Vipshop Holdings
Second Quarter 2013 Earnings Conference Call Script
August 15, 2013

VIPSHOP.COM

Operator:

Good day everyone and welcome to Vipshop Holdings' second 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 2Q13 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 second quarter 2013 earnings conference call.

We are proud to report another solid quarter with strong revenue growth and margin expansion. Total active customer count increased by almost 140% year-over-year to 3.5 million, helping to drive a 160% year-over-year increase in sales to over $351 million. At the same time, we continued to grow our profitability, with GAAP net income increasing to US$9.0 million. We believe that these results attest to our growing market leadership and brand reputation as China's leading online discount retailer for brands. We believe that this unique and clear positioning gives us two key strategic benefits:

First, by being focused on specializing in the underdeveloped discount retailing market in China, we have established a core competence and leadership position. Through this intense focus, our capabilities in merchandizing, logistics, brand partnership, and consumer intelligence are specifically designed for the flash sales and online discount retailing business. By leveraging these distinct skill sets, we continue to provide our 3,200 brand partners with a robust one-stop solution for efficient inventory and cash flow turnaround. This is in a stark contrast to many other B2C sites and marketplace operators that have recently set up their own discount retailing channels and are simply providing listing capabilities.

Second, is the scale effect inherent in our business model. Our improved scale not only enabled this strong sales growth, but it also helped reduce our operating costs as a percentage of sales further improving our profitability. We are now reaching levels in the economies of scale that now make Vipshop the default, go-to, platform for major retailers hoping to quickly liquidate excess inventory. This, in turn, naturally attracts a wider range of shoppers looking for their preferred brand products, further driving our top- and bottom-lines.

These provide us increasing confidence in our ability to manage this strong growth and continue to drive top and bottom line growth. In today's market, Vipshop has emerged as a much bigger and stronger business. We firmly believe, and our results prove, that we have the right model and key core competencies that are critical to expanding and sustaining our business going forward.

At this point, let me hand over the call to our CFO, Donghao Yang so that he may discuss some new user growth initiatives as well as this quarter's financial achievements.

Donghao Yang:

Thanks Eric and hello everyone.

As Eric, discussed, we are extremely pleased about our strong operational performance and ability to manage this tremendous growth. At the same time, we are excited to discuss some new initiatives we have that are aimed at expanding our customer base and improving the user experience on our properties.

To begin with, a key initiative for us in the past few quarters has been the explosive growth on our mobile side. Our mobile sales have increased 67% quarter-over-quarter. This tremendous growth was fueled by two key factors: First, by nature of the flash sale model, mobile is extremely well suited for these "quick decision" shopping that is inherent in flash sale offers. Through our multiple mobile commerce options, which now consist of three mobile applications and a mobile internet website, we provide shoppers with a convenient way to purchase their desired products on our platform anytime, anywhere and on any device. Second, we continued to improve our user experience on our apps by improving the graphics for viewing items, as well as easing the purchasing process for users once they decide they like an item. Such improvements have further helped to increase overall customer interaction and stickiness on our platform. These results demonstrate the increasing appeal for conveniently accessing Vipshop for customers looking for uniquely priced offers on their favorite brands.

In addition, we have expanded our warehouse capacity in our four leased logistics centers in Shanghai, Chengdu, Beijing and Guangzhou and are on track to further increase it to approximately 300,000 square meters by the end of this year. This ramp-up in warehousing space will allow us to better accommodate the surging demand of our customers in China's North East and Eastern regions. Also, in anticipation of the continued growth in consumer demand, we are planning to complete construction of our own warehouse in Guangzhou and Hubei for a total of 300,000 square meters by the end of 2015 and expect it to cost approximately US$200 million.

To conclude, we aim to further expand upon the growth opportunities associated with China's large and underdeveloped discount retail market. Building upon our increasing scale, we remain confident that our market positioning and leadership role will further strengthen Vipshop's customer loyalty and brand partner satisfaction while fostering sustainable growth over the long term.

Now, moving on to our quarterly financial highlights:

Before I get started, I'd like to clarify that all the financial numbers we are presenting today are in USD amounts and all the percentage changes refer to year-over-year changes, unless otherwise noted.

Total net revenues for the second quarter of 2013 increased by 159.7% to $351.3 million. This tremendous growth was primarily driven by a 138.7% increase in the number of total active customers to 3.5 million and a 136.3% increase in the number of total orders to 11 million.

Gross margins further improved to 23.5% from 21.8% in the prior year period, and gross profit increasing by 179.6% to US$82.6 million. This improvement was driven by the increased scale of our business leading to larger discounts from our brand partners, which lowered our product acquisition costs as a percentage of sales.

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. More specifically:

- **Fulfillment expenses** increased by 108.4% to 42.8 million for the second quarter of 2013. As a percentage of total net revenues, fulfillment expenses decreased to 12.2% from 15.2% in the prior year period. This cost reduction was primarily due to the successful implementation of our distributed warehouse strategy as well as our continued shift to high-quality regional and local couriers, lowering our fulfillment cost while shortening delivery times to our end customers.
- **Marketing expenses** increased by 128.9% to 15.1 million. As a percentage of total net revenues, marketing expenses decreased to 4.3% from 4.9% in the prior year period. As you may have noticed, we initiated several large advertising campaigns, which helped generate a lot of buzz and attention around our April sales event. Despite the additional marketing spend on brand advertising, we still remain focused on word-of-mouth referrals. Going forward, we will continue to take a disciplined approach to managing our marketing expenses.
- **Technology and content expenses** increased to 8.7 million. As a percentage of total net revenues, technology and content expenses was 2.5%, compared with 2.0% 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 92.9% to 10.8 million. As a percentage of total net revenues, general and administrative expenses decreased to 3.1% from 4.1% 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 $6.7 million in **income from operations** for the second quarter of 2013. This is compared to a loss from operations of 5.4 million in the prior year period. Operating income margin was 1.9%, compared to an operating loss margin of 4.0% in the prior year period.

Non-GAAP income from operations, which excludes share-based compensation expenses, increased to 9.5 million, compared to a non-GAAP loss from operations of US$3.8 million in the prior year period. Non-GAAP operating income margin increased to 2.7%, compared to a non-GAAP operating loss margin of 2.8% in the prior year period.

Our **net income** for the second quarter of 2013 was 9.0 million, compared to a net loss attributable to ordinary shareholders of 5.8 million in the prior year period. **Net income margin** increased to 2.6%, compared with a net loss margin of 4.3% in the prior year period. Net income per diluted ADS increased to 16 US Cents, compared to a net loss per diluted ADS of 11 US Cents in the prior year period.

Non-GAAP net income increased to 11.8 million compared to a non-GAAP net loss of 4.2 million in the prior year period. Non-GAAP net income margin increased to 3.4% compared with a non-GAAP net loss margin of 3.1% in the prior year period. Non-GAAP net income per diluted ADS was 20 US Cents in the second quarter of 2013 compared to a non-GAAP net loss per diluted ADS of 8 US Cents in the prior year period.

As of June 30, 2013, our Company had cash and cash equivalents of 167.2 million and held-to-maturity securities of 217.3 million. For the second quarter of 2013, **net cash from operating activities** was 11.1 million.

Looking at our business outlook. For the third quarter of 2013, we expect our total net revenues to be between US$365 million and US$370 million, representing a year-over-year growth rate of approximately 134% to 137%. 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.

Closing Remarks from Donghao Yang:

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