	Ongoing	

Source: Regulatory authorities, Bloomberg, UOB Kay Hian

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