

SECTOR UPDATE

Internet – China

Navigating Headwinds And Uncovering Opportunities Upon Tariff Pressures

Chinese internet companies' share prices have dropped 10-30% mtd following the implementation of incremental tariffs from the US. Chinese internet companies have limited business exposure to the US except for PDD's Temu. However, the 34% tariffs announced by China on all US imports could have potential implications for China mega-caps' AI capex in relation to US chip imports. We prefer domestic-focused plays which stand to benefit from domestic policy stimuli, with Southbound inflow to be a key driver. Maintain MARKET WEIGHT.

WHAT'S NEW

- **Undemanding valuation and ample net cash reserves as defensive plays.** Mtd, the share prices of internet companies have corrected by 10-30%. We reviewed valuations across the sector and uncovered potential opportunities in view of the mega-caps' undemanding valuation and ample net cash as a solid moat to navigate against geopolitical uncertainties. In addition, Chinese internet companies have limited US business exposure, with the majority of revenue and profit generated from domestic e-commerce, entertainment and advertising, and overseas exposure diversified across Asia, Europe, the Middle East, Latin America and the US. For the e-commerce sector, we prefer Alibaba and JD for their major domestic revenue exposure and limited impact from the recent incremental tariff implementation. Alibaba's and JD's net cash and long-term investment are 77%/93% of total market cap, currently trading at an undemanding 11x and 8x 2025F PE against 10%/13% 2025-28F EPS CAGR respectively. In terms of internet companies with rich net cash reserves, we like Beike, EDU, TAL with net cash and long-term investment at 76%/75%/239% of total market cap respectively.
- **Compared with the previous market trough** (average 11x PE) in Oct 22 over concerns on ADR de-listings and the May 24 trough (average 12x PE), China internet PE is currently trading at 12x P/E, with a 10-15% profit growth outlook. We see a 15-35% downside to trough valuations for some mega-caps, although companies such as Baidu, PDD and Netease are trading at 17-33% lower than the trough PE multiples.
- **Potential impact of recent tariffs.** Following the implementation of an incremental 34% US tariff on Chinese imports (effective 5 Apr 25) and the upcoming removal of the de minimis exemption for packages under US\$800 from Mainland China and Hong Kong (effective 2 May 25). We expect these changes to impact Temu's US order volumes, while also causing short-term logistics delays that may dampen consumer sentiment due to increased processing volumes by USPS and third-party logistics providers. We expect ASP increases for Temu's fully entrusted SKUs, where Temu operates under a principal model and bears full end-to-end air freight costs. As such, we forecast Temu's US GMV to grow at a moderated 6% yoy to US\$20b in 2025.

PEER COMPARISON

Company	Tickers	Rec	Price @8 Apr 25 (lcy)	Target Price (lcy)	Upside/(Downside) to TP (%)	Market Cap (lcy m)	PE			EV/EBITDA			EV/Sales			ROE
							2025F	2026F	2027F	2025F	2026F	2027F	2025F	2026F	2027F	
Alibaba	9988 HK	BUY	102.50	170.00	65.9	1,959,581	10.8	9.6	8.5	6.2	5.5	4.9	1.3	1.2	1.1	12.0
Tencent	700 HK	BUY	440.40	670.00	52.1	4,053,079	15.7	14.1	12.4	14.0	12.6	11.1	5.4	5.0	4.5	21.8
Meituan	3690 HK	BUY	140.60	216.00	53.6	859,023	16.2	13.1	10.6	12.1	9.7	8.0	1.8	1.5	1.4	22.1
JD.com	9618 HK	BUY	137.60	220.00	59.9	445,874	7.6	7.0	6.6	4.9	4.4	4.0	0.2	0.2	0.2	17.6
NetEase	9999 HK	BUY	145.30	200.00	37.6	468,558	12.8	11.7	10.7	8.7	8.0	7.3	2.8	2.6	2.5	22.6
Trip.com	9961 HK	BUY	433.40	630.00	45.4	279,148	15.6	13.9	12.0	12.4	10.5	9.3	3.6	3.2	2.8	12.9
Baidu	9888 HK	HOLD	78.60	84.00	6.9	220,456	8.0	7.4	6.5	1.2	1.1	1.0	0.3	0.3	0.3	9.4
PDD	PDD US	BUY	100.00	130.00	30.0	138,891	8.2	6.8	5.9	5.3	4.3	3.7	1.4	1.2	1.1	44.9
Kuaishou	1024 HK	BUY	46.00	75.00	63.2	198,019	9.2	7.9	6.6	5.7	4.7	4.2	1.2	1.1	1.0	27.6
Tongcheng	780 HK	BUY	19.80	22.00	11.2	46,093	13.7	11.5	10.0	8.8	7.6	6.8	1.9	1.7	1.5	10.5
Kingsoft	3888 HK	BUY	36.40	55.00	51.1	48,594	23.4	19.4	15.8	6.3	5.4	4.9	2.1	1.9	1.7	7.1
EDU	9901 HK	BUY	33.60	52.00	54.8	55,609	13.2	10.6	9.4	5.0	3.9	3.6	0.6	0.5	0.5	10.4
TAL	TAL US	BUY	10.90	18.00	64.5	6,610	24.6	17.1	4.1	18.3	10.4	8.6	1.1	0.8	0.4	3.2

Source: Bloomberg, UOB Kay Hian

MARKET WEIGHT

(Maintained)

STOCK PICKS

Company	Ticker	Rec	Share Price (lcy)	Target Price (lcy)
Tencent	700 HK	BUY	440.40	670.00
Alibaba	9988 HK	BUY	102.50	170.00
TAL	TAL US	BUY	10.90	18.00
Trip.com	9961 HK	BUY	433.40	630.00

Source: Bloomberg, UOB Kay Hian

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• **Sensitivity analysis for PDD.** 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 34% 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). For a base-case scenario, we assume a 35% tariff and a 15.6% US revenue exposure to PDD. This translates to 2025F EPS of US\$74, implying 0% impact on EPS. For a bear-case scenario, we assume a 65-105% tariff and a 16-18% US revenue exposure to PDD, which will lead to a 7-13% negative impact to PDD's 2025F EPS. For a bull-case scenario, we assume a 35% tariff and a lower 14% US revenue exposure to PDD, translating to 2025F EPS of US\$77.2, implying a positive 4% impact on EPS.

• **Intact progress in overseas expansion to mitigate geopolitical risks.** Temu has expanded to over 60 countries and regions, including the US, Germany, Japan and South Korea. The US and European markets account for 80% of Temu's GMV. Despite potential adverse impact from US tariffs, we opine Temu's price advantages still exist as compared with US offline and online 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%.

**ESSENTIALS**

• **Potential increase in chip restriction.** The 34% tariffs announced by China on all US imports could have implications for China mega-caps' AI capex in relation to US chip imports. However, with the mega-caps shifting focus from AI infrastructure to AI applications, we remain confident about the resilient AIGC growth outlook on ramped-up capex in 2025.

• **Alibaba lifted its AI-related capex guidance** with annual spending of Rmb100b or US\$14b for the next three years. We expect Alibaba Cloud to solidify its AI/cloud scale leadership and we raise our cloud revenue growth to 23-25% yoy in the next three years compared with our previous estimate of 13%.

• **Tencent expects capex to be in the low teens of revenue,** while we estimate Rmb93b-108b for 2025-26. Meanwhile, Tencent purchased NVIDIA H20 chips worth several billion renminbi, primarily to support WeChat's integration with DeepSeek. However, despite being China's largest cloud provider, this remains relatively modest compared with the US\$60b-80b annual capex of leading US tech giants.

• **Intact 2025 outlook for other internet companies:**

- **JD:** JD guided double-digit growth in revenue and non-GAAP net profit in 2025, propelled by the national subsidies programme. We forecast an 8.7% yoy revenue growth and 13% yoy earnings growth in 2025. JD's strategy will centre on optimising supply chain efficiency to drive margin expansion, aiming to achieve high single-digit margins in the long term. Regarding category-level margin improvements, JD sees substantial upside potential across supermarkets.

- **Meituan:** We forecast 1Q25/2025 revenue to grow 17%/18% yoy and core local commerce to expand 17%/18% yoy. Core local commerce EBIT is expected to see 25-28%/18% yoy growth in 1Q25/2025. Even with expansions into other countries, incremental losses are expected to be moderate. Future efforts will focus on increasing GTV market share and improving profitability, with the ultimate goal of becoming the market leader in Saudi Arabia. Meituan's AI-related capex is expected to increase significantly by several billion renminbi in 2025, with depreciation costs in the low billions.

- **TCOM:** 1Q25 and 2025 outlooks remain intact. 1Q25 revenue is guided to grow 14-19% yoy to Rmb13.8b, mainly boosted by international tourism. Gross margin is expected to remain flattish yoy at 81%, mainly supported by AI integration in 1Q25. Non-GAAP operating margin is guided to drop 5ppt yoy to 27% in 1Q25, with sales & marketing (S&M) ratio estimated to grow 5ppt yoy to 24%. TCOM also forecasts overall revenue growth of 14.5% yoy to Rmb61b for 2025, with gross margin remaining flattish yoy at 80.5% in 2025.

**SENSITIVITY ANALYSIS**

Sensitivity analysis		Tariff				
EPS 2025F		65%	75%	85%	95%	105%
US exposure	12.0%	91.3	89.9	89.5	89.1	88.7
	13.0%	89.3	87.8	87.3	86.8	86.2
	14.0%	87.3	85.7	85.0	84.4	83.8
	15.0%	85.4	83.6	82.8	82.1	81.3
	16.0%	83.4	81.5	80.6	79.8	78.9
	17.0%	81.4	79.4	78.4	77.4	76.4
18.0%	79.5	77.3	76.2	75.1	74.0	

  

% impact to EBITA p		Tariff				
US exposure		65%	75%	85%	95%	105%
US exposure	12.0%	7%	5%	5%	4%	4%
	13.0%	5%	3%	2%	2%	1%
	14.0%	2%	0%	0%	-1%	-2%
	15.0%	0%	-2%	-3%	-4%	-5%
	16.0%	-2%	-5%	-6%	-7%	-8%
	17.0%	-5%	-7%	-8%	-9%	-10%
18.0%	-7%	-9%	-11%	-12%	-13%	

Source: PDD, UOB Kay Hian

### EARNINGS REVISION

- **Pinduoduo (PDD US)**. We lowered our 1Q25/2025 revenue estimates by 5%/3% respectively after factoring in the potential supply chain disruptions and uncertainty around demand elasticity due to likely price hikes passed on to end-consumers by merchants. We cut our 1Q25/2025 non-GAAP net profit estimates by 7%/7% respectively. As such, we lower our target price to US\$130.00. We assigned 9x 2025F PE for PDD's core valuation and 2x 2025F EV/sales for Temu which contributes US\$48.7b or 24% valuation to PDD. Our target price implies 10.8x 2025F PE against a 17% EPS CAGR over 2025-28. PDD is now trading at 8.7x 2025F PE and 2.8x 2025F EV/sales, below its historical mean of 6x.

### VALUATION/RECOMMENDATION

- **Tencent (700 HK)**. Maintain BUY with a target price of HK\$570.00. We saw accelerated grossing contributions from strong overseas game titles and rejuvenation of evergreen titles. Tencent's potential launch of HoK World and HoK Breaking Dawn in 2025 serves as the key catalyst, with total monthly revenue projected to reach Rmb1.5b-2.5b. Our target price implies 22.0x 2025F PE. The company is trading at 15.2x 2025F PE, 1SD below its historical mean of 25.3x.
- **Alibaba (9988 HK)**. Maintain BUY with a target price of HK\$170.00 (US\$170.00) which implies 17.2x FY26F PE. We assigned a 10x EV/EBITA to the core commerce business and 15x EV/sales to the cloud business, generating HK\$87.00 and HK\$44.00 in our HK\$170.00 SOTP valuation. We expect e-commerce growth to stabilise, but believe AI has tremendous growth potential as Alibaba transforms into the largest AI company in China.
- **TAL Education (TAL US)**. Maintain BUY with a target price of US\$18.00. We believe TAL's new initiatives such as learning content solutions and hardware products, overseas education programmes and AI applications could open up new pillars for growth, despite operating losses in the medium term. Our target price implies 13x FY26F PE and 0.2x PEG vs a three-year EPS CAGR of 37%. The company is trading at 10.6x FY26F PE.
- **TCOM (9961 HK)**. Maintain BUY with a target price of HK\$630.00 (US\$81.00). TCOM is poised for robust market share gains from strong international and outbound travel demand. We opine TCOM's optimistic prospects in 2025 are fuelled by market share gains from international travel benefitting from heightened investment in its international brand Trip.com. Our target price implies 24.5x 2025F PE, in line with global peers.

### SECTOR CATALYST AND RISK

- **Catalysts:** Supportive government policies, increasing online retail penetration driven by less developed areas and younger generations, continuous improvement in technology and e-commerce infrastructure, commitment to artificial intelligence generated content (AIGC) development to boost efficiency.
- **Risks:** High user acquisition expense and increased competition as multiple players are looking to expand their market share, heavy investment in new retail and local services strategy to drag down e-commerce companies' margins and ROE, and slower-than-expected top-line growth.

### MARKET CAP VS NET CASH

Company	Ticker	Price (lcy)	Mkt Cap (lcy m)	2025F (x)	2026F (x)	Price Changes month-to-date	2025F Net Cash (Rmbm)	Net Cash / Mkt Cap	(Net Cash + LT Inv) / Mkt Cap	EPS CAGR 25-28F	Revenue CAGR 25-28F	Valuation 10/31/2022	Trough 3/31/2024	Potential Downside/Upside
Alibaba	9988 HK	102.50	1,959,581	10.8	9.6	-27%	289,884	15%	77%	13%	11%	7.7	7.7	-29% -29%
Tencent	700 HK	440.40	4,053,079	15.7	14.1	-17%	210,841	5%	42%	15%	12%	11.6	12.1	-26% -23%
Meituan	3690 HK	140.60	859,023	16.2	13.1	-23%	232,836	27%	53%	21%	12%	14.2	9.1	-12% -44%
JD.com	9618 HK	137.60	445,874	7.6	7.0	-19%	103,787	23%	93%	11%	5%	13.3	6.5	74% -15%
NetEase	9999 HK	145.30	468,558	12.8	11.7	-10%	153,760	33%	42%	-1%	9%	8.4	15.0	-34% 17%
Trip.com	9961 HK	433.40	279,148	15.6	13.9	-15%	111,268	40%	87%	14%	13%	11.2	12.5	-28% -20%
Baidu	9888 HK	78.60	220,456	8.0	7.4	-13%	103,129	47%	163%	13%	7%	7.6	10.7	-5% 33%
PDD	PDD US	100.00	138,891	8.2	6.8	-17%	180,161	130%	214%	13%	11%	8.8	9.7	8% 18%
Kuaishou	1024 HK	46.00	198,019	9.2	7.9	-28%	2,628	1%	38%	12%	8%	11.3	9.3	23% 1%
Tongcheng	780 HK	19.80	46,093	13.7	11.5	-2%	12,400	27%	40%	11%	8%	14.9	16.5	9% 20%
Beike	2423 HK	48.10	174,272	25.0	15.0	-25%	67,836	39%	73%	n.a.	10%	19.7	19.6	-21% -22%
Kingsoft	3888 HK	36.40	48,594	23.4	19.4	-20%	28,624	59%	75%	36%	20%	51.6	19.3	121% -17%
EDU	9901 HK	33.60	55,609	13.2	10.6	-13%	38,323	69%	73%	16%	12%	n.a.	35.7	n.a. 169%
TAL	TAL US	10.90	6,610	24.6	17.1	-19%	16,401	248%	268%	98%	53%	20.9	16.0	-15% -35%

Source: Bloomberg, UOB Kay Hian

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