

**Operator:**

Ladies and gentlemen, good day everyone and welcome to Vipshop Holdings Limited's second quarter 2019 earnings conference call.

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

**Jessie Fan:**

Thank you, operator. Hello everyone and thank you for joining Vipshop's second quarter 2019 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 second quarter 2019 earnings conference call.

We delivered strong operational and financial results for the second quarter of 2019. During the quarter, our total active customers continued to grow at a healthy pace, increasing by 11% year over year. Since we refocused on discount retail, the stickiness of both our existing and new customers has improved. We are delighted to see our existing customers becoming a lot more active, while at the same time, new customer repeat purchase rate in the quarter after the first purchase has increased. These successes are the result of our focus on merchandising.

Since we refocused on discount apparel and our profitability, we have seen substantial improvement in our financial results and key operating metrics, proving our strategy is very effective. We remain committed to executing on our merchandising strategy and further expanding our market share in the discount apparel sector in China. We are confident that we can continue to deliver steady profitability improvement in the future, which will generate sustainable, long-term shareholder return.

We strive to be the one-stop discount retail platform for our suppliers, solving all their inventory management issues in the off-price segment within our ecosystem. We have over a decade of experience in online discount retail, and we believe in this age and time, online and offline are closely linked. Shoppers will increasingly demand Omni-channel shopping experiences. Given that, we began to enter the offline discount retail segment this year, and our acquisition of Shan Shan Outlets is an important part of our new retail strategy. Shan Shan Outlets is a profitable

business with healthy operating cash flow. Importantly, they have a top-notch management team with a decade of experience in managing and operating outlets in China, whom will stay with Vipshop after the acquisition.

Strategically, we will continue to focus on our online business, while our offline strategy, including our investment into Shan Shan Outlets, Vipshop offline stores, and Vipmaxx offline stores, is complementary to our online business. Our goal is to help our suppliers manage their inventory cycles more effectively via different channels within our ecosystem.

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.

We finished the second quarter of 2019 with robust financial results. Our topline grew by 10% year over year, exceeding our expectations. Importantly, our non-GAAP net margin attributable to Vipshop's shareholders increased by 1.9 percentage points year over year, which is the result of improved gross margin and more effective cost control. During the quarter, we generated robust free cash flow of 1.2 billion RMB, as compared with negative free cash flow of 903 million RMB in the prior year period, representing a 2.2 billion RMB increase year over year.

In the second quarter of 2019, we saw improved conversion rate and elevated customer engagement from both our existing and new customers. As a result of that, our GMV grew by 11% year over year, driven by the robust growth in our core categories. Specifically, GMV for apparel-related categories has seen 19% year-over-year growth, which is the fastest among all major categories.

During the quarter, we made further progress in outsourcing our last mile delivery to third party couriers. Currently, around 30% of our daily orders are delivered by third party partners. We continue to carefully monitor the effect on customer experience throughout this process, and are evaluating whether or not it would be beneficial to outsource more orders, which will further reduce fulfillment cost.

We will be prudent in our investment in the offline segments as they're more asset heavy than the online business, and we need some time to gain operating experience in these newer areas. Rest assured, we will be monitoring the profitability and return on investment from all our businesses very closely. The focus on the high margin apparel category has and will continue to enable us to deliver improvement in our gross margin and overall profitability.

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 second quarter of 2019 increased by 9.7% to 22.7 billion from 20.7 billion in the prior year period, primarily driven by the growth in the number of total active customers.

**Gross profit** for the second quarter of 2019 increased by 25.9% to 5.1 billion from 4.0 billion in the prior year period. **Gross margin** increased to 22.4% from 19.5% in the prior year period.

- **Fulfillment expenses** for the second quarter of 2019 were 2.2 billion, as compared with 1.9 billion in the prior year period. As a percentage of total net revenue, fulfillment expenses were 9.7% as compared with 9.1% in the prior year period, primarily attributable to a write-down of 276 million related to the Zhaoqing warehouse due to land subsidence during construction. Excluding the write-down, fulfillment expenses as a percentage of total net revenue for the quarter were 8.5%.
- **Marketing expenses** for the second quarter of 2019 decreased to 878 million from 900 million in the prior year period. As a percentage of total net revenue, marketing expenses decreased to 3.9% from 4.3% in the prior year period.
- **Technology and content expenses** for the second quarter of 2019 decreased to 422 million from 511 million in the prior year period. As a percentage of total net revenue, technology and content expenses decreased to 1.9% from 2.5% in the prior year period.
- **General and administrative expenses** for the second quarter of 2019 were 706 million, as compared with 615 million in the prior year period. As a percentage of total net revenue, general and administrative expenses were 3.1% as compared with 3.0% in the prior year period.

Our **income from operations** for the second quarter of 2019 increased by 141.2% to 965 million from 400 million in the prior year period. **Operating margin** increased to 4.2% from 1.9% 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, increased by 97.6% to 1.2 billion from 595 million in the prior year period. Non-GAAP operating income margin increased to 5.2% from 2.9% in the prior year period.

Our **net income attributable to Vipshop's shareholders** for the second quarter of 2019 increased by 19.3% to 814 million from 682 million in the prior year period. **Net margin attributable to Vipshop's shareholders** increased to 3.6% from 3.3% in the prior year period. Net income attributable to Vipshop's shareholders per diluted ADS increased to 1.21 RMB from 0.99 RMB in the prior year period.

**Non-GAAP net income attributable to Vipshop's shareholders**, which excludes share-based compensation expenses; amortization of intangible assets resulting from business acquisitions and equity method investments; tax effect of amortization of intangible assets resulting from business acquisitions; investment gain and revaluation of investments excluding dividends; tax effect of investment gain and revaluation of investments excluding dividends, and share of gain in investment of limited partnership that is accounted for as an equity method investee, increased by 84.2% to 1.1 billion from 577 million in the prior year period. **Non-GAAP net margin attributable to Vipshop's shareholders** increased to 4.7% from 2.8% in the prior year period. Non-GAAP net income attributable to Vipshop's shareholders per diluted ADS increased to 1.58 RMB from 0.84 RMB in the prior year period.

As of June 30, 2019, our company had cash and cash equivalents and restricted cash of 7.8 billion and short term investments of 238 million. For the second quarter of 2019, net cash from operating activities was 3.4 billion.

Looking at our business outlook for the third quarter of 2019, we expect our total net revenue to be between 17.8 billion RMB and 18.7 billion RMB, 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.