Vipshop Holdings Limited
First Quarter 2016 Earnings Conference Call Script
May 2016

Operator:

Good day everyone and welcome to Vipshop Holdings Limited's first quarter 2016 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. Hello everyone and thank you for joining Vipshop's First Quarter 2016 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 chairman, chief executive officer and co-founder, and Donghao Yang, our chief financial officer. At this time, I would now like to turn the conference call over to Eric Shen.

Eric Shen:

Good morning and good evening everyone. Welcome to our first quarter 2016 earnings conference call. Our first quarter results once again show the strong power of our platform to attract and retain customers and suppliers. Active customers and total orders continued to grow at a year-over-year pace north of 50%, and pushed our top-line to reach over 12 billion RMB for the quarter.

Now, after several quarters of testing and adjusting our process for balancing profitability and customer acquisition growth with various means of marketing and promotions, we feel we have improved control between these competing levers and should experience more stabilized growth going forward.

Focusing on our market opportunity, in this highly fragmented discount retail segment, we have only just begun to scratch the surface. By leveraging our growing expertise and footprint, as well as fulfillment and logistics capabilities, we aim to expand and target new users in wider age groups. These diversified users often have different fashion demands. Through our data analytics, our buyers can better customize our recommendations for each of these users with a wider range of merchandise. It will enable us to grow our current base of just over 50 million total users and target a larger segment of China's 400 million plus online shoppers. We also aim to further expand our penetration of existing suppliers as well as continuously adding new ones. Through both of these means, we aim to further growth the discount retail space and consolidate market share throughout China.

Looking ahead, our focus remains on top-line and customer growth. We will accomplish this by continuing to offer our customers an unmatched shopping experience, from product discovery to delivery. And more specifically, by expanding selection, ensuring quick and consistent delivery times, and providing friendly after-sales service which includes a painless return policy.

Our discount retail offering remains unique in the Chinese market and we have built a deep moat to protect our core business. Once again, we are committed to our robust growth strategies, and are confident in the future prospects of our company. 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 the financial results.

Donghao Yang:

Thanks Eric and hello everyone.

We are pleased with our first quarter 2016 financial results. As Eric mentioned, during the first quarter, we continued to achieve strong growth in revenue, active users and total orders. Even as we have been focusing our efforts on growing our top-line and expanding our market share, we were able to further strengthen our operating margin to 4.9% from 4.6% in the prior year period, and non-GAAP operating income margin to 6.3% from 6.0% in the prior year period. The continued growth of our operating margin and stability of our gross margin demonstrates the tremendous operating leverage inherent in our business model and reflects our ability to reinvest earnings into propelling growth while maintaining healthy margins. During the remainder of 2016, we will continue to focus on our growth strategies, through increasing investment in promotional activities and marketing initiatives, while maintaining stable profitability.

As we announced in our previous earnings call, we have recently launched a financing program for customers in order to boost customer spending, after several years of operating a successful financing program for suppliers. As of March 31, 2016, the total balance of credit outstanding to customers was approximately 570 million RMB and our total balance of credit outstanding to suppliers was 488 million RMB.

We have introduced our consumer financing program to help us further increase stickiness and enhance the overall customer experience, while boosting the average spend per customer. And the strategy behind our supplier financing has always been to strengthen our supplier relationships and secure more preferred inventories, which in turn translates into increasing the order volume and improving the customer experience.

Recognizing the rising concerns and associated risks of internet finance, we implemented strong credit check and risk assessment systems from the inception of both the supplier and consumer financing programs. To elaborate, on the consumer side we have a seasoned team of experts responsible for monitoring for fraud, obtaining collection, analyzing default behavior, and adjusting credit approval metrics accordingly. These stringent risk control measures have resulted in no bad debt being recorded across both supplier and consumer financing and we had a 90-day overdue payment rate of less than 0.3%, as of March 31.

At the end of the day, our financing programs were established to support our core business growth, and not to operate as independent growth drivers. With that in mind our strategy is to judiciously expand the programs' scale overtime through balancing core growth opportunities with risk control.

On the logistics side, we have continued to build out a robust infrastructure of warehouses and network of invested-delivery companies to support and enhance our order fulfillment capabilities. By the end of the first quarter, our total warehouse capacity reached 1.6 million square meters. We remain committed to our goal of adding roughly 500,000 square meters of warehousing capacity in 2016.

On the last mile side, our in-house and invested last mile capabilities supported over 80% of the orders on our platform. Over the long term, we intend to expand our last-mile capabilities to support approximately 90% of the orders on our platform.

Looking ahead, we will continue to diversify our product offering, enhance our supplier and customer financing programs and further improve our logistic capacities, in order to ensure an excellent end-to-end user experience, and deliver enduring value to our loyal shareholders.

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 first quarter of 2016 increased by 41% to 12.17 billion, primarily attributable to a 52% year-over-year increase in the number of active customers which grew to 19.7 million and a 53% year-over-year increase in total orders to 58.7 million. This rapid volume growth, including accelerated cross-border product sales, resulted in lower ASPs for the quarter. As you know, ASPs will vary from season to season, as well as with any large promotional and marketing events we have in a given quarter.

Gross profit for the first quarter of 2016 increased by 38% to 2.96 billion, primarily driven by the expanding scale of the business. **Gross margin** for this quarter was 24.3%, as compared with 24.9% in the prior year period.

- **Fulfillment expenses** for the first quarter of 2016 were 1.08 billion, as compared with 806 million in the prior year period, primarily reflecting the increase in sales volume, and number of orders fulfilled. As a percentage of total net revenue, fulfillment expenses decreased to 8.9% from 9.4% in the prior year period, primarily reflecting the scale effect associated with our growth in total net revenue.

- **Marketing expenses** for the first quarter of 2016 were 604 million, as compared with 403 million in the prior year period, reflecting our strategy to drive long-term growth through increasing investments in strengthening our brand awareness particularly for our mobile application, attracting new users and expanding our market share. As a percentage of total net revenue, marketing expenses were 5.0%, as compared to 4.7% in the prior year period.

- **Technology and content expenses** for the first quarter of 2016 were 327 million as compared with 256 million in the prior year period, reflecting our continued efforts to invest in human capital and advanced technologies such as data analytics, which can help improve the ability to predict consumer behavior and further enhance user experience. As a percentage of total net revenue, technology and content expenses decreased to 2.7%

from 3.0% in the prior year period, primarily reflecting the scale effect associated with the growth in total net revenue.

- **General and administrative expenses** for the first quarter of 2016 were 382 million, as compared with 297 million in the prior year period. As a percentage of total net revenue, general and administrative expenses decreased to 3.1% from 3.4% in the prior year period, primarily reflecting the scale effect associated with our growth in total net revenue.

Driven by the growing scale of our company's operations and decrease in fulfillment, technology and content, and general and administrative expenses as a percentage of total net revenue, our **income from operations** increased by 51% to 596 million for the first quarter of 2016. **Operating margin** increased to 4.9% from 4.6% in the prior year period.

Non-GAAP income from operations, which excludes share-based compensation expenses, impairment loss of investments, and amortization of intangible assets resulting from a business acquisition and equity method investments, increased by 48% to 765 million from 517 million in the prior year period. Non-GAAP operating margin increased to 6.3% from 6.0% in the prior year period.

Our **net income attributable to Vipshop's shareholders** for the first quarter of 2016 increased by 29% to 475 million from 368 million in the prior year period. **Net margin attributable to Vipshop's shareholders** was 3.9%, as compared to 4.3% in the prior year period. Net income per diluted ADS increased to 0.80 RMB from 0.61 RMB in the prior year period.

Non-GAAP net income attributable to Vipshop's shareholders, which excludes share-based compensation expenses, impairment loss of investment in an equity affiliate and other investments, and amortization of intangible assets resulting from a business acquisition and equity method investments, increased by 28% to 623 million from 487 million in the prior year period. **Non-GAAP net margin attributable to Vipshop's shareholders** was 5.1%, as compared to 5.7% in the prior year period. Non-GAAP net income per diluted ADS increased to 1.04 RMB from 0.81 RMB in the prior year period.

As of March 31, 2016, our company had cash, cash equivalents and restricted cash of 3.57 billion and held-to-maturity securities of 704 million. For the first quarter of 2016, net cash from operating activities was 153 million.

Looking at our business outlook for the second quarter of 2016, we expect our total net revenue to be between 12.3 billion and 12.8 billion, representing a year-over-year growth rate of approximately 37% to 42%.