Alibaba Group

December Quarter 2022 Results Conference Call

Transcript

Thursday, 23 February 2023

Introduction

Rob Lin

Head of Investor Relations, Alibaba Group

(Original)

Thank you. Good day, everyone. Welcome to Alibaba Group's December Quarter 2022 Results Conference call. With us are Daniel Zhang, Chairman and CEO; Joe Tsai, Executive Vice Chairman; Toby Xu, CFO. This call is also being webcast from our IR section of our corporate website. A replay of the call will be available on our website later today.

Now let me quickly cover the Safe Harbour. Today's discussion will contain forward-looking statements. Forward-looking statements involve inherent risk and uncertainties that may cause actual results to differ materially from our current expectations. For detailed discussions of these risks and uncertainties, please refer to our latest Annual Report on Form 20F and other documents filed at US SEC or announced on the website of the Hong Kong Stock Exchange. Any forward-looking statements that we make on this call are based on assumptions as of today and we do not undertake any obligation to update these statements except as required under applicable law.

Please note that certain financial measures that we use on this call, such as adjusted EBITDA, adjusted EBITDA margin, adjusted EBITA, adjusted EBITA margin, non-GAAP net income, non-GAAP diluted earnings per share or ADS, and free cash flow are expressed on a non-GAAP basis. Our GAAP results and reconciliation of GAAP to non-GAAP measures can be found in our earnings press release. Unless otherwise stated, growth rate of all stated metrics mentioned during this call refers to year-over-year growth versus the same quarter last year.

With that, I will now turn the call to Daniel.

December Quarter 2022 Highlights

Daniel Zhang

Chairman & CEO, Alibaba Group

(Original)

Thanks Rob. Hello everyone. Thank you for joining our earnings call today.

This past quarter, our business and operations experienced significant challenges due to the rapid changes in the COVID situation during December. Despite these challenges, we delivered double-digit year-on-year growth in our adjusted EBITA and free cash flow through effective business management, cost optimization, and operating efficiency.

With the lifting of COVID-related measures and end of the peak wave, everything is now quickly getting back on track. In general, consumer confidence and business confidence are rising. Logistics has resumed normal operations, with the entire supply and manufacturing chains becoming active. Digital transformation across different industries and sectors has accelerated significantly. Against this backdrop, our various businesses are showing positive trends.

Recently, the IMF raised the estimated GDP growth for China to 5.2% this year. Given the expectation for economic recovery following the lifting of COVID-related measures and China's reopening, I have chosen "progress" as the keyword internally to set the tone for Alibaba's development this year. We need to respond quickly to the changes in the macroenvironment and major cycles. The theme of "progress" represents the need to adapt to trends in the macroenvironment and for Alibaba's own development. In China's post-COVID economic development, although different businesses across our complex ecosystem face their own unique circumstances, we remain confident in our three main strategic pillars of consumption, cloud computing, and globalization.

Now I will share how our business performed this past quarter in a difficult COVID environment, together with some colour on the situation in January and February, and how we plan to capture opportunities across our businesses.

During the December quarter, the China consumer market was highly impacted by COVID cases. Taobao and Tmall GMV dropped mid-single digit year-on-year, and consumption demand was greatly suppressed. In terms of category, apparel and other discretionary goods were weak, while healthcare and wellness-related grew strongly. This is consistent with the data trend released by the National Bureau of Statistics of China. From January to early February of this year, overall sales of online physical goods remained weak, and our China commerce continued to be highly impacted due to COVID cases as well as people traveling home or to other places during the Spring Festival holidays. But as the influence of COVID cases and Spring Festival travel subsided in February, we have observed momentum in consumption recovery – especially recovery in categories such as apparel and sports & outdoor - as work and life returned to normal. All of our merchants have also expressed their strong desire to get to business. We expect this recovery will continue.

In our operations, we are strengthening the user experience and customer value proposition on Taobao and Tmall to reinforce our market leadership with the following measures:

- First, **enhance user stickiness and time spent**. Taobao and Tmall are home to China's most comprehensive population of online shoppers and is the most efficient consumer transaction platform. We are building on our competitive advantage by continuing to introduce a wider variety of consumption-related content in the form of short-form videos, livestreaming, and other formats to strengthen consumer stickiness, product discovery, influence, and user engagement.

- Second, **enhance value-for-money proposition**. Price is always a key factor in consumer purchasing decisions. We will continue to improve competitive pricing on products through the design of marketplace mechanisms, promotional marketing features, and retail model innovations such as Taobao Deals' direct-from-factory goods and farm-to-table offerings.

- Third, **neighbourhood digital retail**. We will cater to consumers' time-sensitive needs for high-frequency everyday necessities through our neighbourhood digital retail businesses, such as Taoxianda and Taocaicai, that fulfill orders from local supply chains using local delivery.

In local consumer services, Ele.me's restaurant order volume growth rate picked up towards the end of this quarter due to increased home-based consumption from COVID cases. Notably, non-restaurant order volume growth rate was far higher than what it was for restaurants. The business saw an increase in revenue due to higher average order value. Ongoing improvements in operating efficiency resulted in lower expense ratios in marketing and logistics. Ele.me continued to demonstrate positive unit economics and it will continue to improve. During COVID, Ele.me adjusted its operations strategy, safeguarded its delivery capabilities, and supported supply recovery.

During peak COVID cases, Amap's user scale and scale of services used were greatly affected. As cases eased, usage of Amap quickly recovered. Ride-hailing and hotel room booking volume grew very rapidly. Amap has become a new platform providing various destination-based consumer services. Fliggy's domestic and outbound travel activity also quickly grew during the Spring Festival holidays. As a result of our ongoing development of the supply chain and service capability over the past two years, recovery of Fliggy's domestic airplane ticket and hotel bookings was significantly faster than the overall domestic travel performance reported by the China National Tourism Administration, and noticeably better in comparison to 2019 before the COVID outbreak.

In international commerce, our various businesses made steady progress. Trendyol continued to deliver strong growth as overall order volume grew around 50% year-on-year, with local consumer services growing even faster. When Turkey was suddenly hit by earthquakes in early February, we actively organized and delivered support for emergency relief. So far, all our employees in Turkey are safe. Trendyol's business operations remain stable, and they have mobilized resources to aid disaster relief. As for Lazada, as the business continued to optimize for order volume growth, they also reduced loss per order by more than 30% year-on-year. We remain firmly committed to continuing to invest in Lazada's region of Southeast Asia. Through close collaboration with Cainiao, AliExpress greatly optimized time-bound order deliveries on key routes. As logistics service quality continued to improve and the impact of V.A.T. and FX rates in Spain and France continued to ease, AliExpress order volume is starting to show positive growth. Our globalization strategy will continue to be firmly focused on Southeast Asia and Europe through a mix of localized retail and cross-border commerce. We will continue to make sustainable long-term investments and build businesses that can withstand economic cycles.

Cainiao is celebrating its tenth anniversary this year. It has built a robust comprehensive business covering China and cross-border international logistics, last mile, logistics technology, and more. It is also continuing to make progress in green logistics and emergency response logistics. In China, Cainiao continued to expand its doorstep delivery services for our Taobao and Tmall consumers. During the most recent 11.11, more than 18 million orders from Taobao and Tmall were delivered to customers' doorsteps daily at its peak, which includes those delivered directly to doorstep or through Cainiao Post locations in residential communities. Cainiao has also built its own international logistics network over the past few years. As of this past quarter, it had more than 15 international sorting centres in operation.

Our cloud business's overall revenue growth rate this quarter was 3% year-on-year. The growth rate for public cloud was double-digit year-on-year, which was partially offset by a decline in hybrid cloud revenue from project delays due to COVID. In terms of revenue by industry, financial services, education, and automobiles are among the growth drivers.

We also announced an important organizational change towards the end of last year. I took on the role of Acting President of Alibaba Cloud in addition to my current role as Chairman and CEO of Alibaba Group. This decision was based on a few considerations:

- First, cloud computing is one of Alibaba's core strategies for the future. Innovation and other technologies will have an impact not just on Alibaba Cloud, but the entire Alibaba Group.
- Second, Alibaba Cloud is also the foundation through which Alibaba serves the real economy and will continue to drive physical-digital integration.
- Third, we believe this is a critical period for technological breakthrough and development in this nexus of cloud computing and AI.

As one of the leading cloud computing service providers globally, we strongly believe in the vast potential of industrial digitalization and the role of cloud computing as infrastructure to the digital economy.

Going forward, we will focus on a few areas to reinforce and strengthen our market leadership position as we look at the opportunities ahead.

- First, **enhance the stability and security of our cloud computing services** while continuing to optimize performance and manage costs through technology advancements.

- Second, **continue to build a dynamic developer and industry ecosystem** for cloud computing.
- Third, **collaborate with partners to provide intelligence-based industry solutions** to our customers in different industries and sectors.
- Fourth, **continue to push forward a holistic cloud-based service product that integrates DingTalk**, our intelligent online workplace collaboration platform and application development platform.
- Lastly, in this exciting era of disruptive breakthroughs initiated by generative AI, computing power is essential. On the one hand, we will continue building our large-scale pre-training models. We are also ready to capture the market opportunities to provide the computing power requirements for the various generative AI models and its applications.

This year marks Alibaba Group's 24^{th} year, and, in Chinese traditional culture, this means we have gone through two complete calendar cycles. We captured two historical opportunities of e-commerce in China for the consumer internet, and the start of cloud computing in China for the industrial internet. We will continue to capture the vast opportunities ahead through the impact of technology on commerce and other facets of our society and environment. Although there are many uncertainties in the journey ahead that are very difficult to evaluate, we remain highly confident in the future of Alibaba and China's development.

Thank you everyone. Let me pass the microphone to Toby who will share our financial results.

Financial Highlights

Toby Xu

CFO, Alibaba Group

(Original)

Thank you, Daniel. Let me start with financial highlights for the quarter. This quarter, our total revenue was RMB248 billion, an increase of 2% year-over-year. Income from operations was RMB35 billion, an increase of RMB28 billion year-over-year, mainly driven by a RMB22.4 billion decrease in impairment of goodwill in relation to Digital media and entertainment segment and a RMB7.2billion increase in adjusted EBITA.

During December quarter, we have continued to improve operating performance of our loss-making businesses by enhancing operating efficiency and optimizing costs that resulted in 16% year-over-year increase in adjusted EBITA to RMB52 billion. Overall adjusted EBITA margin improved by 3 percentage points to 21%.

Now let’s look at cost trends as a percentage of revenue excluding SBC. Cost of revenue ratio remained stable year over year at 60% in December quarter. Our direct sales businesses and logistics services continued to grow, driving up our cost of inventory and logistics, but we were able to keep our cost of revenue ratio stable primarily through optimizing content cost, traffic acquisition and improving operation efficiency.

Product development expenses ratio remained stable during the quarter. Sales and Marketing expenses ratio decreased 3 percentage points year-over-year to 12% in December quarter, reflecting our continued efforts in optimizing user acquisition and user retention spending across businesses. General and administrative expenses ratio remained stable at 3% in December quarter.

Non-GAAP net income was RMB49.9 billion, an increase of RMB5.3 billion or 12% year-over-year, mainly due to increase in adjusted EBITA, partly offset by decrease in equity pickup of our equity method investees’ results.

Our GAAP net income was RMB45.7 billion, an increase of RMB26.5 billion year-over-year, primarily due to the increase in Non-GAAP net income and the RMB22.4 billion decrease in goodwill impairment mentioned earlier.

As of December 31, 2022, we continue to maintain a strong net cash position of 379 billion RMB or 55 billion USD.

Our strong net cash position is supported by healthy cash flow generation. In December 2022 quarter, cash from operating activities was RMB87 billion and free cash flow were RMB82 billion, respectively, which were up by RMB7 billion and RMB10 billion versus a year ago. Majority of the difference between operating cash flow and free cash flow is operating CAPEX at RMB5.8 billion, down by RMB3.5billion versus a year ago.

Net cash inflow from investment and acquisition activities, including disposals, was RMB1.9 billion, compared to an outflow of RMB4.7 billion in the same period last year.

Importantly, we have continued to enhance returns to shareholders through share repurchases given our strong balance sheet and free cash flow generation capability. During the quarter, we repurchased approximately 45.4 million of our ADSs for approximately 3.3 billion USD under our share repurchase program.

Now, let’s look at our segment results.

Revenue from China commerce segment in December quarter was RMB170 billion, a decrease of 1% year-over-year.

Customer management revenue decreased by 9% year-over-year to RMB91.3 billion. Taobao and Tmall online physical goods paid GMV declined by mid-single-digit. Customer management revenue declined a few percentage points further versus paid GMV mainly due to higher order cancellation rate, as a result of supply chain and logistics disruptions caused by Covid-related impacts.

Direct sales and others revenue grew 10% to RMB74 billion, primarily driven by strong growth of our Freshippo and Alibaba Health’s direct sales businesses.

China Commerce Segment Adjusted EBITA increased by RMB749 million to RMB58.6 billion in December quarter. Segment EBITA margin remained stable at 34%. This reflected significant loss reductions from Taobao Deals, Freshippo and Taocaicai, partly offset by decrease in profit from customer management services.

Our International commerce segment revenue in December quarter was RMB19.5 billion, an increase of 18% year-over-year.

Revenue from International commerce retail business increased by 26% to RMB14.6 billion. The increase was primarily driven by accelerated revenue growth of Trendyol, as a result of its strong order growth and more efficient use of subsidies. Lazada and Aliexpress also saw recovered revenue growth this quarter. Revenue from our Alibaba.com wholesale business remained stable year-over-year.

International Commerce Segment Adjusted EBITA loss narrowed by RMB2.2 billion to RMB763 million in December quarter. The loss reduction year-over-year was primarily contributed by the reduced losses from Trendyol and Lazada. Trendyol continues to generate strong revenue growth and has enhanced operating efficiency. Continued narrowing of losses from Lazada was a result of ongoing improvement in monetization rate by offering more value-added services as well as enhanced operating efficiency.

Our Local consumer services segment revenue in December quarter grew 6% to RMB13 billion, primarily due to positive GMV growth of “To-Home” business driven by higher average order value of Ele.me.

Local Consumer Services Adjusted EBITA loss reduced by RMB1.9 billion year-over-year to RMB3.1 billion. Most of the loss reduction was driven by Ele.me business, while other major businesses within the segment also recorded reduced losses.

Ele.me continued to improve its unit economics per order by increasing average order value, reducing delivery cost per order. Its UE continued to improve year-over-year and remained positive this quarter.

Revenue from Cainiao, after inter-segment elimination, grew 27% year-over-year to RMB16.6 billion, primarily contributed by the increase in revenue from domestic consumer logistics services as a result of service model upgrade since late 2021 to enhance consumer experience, as well as increase in revenue from international fulfillment solution services.

In December quarter, 72% of Cainiao's total revenue was generated from external customers. Cainiao recorded adjusted EBITA loss of RMB12 million in December quarter, loss reduced by RMB80 million year-over-year.

Revenue from our Cloud segment, after inter-segment elimination, was RMB20.2 billion in December quarter, an increase of 3% mainly driven by healthy double-digit public cloud growth, partially offset by declining hybrid cloud revenue as we continue to drive high-quality, recurring revenue growth.

Revenue growth from non-Internet industries was 9% and contributed 53% of overall Cloud revenue. The non-Internet revenue growth was mainly driven by solid growth of financial services, education, and automobile industries, which was partially offset by the decline in public services industry.

Revenue from customers in the Internet industry declined by 4%, mainly driven by declining revenue from the top Internet customer that has gradually stopped using our overseas cloud services for its international business. On the other hand, we saw improving demands from Internet customers in the December quarter.

Adjusted EBITA of Cloud segment, which comprised of Alibaba Cloud and DingTalk, was a profit of RMB356 million in December quarter, increased by RMB222 million year-over-year.

Revenue from our Digital media and entertainment segment in December quarter was RMB7.6 billion, a decrease of 6% primarily due to the decrease in revenue from Alibaba Pictures.

Adjusted EBITA was a loss of RMB25 million, reduced by RMB1.3 billion year-over-year, primarily due to the narrowing of loss from Youku driven by disciplined investment in content and production capability.

Let me wrap up with some final thoughts.

Our December earnings results continued to demonstrate our ability to execute and achieve the key operating and financial objectives we've set since the beginning of fiscal year. Despite another quarter of global macro and COVID uncertainties that weighed on our revenue growth, we have:

- Continued to focus on higher quality growth supported by consumers and customer centric initiatives;
- Improved operating efficiency and cost structure throughout the organization;
- Enhanced shareholders return through ongoing share repurchases.

Consistency and persistence were key factors to our success in delivering these results in a challenging 2022.

As Daniel mentioned, we believe 2023 will be a year of "progress" for Alibaba. It is expected that China's economic activities will recover in 2023, which would catalyze and stimulate a gradual consumption recovery. In 2022, we have strengthened our operational and financial capabilities. We are confident that these enhancements would position us well to benefit from China's recovery.

We exited 2022 with a strong financial position of USD55 billion in net cash, allowing us the financial flexibility to grow our businesses and improve returns for key stakeholders including shareholders. In 2023, we intend to increase investments in major businesses that improve their competitive position and growth prospects while maintaining our mindset of enhanced operating efficiency.

Thank you. Now let's turn to Q&A.

Q&A

Rob Lin:

(Original)

Hi, everyone. For today's call, you are welcome to ask questions in Chinese or English. A third-party translator will provide consecutive interpretation for the Q&A session and our management will address your question in the language you ask. Please note that the translation is for convenience purpose only. In the case of any discrepancy, our management statement in the original language will prevail. If you are unable to hear the Chinese translation, bilingual transcripts of this call will be available on our website within one week after the meeting.

Alex Yao (JP Morgan):

(Translation)

Thank you, management, for taking my questions. I'd like to ask a question about the long term, and then a question about the short term.

First, on the long term. As Daniel said, it's been 24 years since Alibaba was established, marking the completion of two full cycles, as we say in Chinese. Over these two decades plus, Alibaba has led the development of digitalized commerce, digitalized logistics, and digitalized big data and computing.

Over the next three to five years, which areas of digitalization does Alibaba plan to be deeply involved in? As you said, over the past 24 years Alibaba has captured two major opportunities: e-commerce and cloud. Looking forward to the next three to five years, are there any areas or sectors where you see opportunities for big growth?

On to my short-term question, coming back to this year, we've seen new technology emerge, like ChatGPT, and we've also seen some changes in the competitive environment, such as JD's launch of a 10 billion yuan subsidy campaign. At this point in time, with opportunities and challenges existing side by side, how is Alibaba considering to further develop its core competitiveness? Will that involve further optimization of costs and driving of operational efficiencies? Thank you.

Daniel Zhang:

(Translation)

Thank you, Alex. I will take those questions one by one.

First, as we've said, our focus over the past 20-plus years has been on transforming commerce, logistics, and computing with digital technology. These areas directly correspond to Alibaba's three core strategies of consumption, cloud computing, and globalization --- globalization for us refers to the globalization of consumption and of cloud computing. Going forward, we will remain firmly committed to these three core strategies.

Why will Alibaba continue to focus on these three core strategies and not seek out new strategic arenas in which to compete? It's because we think that in these three areas the ceiling is high enough and the market is big enough. There will continue to be huge opportunities for us in each of them, especially as we continue to evolve our technology. Let me address each of them, one by one.

Let's start with consumption. Looking at the growth opportunity in China in terms of GDP, the IMF's projection for this year is a 5% growth rate. So you can imagine how large China's GDP will be a decade from now, if that can be sustained for ten years. And if GDP growth of 5% is to be maintained for ten years continuously, it's certain that the contribution of consumption to GDP will grow larger and larger. Total retail sales today are RMB40+ trillion, compared to GDP of RMB110+ trillion. That ratio will certainly grow even larger in the coming years.

At the same time, as technology evolves, it will create even more opportunities for digital commerce. E-commerce ten years ago was completely different from 20 years ago, and today is completely different from ten years ago. A few years back, we said that all commerce would become digital, and post-pandemic that has become a reality. Looking to the future, the application of a new generation of technology, including generative AI, which you mentioned, will certainly will also be transformative and create new digital formats and user experiences in consumption. It will be transformative not only on the consumer side, but also for supply chains. The profound impact of digitalization and data intelligence on supply chains is just beginning.

When it comes to cloud computing, this is an industry where China is really just getting started, compared to the US. IT spending as a proportion of GDP is just 1% in China, but 5% in the US. And cloud accounts for just 15% of IT spending in China, versus 21% in the US. These are figures from IDC. Just looking at these two sets of numbers, you can see the immense opportunity that exists in China. Of course, as technology continues to develop and new cutting-edge technologies come to the fore, like generative AI, which we just touched on, but also VR, virtual reality, which we've discussed previously, all of these technologies are going to require massive computing power. So we can expect to see exponential growth in demand for computing power.

For Alibaba as a globally leading cloud vendor, this story is really just getting started. And these two themes for the future --- consumption and computing --- are trends not just in China but globally. In both of these arenas, consumption and computing, we are the leader in China and one of the top players globally, and have great confidence in the future. Going forward, we will remain firmly committed to our three core strategies and will pursue them unswervingly. We will continue to embrace cutting-edge new technologies and leverage them to create new and more exciting prospects for the future.

Moving on to your second question about new technologies and recent developments in the market. Of course, there are always new developments in the market on a daily basis. In 2023, Alibaba has chosen “progress” as our overarching theme for the year. We’ll be pursuing progress in technology, in commerce, and also in the ways that we create value for our users.

We will be investing to drive progress in new areas of technology and to integrate new technologies into commerce in innovative ways that create new value. We will harness technology to create new formats of commerce and open up new horizons for the future, as we have always done. Over the past two decades plus, Alibaba has done precisely that. Alibaba did not win its leading position in the market by relying on low prices and subsidies and engaging in low-level competition. Rather, we’ve always invested in technology, in the belief that innovation can make technology that had been impossible become possible. And in turn, technological innovation can make commerce that had been impossible also become possible. So, we will continue, as always, to drive new breakthroughs in technology so as to open up new frontiers in commerce and new possibilities for the future.

Ronald Keung (Goldman Sachs):

(Translation)

Thank you, management. We know that in 2022, a major theme for Alibaba was optimizing cost structure and driving operational efficiencies. In 2023, with macroeconomic recovery, are you expecting to see a return to positive GMV growth? When do you expect to see that recovery in terms of GMV or CMR growth turning positive again? And in the current environment, how will you be balancing growth and investment this year? Because we know that some of your peers are engaging in subsidy campaigns in the market. What’s your view on GMV recovery in 2023 and on investment plans for the year? Thanks.

Daniel Zhang:

(Translation)

Like all of you, we have been closely following changes in consumption behaviour following the end of COVID restrictions in China. In my prepared remarks, I already painted as detailed a picture as possible. Overall, January was still challenging through to the Spring Festival, with the ongoing impact of the pandemic and large numbers of people travelling across the country. After the Spring Festival, and in particular after the Lantern Festival, life and work returned to normal and we saw a noticeable improvement in consumer sentiment, as expressed in proactive consumption behaviour.

We also observed changes in different categories, as I mentioned earlier, such as apparel, sports, outdoor, as well as health and wellness products, which continued to be very popular.

On the merchant side, we see a strong desire to get back to business. All merchants, indeed all businesses in China, want to go all out in 2023, not just to get back on track but to try to make up for all they missed out on over the past three years. Everyone, I think, shares that hope. So we are seeing an increase in merchant enthusiasm. Of course, it's only been a short time, just over half a month, since we started seeing these changes, and we do need to keep our eyes on how the picture continues to develop. But overall, we are optimistic about recovery this year and positive momentum in consumption.

The other part of your question had to do with market competition and price subsidies in particular. Price subsidies are nothing new. From time to time, there will always be somebody that decides to subsidize prices to try to win a first-mover advantage or try to turn around their business. If you take a clear-eyed look at history, you'll see that nobody has ever managed to turn around their business or achieve major business breakthroughs by relying on sustained price subsidies. The only way to achieve that, really, is innovation --- technology innovation and business model innovation --- that makes merchants willing to offer consumers the best products at the best prices. No-one can subsidize an entire marketplace. Only when the merchants themselves are motivated and willing to pick up the bill, because they can achieve long-term sustainable returns, can you create a positive loop.

Alibaba has a lot of experience in this regard, which we will fully leverage going forward. Price is definitely an important part of the consumer experience, but it's also about how we make the best use of marketplace mechanisms, our market resources, as well as our "deep pockets". As Toby said in his prepared remarks, we have USD55 billion in net cash. But it's not a question of money. It's a question of commercial and technological capabilities. We aim to leverage these capabilities to create value for our users and maintain our leadership position in the market. Thank you.

Eddie Leung (Bank of America Merrill Lynch):

(Translation)

Good evening. My question has to do with local services. We understand that Ele.me's unit economics (UE) have continued to be positive. But we also know that various short-form video platforms are now also investing heavily in local services --- and we have previously seen various short-form video platforms reshape the competitive landscape in e-commerce. Alibaba has so far been one of the larger leading players in local services, but I'm wondering if you could share with us what potential strategies or approaches you might adopt to better address this new competition?

Daniel Zhang:

(Translation)

We broadly look at local services as falling into two categories: "to-home", and "to-store" (or "to-destination", because a store is one kind of destination).

Our view is very clear. When it comes to to-destination, any media platform, including short-form video platforms, can play a role in promoting a destination, a shop, or a physical location where services are offered. They can do that by offering coupons for purchase, allowing consumers to place an order or to make an appointment in advance. But in essence, what they are providing is media ads. The only difference is that within that ad, you can place an order. But at the end of the day, no matter what kind of order you place on a short-form video platform, to have that order fulfilled you are going to have to go physically to the store. So in essence, the business they are in is an advertising business. To that extent, any media platform that has users and has influence can find opportunities in the to-store business.

But Alibaba has opened up a whole new paradigm in our to-destination business with the successful transformation of Amap that I mentioned earlier. Over the past few years, Amap has evolved from a mere map tool into a complete to-destination services platform that spans map-based search, discovery, transaction, and fulfillment. Amap has already achieved strong user engagement and high penetration in a whole range of categories from ride hailing through to hotel reservations and on to gas stations, charging stations for new energy vehicles, and other automobile-related categories. So we are developing this to-destination business in our own, unique way. It would be difficult for any other kind of media platform to do that.

The other part of local services is to-home. Ele.me, which you mentioned in your question, is part of our to-home offering. Thanks to several years of hard work, Ele.me today is very much on the right track. Unit economics are positive and continue to improve. And beyond that, order volumes, user numbers, and user stickiness are also improving.

We see the to-home business as neighbourhood e-commerce, within which to-home delivery of restaurant meals is one category. Other categories include to-home delivery of medicines, fast-moving consumer goods, and groceries.

To make this work, you need the capability to match neighbourhood-level supply, neighbourhood-level demand, and neighbourhood-level fulfillment capabilities, in real time. That kind of capability is beyond the reach of a pure media platform.

For Ele.me or for any player that aspires to succeed in the to-home space, what's critical is that ability to integrate, in real time, local supply, local demand, and local fulfillment. You need to make those three things intersect at a single coordinate in space and time --- the space being the neighbourhood, the time being the required delivery time --- in order to achieve chemical synergy. That would be very difficult for a pure-play media platform. And that's why we have tremendous confidence.

We continue to grow our local services business successfully in the priority cities we've chosen. Because of the local nature of this business, going after 50 cities versus 100 cities would be two completely different propositions. We continue to focus on the key cities that we've selected, and we continue to improve the service to win the trust of consumers and drive long-term growth.

Jiong Shao (Barclays):

(Translation)

Thank you, management, for taking my question.

Toby, you shared with us that free cash flow in the past quarter exceeded USD11 billion, and we note that Alibaba has also been divesting and monetizing certain investments, such as Paytm in India. And in the last quarter you conducted USD3.3 billion of share buybacks. I'm wondering what other methods could potentially be available for Alibaba to increase shareholder value and return? For example, are you considering distributing dividends or further expanding the share buyback programme?

Toby Xu:

(Translation)

Thank you for your question.

You touched on a couple of things. First, as you will have seen from various media reports, we have been divesting some of our investments. I think that's normal for any corporate. Any company that's making a lot of strategic investments is also at some point going to make a timely exit from those investments. That's part of the original plan; when you make those kinds of strategic investments you are planning on exiting at a certain point.

You also asked about our share buyback program. In fact, as we shared in the previous quarter, that program has already been upsized. It had been a USD25 billion program that was subsequently increased by USD15 billion, taking its scale to USD40 billion. In the December quarter, we bought back around USD3.3 billion of shares. And we do think that pursuing the share buyback program is a good way to return value to our shareholders.

Now, under the existing, already enlarged share buyback program, we still have a remaining quota of USD21 billion that can be deployed. At this point, our priority is not further expanding that quota. Rather, we're looking at how we can best make use of that remaining quota of USD21 billion, how to deploy it and when to deploy it, in line with the authorization given to us by the board of directors.

Alicia Yap (Citigroup):

(Translation)

Thank you, management, for taking my question.

I'd like to follow up on Daniel's earlier remark about how Alibaba intends to focus on and invest in technological innovation so as to create new business models. Daniel, could you please quantify that a bit? For example, in which of the businesses can we expect to see improvements this year? And will that result in accelerated CMR growth, or allow the cloud business to acquire higher-value customers and significantly boost cloud revenue, or will it perhaps be in local services where technology will drive growth? I'd appreciate it if Daniel could give us some more colour on which businesses will benefit from these new technologies and new business models?

Daniel Zhang:

(Translation)

Driving business growth with technology has been an ongoing, constant theme for Alibaba throughout its history. Looking to the future, we see several big opportunities.

The first is around artificial intelligence (AI). Lately, generative AI has become a hot topic all over the world. But we're not talking about having a chatbot for the sake of a chatbot. Rather, we're talking about integrating AI into various scenarios across our businesses. We believe that AI, broadly defined, can play an instrumental role in enhancing consumption, user experience, content generation and understanding, and advertising effectiveness. These are key areas that we have been investing in.

AI can be widely applied to help match supply and demand more effectively, to help merchants achieve higher marketing effectiveness, and to enhance service efficiency and user experience on our platform for both merchants and consumers.

Cloud is another of our key strategies. Alibaba Cloud has developed a broad array of IaaS and PaaS offerings for cloud computing and big data, enabling enhanced data processing capabilities. Building on our big data platforms, we are actively developing large pre-training models. In all these areas, we are happy to see that the view we took on the future has proven to be consistent with the big trends now underway globally. And going forward, there's going to be exponential growth in demand for processing power to support these cloud computing and big data applications. That is also a big opportunity for us.

Another word about AI, because an implicit part of your question had to do with advertising effectiveness and platform efficiency. AI can also be leveraged in in logistics and supply chains. For example, in local services, which we discussed earlier, AI can be applied to better match local demand with local fulfillment capabilities and local supply within a certain time window, to optimise dispatch. These are brand new applications of AI that we are working hard on building and aim to translate into brand new business capabilities.

Jerry Liu (UBS):

(Translation)

I have two questions. The first is on take rates, i.e. on the growth rate of GMV on Taobao and Tmall relative to CMR. Over the past two quarters, CMR growth has lagged GMV growth due to order returns. With the recent recovery in consumption, will we see any change in the relative growth rates of GMV and CMR in this quarter or the next few quarters? Could it be possible for CMR to grow faster than GMV?

Secondly, Daniel has assumed the position of acting president of Alibaba Cloud. Since taking up that role, have you made any adjustments to the long-term or short-term strategies of the cloud business, or its operating priorities? Thank you.

Toby Xu:

(Translation)

Thanks for your questions. I'll take the first one, then hand over to Daniel to answer the second one.

The first question had to do with the relationship between CMR growth and GMV growth. As we previously disclosed, the difference between the two has mainly been caused by a relatively high rate of order returns. Let me briefly explain.

The GMV figures that we disclose are for paid GMV. But after paying for a purchase, consumers may return their order, for example when logistics disruptions affect delivery. When there are serious logistics disruptions and a higher order return rate, the increase or decrease in the GMV of returned orders will be larger than that of paid GMV, in year-on-year terms[1].

As Daniel said in his prepared remarks, logistics has recently recovered, which should result in lower order return rates. Certainly that is the trend that we are starting to see, with the gap between paid GMV growth and CMR growth narrowing.

That's my answer to your first question, in terms of the recent trend that we are seeing. For your second question, I will hand over to Daniel.

Daniel Zhang:

(Translation)

Let me address your second question.

[1] The sentence refers to that when there are serious logistics disruptions and a higher order return rate, the year-over-year growth rate of completed GMV will be slower than the year-over-year growth rate of paid GMV.

The development of the cloud industry is a historic opportunity, not only in China but worldwide. This is an opportunity of extreme strategic importance to Alibaba. For these two reasons, I have taken on the role of acting president of Alibaba Cloud. This is something I am extremely passionate about. We must not fail to seize this historic opportunity.

We have an excellent foundation in Alibaba Cloud today, thanks to the hard work of the previous presidents of this business unit over the past decade plus. We’re now number one in China, and are recognized as among the top cloud vendors worldwide. So our position in the market is excellent and we have a solid foundation to build on.

Going forward, I think the first thing we need to do is get back, if you'd like, to the fundamentals of cloud. Cloud is fundamentally about providing digital infrastructure and computing power to customers, and we need to ensure that we're doing that with consistently high availability, high security, and high stability, achieving performance standards that satisfy and even exceed customer expectations. This is the most fundamental and crucial requirement.

Second, we need to place emphasis on developing public cloud offerings. When we talk about cloud, especially in the China market, it's not often clear that we're all talking about the same thing. As I’ve often pointed out, there are many different definitions of cloud out there. What is cloud computing, really? For Alibaba, we need to be firmly rooted in China, but also have a global vision and hold ourselves to the highest global standards. We need to constantly pursue technological breakthroughs in core capabilities around IaaS and PaaS, to ensure that we are the leader in China and even globally in terms of both performance and cost.

Cloud is a business that requires economies of scale. If you don’t have the scale, then you can’t achieve economy. But where does that economy come from? From the dividends of technology. So I see technological breakthroughs as key. That’s the only way to get customers to truly adopt cloud, to make the best use of cloud, and to achieve significant economic benefit from cloud.

Third, we need to be paying a lot of attention to developing public cloud offerings. Public cloud is where economies of scale lie. And a key thing we need to be working on is better integrating cloud, edge, and terminal to serve the development of the industrial Internet. We also need to seize opportunities in newly emerging data-intensive sectors.

Finally, there is an endless stream of hot industry trends and new technologies. We’ve already touched on this quite a few times, so I won’t repeat myself, but with the advent of generative AI, we can expect to see rapid growth in demand for high-performance computing power. You can’t deploy and operate any large model without that underlying computing power. And that computing power in turn relies on network, chips, deployment, solutions, which all need to be integrated. Today, all the other global vendors are talking about this as well.

We at Alibaba see this as an extremely important opportunity and we aim to translate it into real demand for computing power.

Rob Lin:

(Original)

Thank you everyone for your time listening in today. That concludes today's earnings call. The replay and the transcript will be available on our IR website within one week. We look forward to meeting you and engaging with you in the coming months, and look forward to speaking with you next quarter. Thank you.

[END OF TRANSCRIPT]