

Baidu (BIDU US)

Accelerating Gen AI-empowered business transformation

Baidu announced (16 May) its 1Q24 results: revenue was RMB31.5bn, up 1.2% YoY, and was in line with Bloomberg consensus. Non-GAAP net income of Baidu Core was RMB6.6bn, better than consensus at RMB5.1bn, thanks to better-than-expected cost control. Management highlighted that AI-related ads and cloud revenue are continuously ramping up, and it is accelerating generative AI-empowered search business transformation, to drive better long-term business development prospects. Although ads revenue growth will likely see short-term volatility as the contribution from Gen AI-related search results in overall results has climbed to 11% of the total currently with relative low monetization, management stressed that it will closely monitor the business adjustment impact, and will drive further operating efficiency improvement across other business lines to buffer the margin impact. Baidu's Cloud business is sustainably generating operating profit with decent margins, and long-term margin expansion remains on track with the support from increased revenue contribution from AI cloud. We fine-tune our SOTP-based TP to US\$183.0 (was US\$183.2). Maintain BUY.

- Gen AI cloud revenue continued to ramp up.** Non-ad revenue was up 6% YoY to RMB6.8bn and accounted for 29% of Baidu Core revenue (1Q23: 28%). Baidu Cloud revenue reached RMB4.7bn in 1Q24, up 12% YoY (4Q23: 11%; 1Q23: 8%), thanks to the wearing off of the high-base effect for the smart transportation vertical, and the ramp-up in revenue generation from Gen AI-related cloud revenue. Management highlighted that: 1) Gen AI and foundation model contributed 6.9% of AI cloud revenue in 1Q24 (4Q23: 4.8%); 2) cloud business has recorded a decent operating margin, which should be better than the level of industry peers; and 3) cloud revenue growth would be higher if excluding the smart transportation vertical. We estimate YoY revenue growth of Baidu Cloud to recover to 14% YoY in 2024E (2023: 6%).
- Accelerating ads business transformation with Gen AI.** In 1Q24, Baidu Core's online ads revenue was RMB17.0bn, up 3% YoY, and was 1% better than consensus. Management highlighted that it has been leveraging generative AI capability to transform ads business. Currently, about 11% of Baidu's search result pages are filled with generated results, and these results provide more accurate, better organized, and direct answers to users' questions, which enhance user experience. Management expects softer monetization in the near term owing to the business adjustment as Gen AI-related search results bear low monetization, but guided to closely monitor the impact, which in our view speaks to a manageable margin impact. While this may dampen ads revenue growth in the near term, it shall benefit long-term development if Baidu could unlock the monetization potential from the cost per sale (CPS) ads format leveraging Gen AI capabilities.
- Driving operating efficiency improvement across business lines should provide support for margin.** Baidu's GPM was 51.5% in 1Q24, up 0.2ppt YoY. Non-GAAP OPM for Baidu Core was 23.5%, 1.6ppt better than Bloomberg consensus, thanks to better-than-expected operating efficiency gains. Although the short-term headwind on ads revenue growth brought by business adjustment is likely to weigh on margin expansion, the move to drive operating efficiency improvement across business lines should provide support for margin, in our view. We forecast Baidu Core non-GAAP OPM to reach 24.7% in 2Q24E, flat YoY.

BUY (Maintain)

Target Price **US\$183.00**
 (Previous TP) US\$183.20
Up/Downside **65.2%**
Current Price **US\$110.75**

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Stock Data

Mkt Cap (US\$ mn)	39,666.2
Avg 3 mths t/o (US\$ mn)	218.1
52w High/Low (US\$)	155.99/94.41
Total Issued Shares (mn)	358.2

Source: FactSet

Shareholding Structure

Robin Yanhong Li	16.5%
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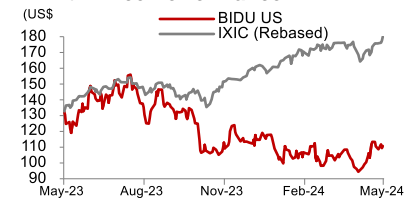
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	15.2%	9.2%
3-mth	3.4%	-2.6%
6-mth	1.3%	-14.6%

Source: FactSet

12-mth Price Performance



Source: FactSet

Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	124,493	123,675	134,598	138,474	149,352
YoY growth (%)	16.3	(0.7)	8.8	2.9	7.9
Adjusted net profit (RMB mn)	18,830.0	20,680.0	28,747.0	27,667.3	29,614.4
YoY growth (%)	(14.5)	9.8	39.0	(3.8)	7.0
EPS (Adjusted) (RMB)	53.53	58.90	81.06	77.25	81.87
Consensus EPS (RMB)	na	na	80.85	77.13	82.67
P/E (x)	27.0	36.8	13.8	13.3	12.2
ROE (%)	5.1	3.4	8.4	8.0	7.8

Source: Company data, Bloomberg, CMBIGM estimates

Figure 1: Baidu: quarterly financial results

(RMBbn)	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23	3Q23	4Q23	1Q24	1Q24 Consensus	Diff%
Baidu Group											
Online marketing	16.9	18.3	19.9	19.6	18.0	21.1	21.3	20.8	18.5	18.5	0.2%
YoY growth (%)	-6.4%	12.3%	-5.3%	-5.6%	6.2%	15.4%	7.0%	6.3%	2.9%		
Other services	11.5	11.4	12.6	13.5	13.2	13.0	13.1	14.1	13.0	13.0	0.0%
YoY growth (%)	14.4%	8.1%	15.9%	9.2%	14.7%	14.0%	4.0%	4.7%	-1.1%		
Total revenue	28.4	29.6	32.5	33.1	31.1	34.1	34.4	35.0	31.5	31.5	0.1%
YoY growth (%)	1.0%	-5.4%	1.9%	0.0%	9.6%	14.9%	5.9%	5.7%	1.2%		
Gross profit	12.9	14.5	16.3	16.1	16.0	17.9	18.2	17.5	16.2	15.8	2.8%
Operating profit	2.6	3.4	5.3	4.6	5.0	5.2	6.3	5.4	5.5	5.7	-4.3%
Non-GAAP net profit	3.9	5.5	5.9	5.4	5.7	8.0	7.3	7.8	7.0	5.6	25.9%
YoY growth (%)	-10%	3%	16%	32%	48%	44%	23%	44%	22%		
GPM (%)	45.3%	48.8%	50.0%	48.8%	51.3%	52.5%	52.7%	50.2%	51.5%	50.1%	1.3 ppt
OPM (%)	9.2%	11.5%	16.3%	13.9%	16.0%	15.3%	18.2%	15.4%	17.4%	18.2%	-0.8 ppt
Non-GAAP NPM (%)	13.7%	18.7%	18.1%	16.2%	18.4%	23.5%	21.1%	22.2%	22.2%	17.7%	4.6 ppt
Baidu Core											
Revenue	21.4	23.2	25.2	25.7	23.0	26.4	26.6	27.5	23.8	23.6	0.8%
YoY growth (%)	4.4%	-3.7%	2.3%	-1.2%	7.6%	14.0%	5.3%	7.2%	3.5%		
Baidu Core - online marketing	15.6	17.1	18.7	18.0	16.6	19.6	19.7	19.2	17.0	16.9	0.6%
YoY growth (%)	-3.6%	10.1%	-3.6%	-5.5%	6.3%	14.7%	5.2%	6.3%	2.7%		
Baidu Core - Others	5.8	6.1	6.5	7.6	6.4	6.8	6.9	8.3	6.8	6.6	2.6%
YoY growth (%)	34.4%	20.8%	24.1%	10.4%	11.1%	12.1%	5.5%	9.1%	5.7%		
Non-GAAP OP	3.7	5.1	6.7	5.5	5.4	6.5	6.7	6.2	5.6	5.2	8.2%
Non-GAAP NP	3.8	5.4	5.8	4.9	5.3	7.7	7.0	7.5	6.6	5.1	31.2%
YoY growth (%)	21.9%	-8.3%	-1.5%	6.3%	38.5%	41.2%	20.6%	52.6%	25.8%		
Non-GAAP OPM (%)	17.2%	22.1%	26.4%	21.4%	23.3%	24.7%	25.1%	22.5%	23.5%	21.9%	1.6 ppt
Non-GAAP NPM (%)	17.8%	23.5%	22.8%	19.2%	22.9%	29.1%	26.2%	27.3%	27.8%	21.4%	6.5 ppt

Source: Company data, Bloomberg, CMBIGM

Changes in forecast and valuation

Figure 2: Baidu forecast revision

RMB bn	Current			Previous			Change (%)		
	2024E	2025E	2026E	2024E	2025E	2026E	2024E	2025E	2026E
Revenue	138.5	149.4	159.7	141.6	150.9	159.4	-2.2%	-1.0%	0.2%
Gross profit	71.6	78.3	84.8	73.2	78.3	83.2	-2.1%	-0.1%	2.0%
Non-GAAP net profit	27.7	29.6	33.0	27.0	29.0	31.8	2.4%	2.1%	3.7%
Gross margin	51.7%	52.4%	53.1%	51.6%	51.9%	52.2%	0.1 ppt	0.5 ppt	0.9 ppt
Non-GAAP net margin	20.0%	19.8%	20.7%	19.1%	19.2%	20.0%	0.9 ppt	0.6 ppt	0.7 ppt

Source: CMBIGM estimates

SOTP valuation of US\$183.0 per ADS

Our SOTP-based target price is fine-tuned to US\$183.0, which translates into 17/16x 2024E/2025E PE on a non-GAAP basis, or 11/10x if excluding net cash. Our new SOTP-based target price comprises, per ADS:

- 1) US\$69.2 (was US\$68.1) for Baidu Core (main business, excluding Apollo and Baidu Cloud, mainly including the core search and feed ads business), based on an unchanged 7.0x 2024E non-GAAP PE.
- 2) US\$1.8 for Apollo ASD (unchanged), based on 2.0x 2030E revenue, and discounted back using a 13.0% WACC.
- 3) US\$32.2 for Baidu Cloud (was US\$35.2), based on 3.9x 2024E revenue; our valuation has been revised down mainly due to a lowering of target multiple, which is in line with that of industry peers that are covered by us.
- 4) US\$64.6 net cash (was US\$65.0).
- 5) US\$15.2 (was US\$13.2) for iQIYI and other investments, with a 30% holding discount applied to the share price of US\$21.7 as of 16 May market close.

Figure 3: Baidu: SOTP valuation

Segment	NOPAT (USDmn)	Valuation method/multiple	Valuation (RMBmn)	Valuation (USDmn)	Baidu's stake	Valuation of Baidu's stake (USDmn)	USD/ADS	Valuation as % of total (%)
Core business and cash								
1) Baidu core (ex-Apollo and Cloud)	3,539	7.0	178,883	24,776	100.0	24,776	69.2	37.8
2) Apollo ASD			4,740	656	100.0	656	1.8	1.0
3) Baidu Cloud (ex-ASD)		3.9	83,214	11,526	100.0	11,526	32.2	17.6
4) Net cash			167,080	23,141	100.0	23,141	64.6	35.3
Valuation of core business and cash						60,099	167.8	91.7
iQIYI and strategic investment								
1) iQIYI		Market value	35,752	4,952	51.5	2,550	7.1	
2) Trip.com group		Market value	272,408	37,730	10.8	4,075	11.4	
3) Uxin		Market value	120	17	9.1	2	0.0	
4) HAND Enterprise Solutions (300170 SH)		Market value	6,362	881	5.3	46	0.1	
5) Kuaishou		Market value	233,379	32,324	3.1	1,004	2.8	
6) Yusys Technologies (300674 SH)		Market value	15,260	2,114	5.1	109	0.3	
Valuation of iQIYI and investments						7,785	21.7	
Valuation of iQIYI and investment (with 30% holding discount)						5,450	15.2	8.3

Total Baidu valuation (USDmn)	65,549
Number of ADS outstanding (mn)	358
Valuation per ADS (USD)	183.0

Source: Company data, CMBIGM estimates

Note: 1) American depository share (ADS); iQIYI (IQ US); Trip.com Group (TCOM US); Uxin (UXIN US); HAND Enterprise solution (300170 CH); Kuaishou (1024 HK); Yusys Technologies (300674 CH); 2) data as of 16 May 2024 market close.

Risks

- 1) Slower-than-expected ramp-up in revenue generation from Gen AI-related business.
- 2) Slower-than-expected margin expansion.

Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Revenue	107,074	124,493	123,675	134,598	138,474	149,352
Cost of goods sold	(55,158)	(64,314)	(63,935)	(65,031)	(66,864)	(71,089)
Gross profit	51,916	60,179	59,740	69,567	71,609	78,263
Operating expenses	(37,576)	(49,661)	(43,829)	(47,711)	(47,549)	(50,705)
SG&A expense	(18,063)	(24,723)	(20,514)	(23,519)	(23,264)	(24,942)
R&D expense	(19,513)	(24,938)	(23,315)	(24,192)	(24,285)	(25,764)
Operating profit	14,340	10,518	15,911	21,856	24,060	27,558
Share of (losses)/profits of associates/JV	(2,248)	(932)	(1,910)	(3,799)	(844)	(879)
Adjusted EBITDA	27,504	24,914	29,663	35,824	37,193	41,302
Net Interest income/(expense)	2,255	2,130	3,332	4,761	4,918	5,465
Foreign exchange gain/loss	(660)	100	(1,484)	595	401	321
Other income/expense	9,403	(1,038)	(5,737)	1,785	(275)	(278)
Pre-tax profit	23,090	10,778	10,112	25,198	28,261	32,187
Income tax	(4,064)	(3,187)	(2,578)	(3,649)	(5,500)	(6,941)
After tax profit	19,026	7,591	7,534	21,549	22,761	25,246
Minority interest	(3,446)	(2,635)	(25)	1,234	1,491	1,792
Net profit	22,472	10,226	7,559	20,315	21,270	23,454
Adjusted net profit	22,020	18,830	20,680	28,747	27,667	29,614
BALANCE SHEET						
YE 31 Dec (RMB mn)						
Current assets	183,342	213,315	212,850	230,255	259,577	293,046
Cash & equivalents	35,782	36,850	53,156	25,231	55,584	86,994
Restricted cash	758	10,821	11,330	11,503	11,503	11,503
Account receivables	8,668	9,981	11,733	10,848	10,243	11,048
Other current assets	138,134	155,663	136,631	182,673	182,248	183,501
Non-current assets	149,366	166,719	178,123	176,504	174,153	176,869
PP&E	17,508	23,027	23,973	27,960	32,018	36,109
Intangibles	8,457	8,947	8,095	7,848	1,439	64
Goodwill	22,248	22,605	22,477	22,586	22,586	22,586
Other non-current assets	101,153	112,140	123,578	118,110	118,110	118,110
Total assets	332,708	380,034	390,973	406,759	433,730	469,915
Current liabilities	68,385	74,488	79,630	76,451	79,540	80,236
Short-term borrowings	3,016	4,168	5,343	10,257	10,257	10,257
Account payables	36,716	41,384	38,014	37,717	40,973	40,509
Other current liabilities	28,653	28,936	36,273	28,477	28,310	29,470
Non-current liabilities	72,480	81,594	73,538	67,700	62,731	62,403
Long-term borrowings	0	12,629	13,722	14,223	0	0
Bond payables	60,335	55,772	49,461	43,134	52,388	52,060
Obligations under finance leases	4,693	5,569	4,810	5,040	5,040	5,040
Deferred income	97	129	159	200	200	200
Other non-current liabilities	7,355	7,495	5,386	5,103	5,103	5,103
Total liabilities	140,865	156,082	153,168	144,151	142,271	142,640
Share capital	0	0	0	0	0	0
Capital surplus	47,213	73,888	79,855	87,099	87,202	87,305
Retained earnings	135,483	137,571	143,623	156,527	185,275	220,989
Other reserves	3,102	7,148	8,393	9,465	9,465	9,465
Total shareholders equity	185,798	218,607	231,871	253,091	281,942	317,759
Minority interest	6,045	5,345	5,934	9,517	9,517	9,517
Total equity and liabilities	332,708	380,034	390,973	406,759	433,730	469,915

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	23,090	10,778	10,112	25,198	28,261	32,187
Depreciation & amortization	18,180	16,438	14,725	14,908	5,742	5,654
Tax paid	(4,064)	(3,187)	(2,578)	(3,649)	(5,500)	(6,941)
Change in working capital	(18,207)	(18,691)	(16,758)	(13,067)	4,119	(1,362)
Others	5,201	14,784	20,669	13,225	6,685	7,007
Net cash from operations	24,200	20,122	26,170	36,615	39,307	36,545
Investing						
Capital expenditure	(5,084)	(10,896)	(8,286)	(11,190)	(8,286)	(8,286)
Acquisition of subsidiaries/ investments	(2,396)	(247)	(14)	(115)	0	0
Net proceeds from disposal of short-term investments	(486)	0	0	0	0	0
Others	(19,586)	(20,301)	4,356	(39,092)	(104)	(84)
Net cash from investing	(27,552)	(31,444)	(3,944)	(50,397)	(8,390)	(8,370)
Financing						
Net borrowings	12,390	8,840	(6,813)	(13,093)	(14,223)	0
Share repurchases	(13,054)	(7,581)	(1,925)	(4,764)	0	0
Others	6,329	22,137	2,348	3,695	12,818	3,236
Net cash from financing	5,665	23,396	(6,390)	(14,162)	(1,405)	3,236
Net change in cash						
Cash at the beginning of the year	34,439	36,540	47,671	65,236	37,574	67,087
Exchange difference	(212)	(943)	1,729	282	0	0
Cash at the end of the year	36,540	47,671	65,236	37,574	67,087	98,497
GROWTH	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Revenue	(0.3%)	16.3%	(0.7%)	8.8%	2.9%	7.9%
Gross profit	16.5%	15.9%	(0.7%)	16.4%	2.9%	9.3%
Operating profit	127.4%	(26.7%)	51.3%	37.4%	10.1%	14.5%
Net profit	992.5%	(54.5%)	(26.1%)	168.8%	4.7%	10.3%
Adj. net profit	21.1%	(14.5%)	9.8%	39.0%	(3.8%)	7.0%
PROFITABILITY	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Gross profit margin	48.5%	48.3%	48.3%	51.7%	51.7%	52.4%
Operating margin	13.4%	8.4%	12.9%	16.2%	17.4%	18.5%
Adj. net profit margin	20.6%	15.1%	16.7%	21.4%	20.0%	19.8%
Return on equity (ROE)	12.8%	5.1%	3.4%	8.4%	8.0%	7.8%
GEARING/LIQUIDITY/ACTIVITIES	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
Net debt to equity (x)	(0.5)	(0.5)	(0.5)	(0.5)	(0.6)	(0.6)
Current ratio (x)	2.7	2.9	2.7	3.0	3.3	3.7
Receivable turnover days	27.0	27.0	31.6	29.0	26.3	25.7
Payable turnover days	226.5	218.6	223.5	220.6	222.5	206.3
VALUATION	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec						
P/E	12.2	27.0	36.8	13.8	13.3	12.2
P/E (diluted)	12.3	27.5	37.1	14.0	13.5	12.3
P/B	1.5	1.3	1.2	1.1	1.0	0.9
P/CFPS	14.4	30.5	15.7	11.2	9.2	10.2

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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