Alibaba Group

June Quarter 2023 Results

Conference Call

Transcript

Thursday, 10 August 2023

Introduction

Rob Lin

Head of Investor Relations, Alibaba Group

(Original)

Thank you. Good day, everyone. Welcome to Alibaba Group's June Quarter 2023 Results Conference Call. With us are Daniel Zhang, Chairman and CEO; Joe Tsai, Executive Vice Chairman; Toby Xu, Chief Financial Officer. We have also invited Trudy Dai, the CEO of Taobao and Tmall Group to join the call. 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 Harbor. Today's discussion may contain forward-looking statements, including without limitation statements about the outlook of our businesses and our reorganization. Forward-looking statements involve inherent risks 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 20-F and other documents filed with the U.S. Securities and Exchange Commission 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 to Daniel.

Group Overview

Daniel Zhang

Chairman and CEO, Alibaba Group & Chairman and CEO, Cloud Intelligence Group

(Original)

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

We started the fiscal year with a robust quarter. The latest macro data indicates some uncertainties in the pace of post-covid recovery, but as economic and consumer activities continue to resume, our businesses demonstrated encouraging trends that reflect the economy's resilience, confidence in a consumption recovery, and the significant potential from an integrated development of the digital economy and the real economy. The solid quarter also showed promising early results of our reorganization, which is beginning to unleash new energy across our businesses. Our revenue reached RMB234 billion, grew at 14% year-over-year, and growth was achieved across our different business segments. Our adjusted EBITA increased 32% year-over-year to RMB45.4 billion, showing progress in our continued focus on operating efficiency and quality of operation. Next, I will go through the results of each of our major businesses. First, let me invite Trudy to share the Taobao and Tmall Group updates.

Taobao and Tmall Group Business Update

Trudy Dai

Director and CEO, Taobao and Tmall Group

(Translation)

Good evening, everyone. This is Trudy and it is my pleasure to speak with you all again.

In the just-concluded June quarter, under our "putting users first" strategy, the Taobao app's user base has been put on a rapid growth track. From April of this fiscal year, the average number of DAUs on the Taobao app each month has grown by 6% or higher year-over-year. Last month, July, growth was over 7%. Based on third-party data, our DAU leadership in the e-commerce space continues to widen. More users are choosing to use the Taobao app.

At the same time, our "building a prosperous ecosystem" and "realizing technology-driven innovation" strategies are also starting to yield results. Since we launched the "value-for-money battle" this fiscal year, we've seen a very clear trend of merchant growth on Taobao and Tmall. In the June quarter, we onboarded a large number of new merchants, a significant portion of whom quickly started contributing to our value-for-money battle, winning over and converting users. So, our "value-for-money battle" will continue going forward and will remain an area of major investment. We need to give users the experience of "good merchandise is not expensive" on Taobao and Tmall, and we need to guide merchants to enhance the value-for-money in order to achieve business scale growth and long-term stable returns. In fact, we saw initial evidence of this in the June quarter: merchant confidence in doing business on our platform increased significantly, and merchant spending also grew, with an increase of over 20% in the daily average number of merchants paying for advertising. This all goes to show that more merchants are taking Taobao and Tmall as their first-choice platform for the stable operation of long-term business.

As for "realizing technology-driven innovation", we have already upgraded merchant tools with AI, enabling merchants to open stores, launch new products, operate their businesses, and conduct marketing campaigns with much greater efficiency, and helping to optimize store display and product descriptions, and thereby significantly enhancing the shopping experience for users.

As a result of these three strategies, the Taobao and Tmall Group recorded close to RMB 80 billion in CMR this quarter, a year-over-year increase of 10%. Within that, we saw very strong willingness to invest among merchants coming to Taobao and Tmall from other platforms. As for the platform itself, the Taobao and Tmall Group remains committed to growing revenues while reducing costs and raising efficiency. We will spend where it makes sense to, and will save where we can. As a result, despite our huge investments in users, in the "value-for-money battle", and in AI, the Taobao and Tmall Group recorded a 9.1% year-over-year increase in adjusted EBITA in the June quarter, slightly lower than CMR growth.

Also, during the just-concluded 6.18 Taobao and Tmall Shopping Festival, we achieved a two-wheel drive effect of "user scale" and "purchasing power". The data show that within the two factors that drove GMV growth during 6.18, growth in the number of paid orders and in the average ticket size was remarkably similar. In other words, the contribution of each of those two factors was highly balanced. On the one hand, the number of 88vip members and GMV both grew by double digits year-over-year; and on the other hand, as part of our "value-for-money battle", during this year's 6.18 we launched a Taobao Good Price Festival, marking the first time in the history of 6.18 that there was a dedicated promotion channel for Taobao merchants. This Taobao Good Price Festival proved effective in promoting value-for-money offerings and attracting more users from lower-tier cities and young users to visit and make purchases.

So, if I were to sum up the June quarter in one sentence, I would say: "Our three strategies of putting users first, building a prosperous ecosystem, and realizing technology-driven innovation are starting to yield results". Throughout the remainder of the fiscal year, we will continue to implement these three strategies. Specifically:

First, we will do our utmost to meet the needs of diverse groups of Chinese consumers, and to satisfy their demands around shopping, consumption, and daily life. To do that, we will continue to invest heavily in developing content around shopping, consumption, and daily life.

Second, we will also continue to invest heavily in the "value-for-money battle", in two different ways. On the one hand, we will continue, in line with our mission, to support small and medium merchants with targeted programs such as those for merchants in industrial clusters and for new SME merchants. And in parallel, we will build a more advanced, open, and inclusive merchant ecosystem and will attract more merchants to engage in the "value-for-money battle", so as to create a virtuous cycle on Taobao and Tmall of "merchant ecosystem – revenue growth – stronger profitability". And that is precisely what our mission has always been.

Third, we will continue to invest in AI. It is our conviction that technology creates commercial value: Taobao and Tmall have the largest collection of merchants and of merchandise on the Internet, and are the most fertile soil anywhere on the Internet to explore AI applications. Hence, in this technological revolution, the Taobao app has the greatest potential to become a "one-stop smart portal for life and consumption, enabled by AI", satisfying the broadest variety of diverse needs across our huge base of 1 billion users.

At Alibaba, we often say "seeing is believing". As the CEO of the Taobao and Tmall Group, I am confident that over this three-year management cycle, through the execution of our three key strategies, the Taobao and Tmall Group will create a virtuous investment cycle. This cycle begins with investment in users, leading to user growth, which in turn leads to merchant growth, which leads to transaction growth, and ultimately leads to revenue and profit growth. This growth allows us to reinvest in users and further promote user growth. Along the way, even though there may be occasional months where our business fluctuates, under the leadership of the Taobao and Tmall Group's board of directors and management team, we will remain firmly committed to our three key strategies, to continuing to invest in users, providing strong support for merchants, and upgrading our platform with technology for the long term. And we are fully confident in the results we will achieve. Thank you.

Group Overview

Daniel Zhang

Chairman and CEO, Alibaba Group & Chairman and CEO, Cloud Intelligence Group

(Original)

Thank you, Trudy. Now I will share the updates on our other major businesses.

Alibaba International Digital Commerce Group ("AIDC") delivered 41% overall revenue growth this quarter, and its retail businesses achieved 60% revenue growth year-over-year. This was driven by solid order growth of our international retail marketplaces at around 25% year-over-year, advertising revenue growth because of enhanced monetization and higher direct sales revenue contribution as AliExpress expands its new "Choice" model. Lazada also delivered rapid order growth based on its differentiated country strategy, accelerating progress in high-priority markets such as the Philippines and Thailand. In Türkiye, Trendyol continued to maintain its growth momentum and market leadership. We are starting to see economies of scale in our international retail businesses, as enhancing monetization and operating efficiency reduced adjusted EBITA loss. AIDC's adjusted EBITA loss decreased by 70% year-over-year during the quarter. Looking ahead, we will continue to expand the "Choice" model leveraging the capabilities of an integrated cross-border supply chain and enhanced consumer experience with higher certainty in logistics and service level. The plan is to expand the "Choice" model from AliExpress to certain of our other retail platforms, while upgrading our product and services, especially in providing a better localized experience.

During the quarter, revenue from Local Services Group grew 30% year-over-year, driven by strong combined order growth across both Ele.me and Amap. Amap's daily active users and "to-destination" services expanded due to the strong recovery in commuting and travel demand after the pandemic measures were lifted. With a long-term strategic focus on technology leadership, Amap released new product features such as traffic light countdown and tunnel navigation during the quarter, which were well received by its users. Its market share in map navigation services continued to expand. During the quarter, Ele.me focused on investing in its own service capability enhancement and a more inclusive partnership strategy, which helped sustain healthy order growth while maintaining positive unit economics.

Cainiao Smart Logistics Network Limited's revenue during the quarter grew 34% year-over-year, primarily driven by the volume increase of international fulfillment solution services (mainly serving AliExpress) and China domestic consumer logistics services. Cainiao's adjusted EBITA of the quarter was RMB877 million due to the continued focus on quality of operation and lower transportation costs as international air cargo prices came down. Looking ahead, Cainiao will continue to invest in building logistics networks for cross-border and domestic parcels, and leveraging Alibaba's multiple digital commerce use cases to expand its network effect. Cainiao will also share part of the savings from its operating efficiency improvement and transportation cost reduction with its customers through price strategy adjustments, and pursue higher economies of scale on a larger revenue base.

During this quarter, Alibaba Cloud's revenue grew 4% year-over-year. The growth rate was negatively impacted by the normalization of CDN demand, as usage of video streaming, remote working and remote learning came down when offline activities resumed after pandemic measures were lifted. The growth rate was also partly impacted by revenue decline from a top customer. In the past quarter, we have received strong demand for model training and related AI services on cloud infrastructure, which were only partially fulfilled due to the near-term supply chain constraints globally. We believe the growth opportunities driven by AI services have just begun.

We believe that the technology evolution brought by AI is not a short-term opportunity but the beginning of a new era. As one of the world's leading cloud service providers, we will continue to invest in forming a full-stack product and technology leadership across IAAS, PAAS and MAAS layers. This is key for us in capturing AI opportunities and sets a differentiating advantage for AliCloud vs. other players in China, which mainly focus on one of the layers.

We will leverage and expand this advantage when serving the needs of our customers, including the training and service needs of large language model startups, as well as industry demands for customized models and vertical models. We believe the high-performance and low-cost computing power required for model training and services will open up brand-new opportunities for cloud computing services. Over the long term, Alibaba Cloud will benefit from the application of AI in all industries. In the MaaS layer, we have built ModelScope, a leading open-source online community in China for models and related tools & services, which is very popular among developers. The community hosted over 1,000 AI models, including Meta's recently released Llama2 and our own open-source model, the seven billion-parameter version of Tongyi Qianwen. We believe the aggregation and engagement of a model ecosystem will significantly help developers optimize their models and use services on Alibaba Cloud. Since April, we released our own large language model Tongyi Qianwen, Audio-to-text transcription platform Tongyi Tingwu, and text-to-image model Tongyi Wanxiang, which together have accumulated millions of users.

In this quarter, Alibaba Cloud's adjusted EBITA reached RMB387 million, representing year-over-year growth of 106%. This was mainly due to reduced colocation and bandwidth costs of DingTalk as a result of normalized usage after the pandemic, as well as enhanced product mix and efficiency improvement (for example, server utilization) in our cloud business. We will continue to focus on the quality of operations. And as we continue to scale up, we will work to achieve economies of scale that will deliver long-term operating benefits and contribute to our profitability.

Our Digital Media and Entertainment Group ("DME") delivered 36% revenue growth year-over-year, and the first-ever quarter of profitability. This was a result of the following factors: 1) Youku's growth in subscription revenue 2) higher revenue contribution from Damai and Taopiaopiao, which both benefited from the recovery of offline shows and cinemas after the pandemic 3) Alibaba Pictures' launch of several blockbusters and robust China box office demands during the quarter. Going forward, we will continue to improve our content production capabilities and enhance DME business' operating results through high-quality content creation and distribution.

In July, we published our FY2023 ESG Report. Over the past year, we have made progress across the seven strategic dimensions of social responsibility, especially in restoring our green planet. We achieved solid emission reduction under Scope 1, 2 and 3. We drove emission reduction across our business ecosystem, which was roughly equivalent to the total annual greenhouse gas emissions of one million average households in China. Leveraging our unique position connecting consumers and merchants, our product innovation Carbon88 ledger platform enables our consumers and merchants to join the carbon-saving efforts across our ecosystem.

Following the announcement of our 1+6+N reorganization in March, the six business groups have started operating in a new way under the leadership of their respective boards. The past quarter's solid performance was also a reflection of the early results of this change, and further enhanced our confidence towards the future. As part of the new governance framework, we are also further strengthening the company's capital management, moving ahead with our various programs to improve shareholder return under the leadership of the newly established Capital Management Committee. The capital market projects we announced last quarter are all underway and we have also been continuing share repurchase activities in the market. We will keep you updated on the progress in the future.

Lastly, this will be the 36th earnings call I have participated in since our IPO in 2014, and the final one as Chairman and CEO of Alibaba Group. It truly has been a privilege of a lifetime to lead this company as CEO on our three strategies of consumption, cloud computing and globalization since 2015, and be a part of Alibaba's high-growth period. As Chairman, it was an extraordinary experience to take on the challenges brought on by the pandemic and unprecedented changes in the macro environment over the past four years. This has been an invaluable life experience. I sincerely thank our shareholders and analysts for your trust and support over the years. This quarter is the culmination of my 8-year leadership of Alibaba and the start of my new journey. I hope you continue to support Joe, Eddie, and the new management team. As Cloud Intelligence Group moves towards becoming a public company, I look forward to re-engaging with everyone in my new role in the journey ahead.

Thank you, everyone! Now I will pass to Toby to go through the financial updates.

Financial Highlights

Toby Xu

CFO, Alibaba Group

(Original)

Thank you, Daniel. Due to the strong business momentum and our focus on operating efficiency across businesses, we achieved robust financial performance in the past quarter.

Total consolidated revenue was RMB234.2 billion, an increase of 14%. Consolidated adjusted EBITA increased by RMB11 billion or 32% to RMB45.4 billion in the quarter due to improvements across all business segments. Non-GAAP diluted earnings per share was RMB2.17, an increase of 48%.

Additionally, during the quarter, we repurchased USD3.1 billion worth of our shares, which accounted for 1.4% of total shares outstanding. This is supported by our continuous generation of strong free cash flow. During the quarter, free cash flow was RMB39.1 billion (or USD5.4 billion), an increase of 76% year-over-year. Our strong free cash flow and balance sheet continue to put us in an excellent position to strengthen our competitiveness and capture new opportunities.

Now let's look at cost trends as percentage of revenue excluding SBC. Cost of revenue ratio, excluding SBC, decreased 1 percentage point to 61% during this quarter. Product development expenses ratio decreased 1 percentage point to 4% during this quarter. Sales and Marketing expense ratio remained stable at 12% in this quarter. And General and administrative expenses ratio remained stable at 4% in this quarter.

Our net income was RMB33 billion, an increase of RMB 12.7 billion compared to the same quarter last year. The increase was primarily attributable to the increase in income from operations and the increase in share of results of equity method investees, partly offset by the net losses arising from the decreases in market prices of our equity investments in publicly traded companies, compared to net gains from these investments in the same quarter last year.

As of June 30, 2023, we continued to maintain a strong net cash position of RMB419.2billion or USD57.8billion. Free cash flow this quarter was RMB39.1 billion, an increase of 76%. The increase reflected an improvement on profitability and a decrease in capital expenditure.

Now let's look at the segment results.

Starting this quarter, we have implemented a new organizational and governance structure, under which we now have six major business groups and various other businesses.

Accordingly, our segment reporting has been updated to reflect our Reorganization. Under our updated segment reporting, segment revenue and adjusted EBITA are presented before consolidation adjustments.

We have also provided revenue and adjusted EBITA trend of each business groups for the last five consecutive quarters in the appendix of the earnings presentation for easy reference.

Now let's look at the Taobao and Tmall Group.

The "Users First Strategy" of Taobao Tmall Group is yielding positive user growth momentum and improving user retention on Taobao app, which have supported strong revenue growth and a successful 6.18 Shopping Festival during the quarter.

Revenue for Taobao and Tmall Group was RMB115 billion, an increase of 12%. Customer management revenue increased by 10% to RMB79.7 billion, primarily due to increase in number of paying merchants, increase in merchant's willingness to invest in advertising on our platform and increases in online physical goods GMV excluding unpaid order.

Direct sales and others revenue increased 21% to RMB30.2 billion, primarily due to strong sales driven by the consumer electronics category.

Taobao and Tmall Group adjusted EBITA increased by 9% to RMB49.3 billion. The increase was primarily due to the increase in profit from customer management service and narrowing losses in certain businesses, which was partially offset by Taobao and Tmall Group's investments in growing Taobao App users that has resulted in increasing DAU of 6.5%

Alibaba International Digital Commerce Group revenue was RMB22.1 billion, an increase of 41%. Revenue from International commerce retail business increased by 60% to RMB17.1 billion. The increase was primarily due to solid performance of all major retail platforms, and improvements in monetization. Revenue from our International commerce wholesale business remained stable at RMB5 billion compared the same quarter last year.

AIDC's adjusted EBITA loss narrowed by RMB960 million to a loss of RMB420 million in June quarter. Losses significantly narrowed year-over-year, primarily because of improved margins of Trendyol and Lazada, partly offset by the increase in investments in new businesses, such as Miravia and AliExpress Choice.

Trendyol continued to deliver strong order growth in both of its e-commerce and local consumer service businesses. Through robust revenue growth and continuing improvement in operating efficiency, for the first time, Trendyol achieved positive operating results during the quarter. The reduced loss from Lazada is primarily due to improvement in monetization.

Local Services Group revenue in June quarter grew 30% to RMB14.5 billion, primarily due to robust GMV growth of Ele.me and the rapid order growth of Amap.

Local Services Group adjusted EBITA was a loss of RMB2 billion this quarter, compared to a loss of RMB2.8 billion in the same quarter last year, reflecting the continued narrowing of losses driven by Ele.me's order growth and positive unit economics per order, as well as rapid order growth of Amap driven by market demand.

Total revenue from Cainiao Smart Logistics Network Limited grew 34% to RMB23.2 billion, primarily contributed by the increase in revenue from international fulfilment solution services and domestic consumer logistics services.

Cainiao adjusted EBITA was a profit of RMB877 million, compared to a loss of RMB185 million in the same quarter last year. Profitability turned positive year-over-year primarily because of improved operating results from international fulfilment solution services and domestic consumer logistics services.

Revenue from Cloud Intelligence Group was RMB25.1 billion in June quarter, an increase of 4%. The revenue growth was mainly driven by Alibaba-consolidated businesses and customers within financial services, education, electric power, and automobile industries, partly offset by our proactive efforts to manage revenue from project-based cloud services.

Cloud's adjusted EBITA was increased by 106% to RMB387 million, primarily due to reduced colocation and bandwidth costs of DingTalk as a result of normalization of usage as compared to the same quarter last year.

Revenue from our DME group was RMB5.4 billion, an increase of 36%, primarily driven by growth of online entertainment business, as well as a strong recovery of offline entertainment business.

Adjusted EBITA recorded a profit of RMB63 million, compared to a loss of RMB907 million. The improved adjusted EBITA was mainly due to the increase in revenue from Alibaba Pictures and Damai.

Revenue from All Others segment increased slightly by 1% to RMB45.5 billion, primarily due to the revenue growth contributed by Alibaba Health, Fliggy, Freshippo, and Intelligent Information Platform, partly offset by the decrease in revenue from Sun Art due to decrease in ticket size resulted from the decrease in consumer stockpiling behavior compared to the same quarter last year.

Adjusted EBITA from All Others segment was a loss of RMB1.2 billion compared to a loss of RMB2.3 billion in the same quarter last year, primarily due to improved operating results from Freshippo, Lingxi Games, and Fliggy.

Thank you, and that's the end of our prepared remarks. We can open up for 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. 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.

Ronald Keung (Goldman Sachs):

(Original)

Thank you. Thank you, Joe, Daniel, Toby, Trudy, and Rob. Can you share – can management share just how have broader consumption trends been tracking after a pretty strong June 18th shopping festival and following on that within the Taobao, Tmall Group besides the DAU DAC metrics that are KPIs, how are we thinking about the balance between Taobao, Tmall, for example, other metric such as market share versus our Taobao, Tmall Group, say absolute profit level if we think of it on a three-year horizon? Thank you.

Trudy Dai:

(Translation)

Thanks, and let me start with your first question about consumption trends. As we've seen, there is a gradual recovery underway in the Chinese economy, and the Chinese government has made many efforts to stimulate consumption.

On your other question about market share and profitability, I'd like to come back to the three key strategies we're pursuing: putting users first, building a prosperous ecosystem, and realizing technology-driven innovation. It is our conviction that growth in user scale will lead to merchant growth, creating a virtuous cycle. With more merchants growing their businesses, we will achieve higher revenues, allowing us to further reinvest in user scale and experience.

Looking to the future, there certainly will be uncertainties ahead of us. Faced with uncertainties and volatility, the greatest certainty we have is the need to continue to grow our user scale and our merchant scale. We are very optimistic that as long as we maintain our leadership in both user scale and merchant scale, our investments will translate into higher revenues and profits growth potential in the medium to long term.

Alicia Yap (Citigroup):

(Original)

Hi. Good evening, management. Thanks for taking my questions and thank you Daniel and all the best for your new journey.

(Translation)

Looking at the DAU growth figure of 6.5%, and the double-digit growth in 88 VIP members' spending, I'm wondering if management could give us more details on what lies behind those numbers. For example, where did new users come from this quarter? Are they mostly from lower tier cities? How do these new users compare with existing users in terms of their spending power and willingness to spend?

Also, what is driving the robust growth in 88 VIP members' spending? Is it more about their higher frequency of purchases, or is that they are purchasing big-ticket items in certain categories? Will this trend continue on into July?

Finally, I'd like to ask about your current goals. Given that the overall economy remains rather weak, how confident are you in your ability to achieve your goals in the current economic environment?

Trudy Dai:

(Translation)

Thank you. I'll start with your first question on the increase in DAUs and any changes we are seeing in the mix of new users.

What we are seeing is that our "value-for-money battle", and all our efforts to better serve users who demand more value for money, have very much been paying off.

At the last earnings call, we presented our three key strategies. There are several major factors underlying the robust performance that you've seen in the June quarter, which I will set out below.

First, improvement in the macroeconomic environment. Consumption is gradually recovering, and the penetration of online retail continues to increase.

Second, as a result of our value-for-money battle, we've built a platform that is bringing to market an increasing assortment of good merchandise at good prices. This proposition is attracting more consumers, with improved conversion. Among our active consumers, we are seeing faster growth in users who are from lower tier cities, are young people, or are older people.

Looking at the numbers from this year's 6.18 shopping festival, we see several large consumption trends --- because you asked about sales to 88 VIP members and the relationship between users and order frequency.

We’ve seen increasingly strong interest on the part of users in value-for-money offerings, and increasingly high engagement. So this year’s 6.18 shopping festival attracted a lot of young consumers to take part and make purchases.

Another driver of sales this year was new product launches. Over three million new products were launched by brands on Tmall at this year’s 6.18, driving sales in appliances, home decoration, apparel, beauty, and more.

So coming back to the topic of 88 VIP members, we can see that these premium users are attracted by new products and richer supply.

Gary Yu (Morgan Stanley):

(Original)

Thank you, management, for the opportunity. I have one question related to cloud and a follow-up on AI. Just wanted to check when do we expect to see cloud revenue grow to kind of further accelerate to a higher level, given there appears to be some reluctance for corporates to spend on IT spending? And a related question on AI is given the fast adoptions of our AI offerings that we have launched recently, how should we look at the timeline and roadmap from a regulatory and also monetization standpoint? Thank you.

Daniel Zhang:

(Original)

Yeah, I think if you look at the cloud landscape in China, I think the total cloud infra as percentage of the IT infra still in a lower, actually in a relatively lower percentage as compared to the US peers. So, we still - we see that still the huge potential, first in the - this cloud infra penetration.

Secondly, I think with this AI revolution, I think that this will bring incremental opportunities, and because today all the companies want to use the AI capabilities to upgrade their services and in their own application. So - but they need a high computing – high-performance computing power to support this operation not only in today's training, but also in the infra services to be provided. So I think these two are, we believe, the primary growth engine for the long term.

Yeah, if you look at our own performance, I think right now we are taking some time to digest some impact from the - first from the decline of the demand, post-pandemic, as we said in our scripts. For example, for many services relating to remote work, remote education, as well as the online streaming, the demand, obviously, is lower post-pandemic, which I think is a very important factor to drive our growth rate. And also, we also have some impact from the decline in demand from one top customers - one of the top customers. So I think we need to - still need some time to digest this. Also, we're also making some proactive measures to make sure we focus on public cloud growth and focus on high-quality cloud service growth. So I think with this right sales structure and the customer profile, we are in a better position - we'll be in a better position to have a long-term sustainable growth.

For the second question, how to monetize this AI opportunity. I think the answer is very straightforward. It's like, as a cloud service provider, our best monetization model is to have all the AI companies, all the models using Alibaba Cloud Infra, and our high-performance low-cost computing power to build their AI. So I think, while we do our foundational model in Ali cloud and deploy this - and deploy it on our cloud infra, is to not only just run our own model, it's to help our cloud industry partners to use this foundational model to build their - to do their fine tuning, to build their own model in their vertical industries and in their own customized applications. So, I think this is - I think, for us, I think this is a huge opportunity and I think we would do everything we can to make sure we provide best-in-class services to help these new generations of innovation to be occurred on our cloud infra. Thank you.

Just to add one more point, which is, when we talk about this ecosystem, and we strongly believe in this AI new era there is a new ecosystem that is generating - is incubating. So that's why we do a lot to grow our model - our community model scope to make sure all the relevant models, all the good models in the market, not only from Alibaba, the vast vast majority of them are from ecosystem, to make all the models available for the developers, for the industry partners. And we provide tools, applications to help them to use these models. And a lot of them are open-source models, as I said in my script. And then from our side, we are also - we'll continue our efforts to upgrade our model and also continue our open-source strategy for the models. And the more people use models, then the more people will use computing power. That's the short answer. Thank you.

Jiong Shao (Barclays):

(Translation)

Thanks, management, for taking my question. I have a follow-up question for Daniel regarding AI. We know that Alibaba Cloud has launched its Tongyi model and has recently opened up two open-source models, and in addition is also hosting an open-source model from Meta. Given all the uncertainties in this market, I'm wondering what the industry landscape will look like for large language models in China three to five years from now? How many companies will have successful foundational models? What will the mix look like as between proprietary versus open-source models? And what factors will determine their success or failure?

Daniel Zhang:

(Translation)

That's an excellent question, and difficult to answer. This is the beginning of a new era, so it's hard to predict the next three to five years. In this industry, things are moving so fast that most people take a month-by-month view to tracking the changes.

Let me share some of my own observations and judgments. There are quite a lot of companies in China today that are working on large models. Going forward, I think there are basically two development pathways available to these companies. One is the one that Alibaba has chosen because we are a cloud provider. We will continue to develop our large models, and as we evolve them, will continue to open them up, including making them open source, so that more people will make use of these foundational models. As these are foundational models, they should be accessible and inclusive. So we are making them available for more developers to use. That is one direction, or pathway.

The other pathway is to start out with a foundational model, but then to focus on a few particular domains where you have expertise. That will depend on the quality and scale of the data that such companies have in a given domain, and their insight. So I think there will be some AI companies who will start out by developing large models, but will quickly move into developing specific bodies of intelligence for specific domains. These are the two trajectories that we can foresee.

Strictly speaking, those in that second category are not large model companies. What they're really doing is developing vertical models. In today's market landscape, it's hard to distinguish between the two, and everyone says that they are building large models, but the vast majority will in fact end up focusing on a particular domain.

But another crucial point I would add is that the AI opportunity is larger than just AI per se. AI will create a brand-new opportunity to upgrade all existing applications and services, including both 2C and 2B. In fact, AI is relevant across all industries and all sectors, for all different kinds of Internet applications and services. As we've said ourselves, it's worth rethinking and rebuilding all of Alibaba's own businesses leveraging next-generation AI. And I think that's true not just for Alibaba but for all different sectors and all kinds of services. On this point, there is strong consensus.

Thomas Chong (Jefferies):

(Original)

Thanks, management for taking my questions. I have a question regarding the international business. Given that the strong performance that we are seeing across different countries, I just want to get the thoughts from management regarding the competitive landscape in different regions and our growth strategies. And then a follow-up question on that one is really about the logistics side. Given the strong performance of Cainiao, how should we think about the synergies between Cainiao and our international business to enhance the user experience? Thank you.

Daniel Zhang:

(Original)

Yeah. Actually, we reported a very good quarter for our AIDC, our overseas digital commerce business. And we are happy to see that our strategies, after a couple quarters of efforts, and we see a strong sign of success. And we strongly believe this is a sustainable trend.

And as you ask, I think we are trying to find our unique position in the global market. And we are - when we talk about global market, we have very clear target by market, by region - not only by region, also by country. Because consumption is highly relevant to the culture and highly relevant to the local retail landscape. So we need to find our uniqueness - unique strength to create the real value to the customers in the destination country.

Our unique advantage - of course, one of the advantages is the supply from China. I think the Choice model just to unlock the advantage by a consolidated/integrated supply chain from end to end. So going forward, we'll continue to scale up this model and together with the growth of the platform model and in different markets. And we have differentiated market strategies. In some businesses, we focus on cross-border. This could be a main course for some businesses, but for some other market, we focus on local to local as a main course plus cross border from China as a dessert. And also today may cross border from China, maybe tomorrow, cross border from other countries.

And also, we are trying to leverage our strong coverage in China with our B2B business, because we are a very successful B2B business, which basically have a very strong connection with our - with many Chinese exporters. They are all SMEs. Some of them sell industrial products, but we have many of our exporters sell consumer products. So this could be a huge - I mean, flying wheel to connect the integrated supply chain from B2B to B2C.

So for your second - for your question about Cainiao and AIDC, I think this quarter is a very good example - shows a very good example of how the synergies we can create - created between the - among the different business groups in Alibaba.

So I think the strong growth of AIDC is - one of the main reasons is our improved logistics and service experience - together with the strong performance of our logistic network. So for example, right now we are providing five-day global delivery, which means a global delivery within five days. If you can give the customers thousands of miles away – tens of thousands of miles away from China a high certainty of the logistic experience, this could be the best user acquisition tool and user acquisition model. So, if we combine these two together and see very strong synergies and we’ll continue to do that.

And on one hand is to enhance the assortment strategies to make sure we have the right supply. Second is to enhance the logistics and service standard and capability and to make sure customers can have the good experience. If they have a good experience in their first few tries, they will be with us. I think they have, because with a good experience, the price point from China supply has a unique strength in the world.

James Lee (Mizuho):

(Original)

Yeah, thanks for taking my questions here. It's just one follow-up on question on, you know, cloud computing specifically. And Daniel, can you comment about – obviously, you commented about technology. That's super helpful. Can you talk about maybe from the marketing perspective, you know, what verticals are important for you to pursue in the near term to drive the growth of the business, and why? Thanks.

Daniel Zhang:

(Original)

So actually, Cloud is relevant to all the industries. If you ask me which industries we are – we prioritize, I would say actually first of all I think the Internet companies, I think because all the Internet companies are digital native companies and they're supposed to grow their business on cloud. And so from this part - I think if you look at the history of Alibaba Cloud, we will grow together with the Internet companies, especially the mobile internet companies in China, together. So, I think – in this part, I think we still have a big space to penetrate, to help all the Internet companies. Today, not all of them are purely digital native, data-driven, and even though everybody has a mobile app and has a web page, but I think the level of digitalization and complexity of their digitalization is quite different. So I think in this regard, we can still work closely with them, starting with the penetration of the cloud infra and also with more penetration with the PaaS products. I think a PaaS service, and AI service, today, so I think the Internet obviously is a very important sector.

And also financial services, because financial services is a very big industry and there are many companies, many types of sub-sectors are in this sector, in this industry. So, I think we also spend a lot of our resources on these.

And also, we are also developing our services and product services to serve industries like automobile. Because if you look at the EV companies, and all the EV companies, no matter they are new EV players, the "new force", or the existing ones, I think pretty soon all of them, they are purely digital-driven companies, they're data-driven companies.

So, I think we will – generally speaking – I just gave you a few examples, but generally speaking, we will focus on the industries with a higher level of digitalization and we will prioritize the industry digital native or they have a very successful digital transformation or they are on birth from day one they are digital native. So, this is our focus and strategy. Thank you.

Jialong Shi (Nomura):

(Translation)

Thanks for taking my question. My question has to do with the e-commerce business. Could management share with us your growth outlook for Taobao and Tmall in the September quarter, in terms of DAUs and revenues? And then coming back to the June quarter, Taobao and Tmall saw a decline in margin year-over-year. I note that Tmall Supermarket and Tmall Global, which are lower-margin businesses, accounted for a larger proportion of the total, so that could have caused the decline in overall margin. But I'd like to know if there are any other factors that contributed to the year-over-year decline in margin? And how do see margin trending in the future for Taobao and Tmall?

Trudy Dai:

(Translation)

Thanks for the questions. Let me start with the question on Tmall Supermarket. Tmall Supermarket is a 1P business whose margin is improving. In addition, we're investing heavily this year in improving user experience and are rolling out half-day delivery service in 20 cities across China. And in those cities with half-day delivery, we're seeing very significant gains in user scale, orders, and user satisfaction.

E-commerce in general, as a kind of commerce, is affected by a variety of different factors, among which the macroeconomic environment and competitive dynamics are particularly relevant.

Rather than focusing on short-term competition and short-term growth, we're much more preoccupied with ensuring the long-term development of our business and in constantly surpassing ourselves.

And as I said earlier, given the considerable uncertainty and volatility that lie ahead, it's all the more crucial to be investing in building our capabilities.

That's why in the three years to come, we'll be investing resolutely in growing user scale, enhancing user experience, helping merchants grow their businesses, and enhancing the services we provide to merchants.

We have over two decades of experience and insight in the e-commerce space and, based on that, I am fully confident that we will be able to maintain our dual leadership position – leadership in terms of both user scale and merchant scale – going forward.

The investments that we're making today will certainly pay off in the future in terms of driving revenue and profit growth. Thank you.

Rob Lin:

(Original)

Well, thank you everyone, and that's the end of our earnings call today. If you have further questions, feel free to reach out to me and my team. Thank you and we'll see you next quarter.

[END OF TRANSCRIPT]