Vipshop Holdings
First Quarter 2013 Earnings Conference Call Script
May 15, 2013

Operator:

Good day everyone and welcome to Vipshop Holdings' first quarter 2013 earnings conference call.

At this point, I would like to turn the call to Ms. Millicent Tu, Vipshop's Director of Investor Relations. Please proceed.

Millicent Tu:

Thank you, operator. Hi everyone and thank you for joining Vipshop's 1Q13 earnings conference call. Before we begin, I will read the forward-looking statement.

During this conference call, we will make "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 that are based on our current expectations, assumptions, estimates and projections about Vipshop Holdings Limited and its industry. All statements other than statements of historical fact we may make during this call are forward-looking statements. In some cases, these forward-looking statements can be identified by words or phrases such as "anticipate," "believe," "continue," "estimate," "expect," "intend," "is/are likely to," "may," "plan," "should," "will," "aim," "potential," or other similar expressions. These forward-looking statements speak only as of the date hereof and are subject to change at any time, and we have no obligation to update these forward-looking statements.

Joining us on today's call are Eric Shen, Chairman, the company's CEO and Co-Founder, and Donghao Yang, the company's Chief Financial Officer. At this time, I would now like to turn the conference call over to Eric Shen.

Eric Shen:

Hello everyone. Welcome to our first quarter 2013 earnings conference call.

This quarter, we are very pleased with our strong momentum, which once again underscored the strengths of our unique e-commerce model. Fueled by rapid growth in both active customers and total orders, we more than tripled our revenues in this quarter to US$311 million and outperformed our expectations due to stronger post-holiday rebound in demand which we will discuss later. Through growing scale and leverage in our business operation, we continued to expand our profitability and margins during this quarter, which our CFO Donghao will explain shortly.

To begin with, by building upon last year's strong growth momentum and this year's successful secondary, our strategy and success has changed the landscape in China's B2C e-Commerce market. This huge success has enabled us to quickly increase our profile with the major brands as well as Chinese shoppers. As a result, we continue to extend our lead over the competition in China's fast growing discount retail market. For customers, they come to our website because they want the best product selection at the lowest prices available. In order to satisfy them, we have a world class merchandising team of over 300 experienced buyers dedicated to finding the best products from the best brands. For the brands, they demand capable and proven partners to handle their excess inventory without hurting their brand identity. We help over 6,000 brands by quickly liquidate this inventory and for over 800 of them, we have exclusive access to their merchandise. In doing so we reduce any brand dilution, further strengthen our mutual trust with these partners, as well as often providing customers exclusive access to products that are in high demand but limited quantities. None of these advantages can be quickly copied by general ecommerce players overnight. These network and scale effects from our unique online discount retail model, offering our brand partners higher financial returns, faster turnover and, most importantly, reduced brand dilution, further separate us from our existing or emerging competitors in China. These attributes provide us increasing confidence in our ability to continue our success.

At this point, let me hand over the call to our CFO, Donghao Yang so that he may discuss this quarter's achievements and our future strategies in greater detail.

Donghao Yang:

Thanks Eric and hello everyone.

I'd like to further elaborate on four key areas over the course of today's call prior to reviewing our financials:

- First, key highlights of our quarterly financial results;
- Second, the huge growth potential for China's discount retail market;
- Lastly, we'd like to update you on our strategic focuses for 2013.

To begin with, we had another strong quarter of growth across the board. Total revenues increased by 207% year-over year to US$311 million. Despite being a typically slow quarter due to seasonality associated with the Chinese New Year holiday, we saw our customer activity and post-holiday spending rebound much faster and stronger than previous years, helping our top line growth exceed both our expectations and the consensus estimates by a strong margin. Gross margin expanded further to 23.4% while fulfillment expenses continued to trend down to 12.1% of total revenues as a result of our increased scale and improved efficiencies in our logistics network. Moreover, we continued to grow our GAAP net income, which came in at US$5.8 million, thus demonstrating our balanced strategy of maintaining strong top-line growth while improving profitability at the same time.

Second, looking at the huge growth potential of China's discounted retail market, Frost and Sullivan estimates that this market will grow dramatically from only 24 billion US dollars in 2012 to over 90 billion dollars in 2015, representing a compound growth rate of 55%. As Eric mentioned, by leveraging the inherent scale effect associated with our business, we have been and continue to attract tens of millions of online shoppers as well as the brands aiming to target this group of online shoppers which is expected to almost double from 219 million in 2012 to over 423 million by 2016 according to eMarketer.

Lastly, I'd also like to update you on our warehouse capacity expansion strategy. We are continuing to invest in our logistics centers and expanding our warehouse capacity. We expect to increase to 290,000 square meters by the end of this year to primarily accommodate the surging demand of our customers in China's North East and Eastern regions.

Backed by these strong industry drivers and operational strategies, we are increasingly confident in our ability to continue expanding our lead in China's underdeveloped but quickly growing discount retail market. Our ability to capitalize on our first-mover advantage in China's nascent discount retail market, compounded by our recent successful follow-on offering, provides us with the capital and confidence to further implement our expansion strategy and extend our leadership position. By accelerating the expansion of our logistics network and fulfillment capabilities while enhancing our IT infrastructure and mobile commerce capabilities for China's increasingly active online shoppers, we aim to continue delivering strong and sustainable growth for years to come.

Now, moving on to our quarterly financial highlights:

Net revenues for the first quarter of 2013 increased by 207% year-over-year to US$310.7 million. This tremendous growth was primarily driven by a 170% increase in the number of total active customers to 2.8 million and a 187% increase in the number of total orders to 8.8 million.

Like we highlighted earlier, this increase was primarily due to our continued efforts to optimize brand and product selection, increase the number of sales events and increase the number of SKUs available on our websites as well as mobile platform. In addition, we have been able to fully utilize the three logistics centers in Shanghai, Chengdu and Beijing, and regional sub-sites, which enhanced our ability to accommodate and target the increased demands in specific markets, further increasing our market scale and footprint.

As our business continues to scale, we are able to secure more premium inventory from brand suppliers with gradually larger discounts, further decreasing product acquisition costs.

As a result, this led to **gross margins** further improving to 23.4% from 21.2% in the prior year period, and gross profit increasing by 240% to US$72.8 million.

Moreover, as we discussed earlier, we continued to see improvement in operating margins as a result of improved economies of scale and increased operational leverage with our business operation. More specifically:

- **Fulfillment expenses** increased by 123% year-over-year to US$37.7 million for the first quarter of 2013. This primarily reflects an increase in sales volume and number of orders fulfilled. As a percentage of net revenues, fulfillment expenses decreased to 12.1% from 16.7% in the prior year period. As we discussed over the last few quarters, this improvement is very noteworthy in that fulfillment expenses are not only the largest component of our operating expenses but also critical to the customer experience. This cost reduction was primarily due to the successful implementation of our distributed warehouse strategy and the strategy of shifting towards using regional and local delivery services. Also, we continued to expand our capacity to four warehouses which are strategically located in Shanghai, Beijing, Chengdu and Guangzhou. In addition, we continue to shift more fulfillment needs to high-quality regional and local couriers, lowering our fulfillment cost while shortening delivery times to our end customers.

- **Marketing expenses** increased by 124% year-over-year to US$13.1 million. As a percentage of net revenues, marketing expenses decreased to 4.2% from 5.8% in the prior year period. As discussed previously, by maintaining customer satisfaction and high repeat customer demand, we are able to realize significant cost benefits associated with word-of-mouth referrals. Going forward, we expect to further improve our marketing efforts through proactive sales marketing and PR campaigns.

- **Technology and content expenses** increased to US$7.9 million from US$2.4 million in the prior year period. As a percentage of net revenues, technology and content expenses remained stable at 2.6% compared with 2.4% in the prior year period. This is a part of our continued efforts to invest in our IT system and mobile ecommerce capabilities to better support future growth.

- **General and administrative expenses** increased by 70% to US$9.8 million year-over-year. As a percentage of net revenues, general and administrative expenses decreased to 3.2% from 5.7% in the prior year period. The cost reduction reflected our Company's continued cost-control efforts and increased operational leverage.

Driven by the growing scale of our Company's operations, improved gross margin and costs control, we realized US$5.5 million in **income from operations** for the first quarter of 2013. This is compared to a loss from operations of US$8.7 million in the prior year period. Operating income margin was 1.8%, compared to an operating loss margin of 8.6% in the prior year period.

Non-GAAP income from operations, which excludes share-based compensation expenses, was US$8.6 million, compared to a non-GAAP loss from operations of US$6.6 million in the prior year period. Non-GAAP operating income margin was 2.8%, compared to a non-GAAP operating loss margin of 6.5% in the prior year period.

Our **net income attributable to ordinary shareholders** for the first quarter of 2013 was US$5.8 million, compared to a net loss attributable to ordinary shareholders of US$8.6 million in the prior year period. **Net income margin** was 1.9%, compared with a net loss margin of 8.5% in the prior year period. For the first quarter of 2013, we recognized US$1.9 million income tax expenses as a result of our Company's growing profitability. Net income attributable to ordinary shareholders per diluted ADS was 11 US Cents, compared to a net loss attributable to ordinary shareholders per diluted ADS of 33 US Cents in the prior year period.

Non-GAAP net income attributable to ordinary shareholders was US$9.0 million compared to a non-GAAP net loss of US$6.5 million in the prior year period. Non-GAAP net income margin was 2.9% compared with a non-GAAP net loss margin of 6.4% in the prior year period. Non-GAAP net income attributable to ordinary shareholders per diluted ADS was 17 US Cents in the first quarter of 2013 compared to a non-GAAP net loss attributable to ordinary shareholders per diluted ADS of 25 US Cents in the prior year period.

As of March 31, 2013, our Company had cash and cash equivalents of US$231.1 million and held-to-maturity securities of US$141.6 million. For the first quarter of 2013, **net cash from operating activities** was US$71.1 million.

Looking at our business outlook. For the second quarter of 2013, we expect our net revenues to be between US$330 million and US$335 million, representing a year-over-year growth rate of approximately 144% to 148%. These forecasts reflect our current and preliminary view on the market and operational conditions, which are subject to change.

With that, I would now like to open the call to Q&A.
