

Operator:

Ladies and gentlemen, good day everyone and welcome to Vipshop Holdings Limited's fourth quarter and full year 2018 earnings conference call.

At this point, I would like to turn the call to Ms. Jessie Fan, Vipshop's Head of Investor Relations. Please proceed.

Jessie Fan:

Thank you, operator. Hello everyone and thank you for joining Vipshop's fourth quarter and full year 2018 earnings conference call. Before we begin, I will read the Safe Harbor 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, our co-founder, chairman, and CEO, and Donghao Yang, our CFO. At this time, I would like to turn the call over to Mr. Eric Shen.

Eric Shen:

Good morning and good evening, everyone. Welcome and thank you for joining our fourth quarter and full year 2018 earnings conference call.

We delivered solid operational results in the fourth quarter of 2018, with total active customers growing by 13% year over year. Further, our collaboration with Tencent and JD continued to bring us high quality new customers. In the fourth quarter, new customers from WeChat and JD accounted for 23% of our total new customers.

Our existing customers are also becoming stickier to our platform. As of the end of 2018, around 3.2 million customers joined our Super VIP Paid Membership, which is a 38% increase quarter over quarter. The initial renewal rate for customers who joined the program before 2018 was over 70%. We are glad that our customers recognize the value of this membership. All these successes are the result of our focus on merchandising and the shift back to deep discounted products.

In the fourth quarter, we also delivered good results during the two promotional events. The number of active customers who purchased during this year's Singles' Day increased by 23% year over year. In addition, our suppliers are now even more willing to partner with us as a result of the change to focus on discounted retailing. More than 5,500 brands joined the December 8th Anniversary Sale, representing a 14% year-over-year increase.

Looking ahead, we will continue to focus on discounted retailing and execute on our merchandising strategy, which have already shown some positive results in the fourth quarter.

We are committed to procuring the best products that cater to our customers' needs. By becoming the dominant player in the apparel discounted retail segment, we aim to further drive our profitability and deliver robust shareholder return in the long run.

At this point, let me hand over the call to our CFO, Donghao Yang, so that he may discuss our strategies in more detail and go over our operational and financial results.

Donghao Yang:

Thanks Eric and hello everyone.

In the fourth quarter of 2018, we saw a healthy sequential recovery of our net margins, which is a reversal from the previous trend of declining year-over-year net income profile. Additionally, we generated robust free cash flow of 6.0 billion RMB during the quarter, as compared with 2.1 billion RMB in the prior year period.

The positive changes in gross margin and net margin trends resulted from our focus on the highly profitable apparel category. During the fourth quarter of 2018, we began to shift some low-margin categories from our first-party business into the marketplace platform, which reduced their drag on our profitability. Further, GMV contribution from the apparel category, which has a relatively high return rate but is more profitable as compared to other categories, increased from the prior year period. As a result, we delivered improved profitability while still achieving a solid 15% year-over-year growth in GMV.

We began to disclose GMV as an additional operational metric this quarter primarily due to a few considerations. First of all, as compared to total net revenue, we believe GMV serves as a better metric for industry comparison. Furthermore, GMV provides an additional perspective to understanding the scale of our business in light of the recent development in our revenue mix.

We record product revenue for our first-party business and other revenue for our marketplace business. As we currently expect contribution from other revenue to increase, we believe the additional disclosure of GMV could help investors understand the scale of our business in a more consistent fashion. In the fourth quarter of 2018, while our total net revenue grew by 8% year over year, our GMV grew by 15% year over year.

This recent development in revenue mix will have a rather significant impact on our reported total net revenue in the coming quarters, making it less meaningful to compare future total net revenue numbers with historical figures. Therefore, we encourage investors to use GMV as an additional metric to measure the scale of our business, and also focus on our profitability trends going forward.

Please note that we continue to be committed to doing business on the first-party model for our core categories, which is a key competitive advantage for Vipshop.

Moving on to logistics. We continued to build out our warehousing capability, adding around 86,000 square meters of warehouses in the fourth quarter. As of December 31, 2018, we have approximately 3.0 million square meters of total warehousing space, of which around 1.9 million square meters is owned by the Company.

Turning to our Internet finance business. Approximately 6.4 million active customers used our consumer financing service during the quarter, which accounted for around 24% of GMV. As of December 31, 2018, the total balance of credit outstanding to customers was approximately 5.7 billion RMB, and the total balance of credit outstanding to suppliers was approximately 1.3 billion RMB.

We remain focused on stabilizing our margins through implementing strict cost control as well as improving our category mix. Our core competency lies in our ability to procure desirable products at low costs. By continuing to execute on our merchandising strategy, we will enhance our profitability and drive improved shareholder return over time.

Now moving on to our quarterly financial highlights. Before I get started, I would like to clarify that all the financial numbers presented today are in Renminbi amounts and all the percentage changes refer to year-over-year changes unless otherwise noted.

Total net revenue for the fourth quarter of 2018 increased by 8.1% to 26.1 billion from 24.1 billion in the prior year period, primarily driven by the growth in the number of total active customers.

Gross profit for the fourth quarter of 2018 increased by 2.8% to 5.4 billion from 5.2 billion in the prior year period. **Gross margin** was 20.6% as compared with 21.7% in the prior year period.

- **Fulfillment expenses** for the fourth quarter of 2018 were 2.1 billion, as compared with 2.1 billion in the prior year period. As a percentage of total net revenue, fulfillment expenses decreased to 8.0% from 8.9% in the prior year period.
- **Marketing expenses** for the fourth quarter of 2018 were 1.1 billion, as compared with 1.0 billion in the prior year period. As a percentage of total net revenue, marketing expenses were 4.3% as compared with 4.2% in the prior year period.
- **Technology and content expenses** for the fourth quarter of 2018 were 533 million, as compared with 486 million in the prior year period. As a percentage of total net revenue, technology and content expenses remained stable at 2.0% year over year.
- **General and administrative expenses** for the fourth quarter of 2018 were 821 million, as compared with 780 million in the prior year period. As a percentage of total net revenue, general and administrative expenses decreased to 3.1% from 3.2% in the prior year period.

Our **income from operations** for the fourth quarter of 2018 increased by 13.5% to 1.0 billion from 884 million in the prior year period. **Operating margin** increased to 3.8% from 3.7% in the prior year period.

Non-GAAP income from operations, which excludes share-based compensation expenses and amortization of intangible assets resulting from business acquisitions, was 1.1 billion as compared with 1.1 billion in the prior year period. Non-GAAP operating income margin was 4.3% as compared with 4.6% in the prior year period.

Our **net income attributable to Vipshop's shareholders** for the fourth quarter of 2018 increased by 2.3% to 689 million from 673 million in the prior year period. **Net margin**

attributable to Vipshop's shareholders was 2.6%, as compared with 2.8% in the prior year period. Net income attributable to Vipshop's shareholders per diluted ADS was 1.00 RMB, as compared with 1.07 RMB in the prior year period.

Non-GAAP net income attributable to Vipshop's shareholders, which excludes share-based compensation expenses; impairment loss in investments; amortization of intangible assets resulting from business acquisitions and equity method investments; tax effect of amortization of intangible assets resulting from business acquisitions; loss or gain on disposal, revaluation and value changes of investments; and share of result in investment of limited partnership that is accounted for as an equity method investee, increased by 2.9% to 914 million from 888 million in the prior year period. **Non-GAAP net margin attributable to Vipshop's shareholders** was 3.5%, as compared with 3.7% in the prior year period. Non-GAAP net income attributable to Vipshop's shareholders per diluted ADS was 1.33 RMB, as compared with 1.41 RMB in the prior year period.

As of December 31, 2018, our company had cash and cash equivalents and restricted cash of 10.0 billion and short term investments of 2.3 billion. For the fourth quarter of 2018, net cash from operating activities was 5.9 billion.

Looking at our business outlook for the first quarter of 2019, we expect our total net revenue to be between RMB19.9 billion and RMB20.9 billion, representing a year-over-year growth rate of approximately 0% to 5%. These forecasts reflect our current and preliminary view on the market and operational conditions, which is subject to change.

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

Closing Remarks – Donghao Yang:

Thank you for taking the time to join us and we look forward to speaking with you next quarter.