

Kuaishou Technology : NOT RATED

Analyst

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- **Kuaishou Technology is China's leading short video and live streaming social platform**
- **Company plans to upgrade its technology and branding to further cement its market leadership**
- **IPO priced at 4.2x-4.6x FY21F PS (based on our preliminary estimates), a much lower multiple than peers such as Bilibili (BIL US, 16x FY21 PS). SUBSCRIBE**

IPO details

Ticker code	1024.HK
Price offering	HK\$105-115
Total no. of shares	4,158,932,037 shares (over-allotment: 50,737,300 shares)
Offering size	365,218,600 shares (8.88 % of total share capital)
Market capitalisation	HK\$431.4bn-472.4bn
Joint Sponsors, Joint Global Coordinator, Joint Bookrunners and Joint Lead Managers	Morgan Stanley, BofA Securities, China Renaissance
Other Jointbrunners and Joint Lead Managers	HSBC, ICBC, ICBCI, Haitong, CMBI, BOCI, Futu
Conerstone Investor-Assuming over-allotment option is not exercised (% of total capital)	The Capital Group Funds (0.82%), Aranda Investments (0.54%), GIC (0.54%), Invesco (0.44%), Fidelity International (0.44%), BlacRock (0.37%), CPP Investments (0.25%), Sunny Festive (0.25%), MSAL and MSIM Inc. (0.21%), ADIA (0.16%) Subject to 6-months lockup period

Expected timetable

Application close	Friday, January 29, 2021
Result of allocation date	Thursday, February 4, 2021
Date of commencement	Friday, February 5, 2021

Source of all data on this page: IPO Prospectus, DBS Bank (Hong Kong) Limited ("DBS HK")

Remarks:

*MAU: Monthly active users of Kuaishou's apps and mini programs in China

**DAU: Daily active users of Kuaishou's apps and mini programs in China

Investment Thesis

One of the top 2 short video and live streaming social platforms with half of China's population as users. Kuaishou is a leading short video and live streaming social platform in China, with 769m/305m average MAU*/DAU** as of November 2020, positioning it as one of the high traffic social platforms. The company reported revenue CAGR of 117% in 2017-2019 to Rmb39,119m riding on the rising popularity of short video and live streaming. It is also one of the fastest growing internet companies in China.

Multiple revenue drivers on highly engaged user base. Kuaishou is well-known for its highly engaged user base, as daily time spent per DAU rose to 86.7 mins as of November 2020 from 52.7 mins in 2017. Strong user engagement offers potential to diversify monetisation avenues. Kuaishou initially monetised its traffic via selling virtual gifts during live streaming, and this was followed by online marketing services. It is also the second largest live streaming e-commerce platform after Alibaba since tapping into e-commerce market in 2018.

Margin improvement with turnaround potential. Margins are projected to improve in 2021 from: (a) rising contribution of higher-margin online marketing and e-commerce revenue, and (b) lower sales and marketing (S&M)-to-revenue ratio after its large-scale brand promotions in 2020. We expect Kuaishou's earnings to turnaround by 2022 as it achieves greater operating efficiency and stronger brand recognition.

Valuation. Based on our preliminary estimates, the IPO is priced at 4.2x-4.6x FY21F Price/Sales (PS). Compared to other multimedia platforms such as Bilibili (BIL US, 16x FY21 PS), Kuaishou is valued at a lower multiple. The stock is seemingly cheap in our view given the company's stronger market presence in robust live streaming and short video market with encouraging sales growth (117% revenue CAGR during 2017-19) and foreseeable earnings turnaround in 2022 vs. other Chinese peers. Recommend to subscribe.

Key Risks to Our View: Tightening regulatory policies, further outbreak of COVID-19, competition from well-funded competitors, brand reputation



Live more, Bank less

Flash Note

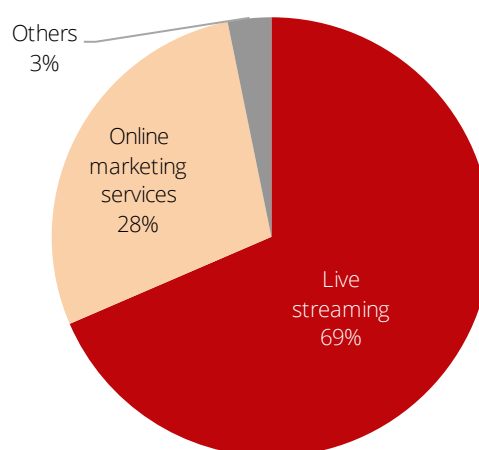
Company overview

Leading short video and live streaming social platform in China riding on entertainment upgrade. Established in 2011, Kuaishou is the leading short video and live streaming social platform with the slogan "Embrace every life". It started its operations from GIF Kuaishou tool and gradually transformed into a short video and live streaming community, riding on the increasing popularity of short video and live streaming in China. In 2014, Kuaishou was the first to introduce integrated recommendation algorithms into content distribution. It is currently ranked the largest live streaming platform by gross billings from virtual gifting and average live streaming monthly paying users (MPUs) the second largest short video platform by average DAUs, and the second largest live streaming e-commerce platform by GMV globally according to iResearch. It has three apps: Kuaishou Flagship, Kuaishou Express and Kuaishou Concept, generating 769m/305m average MAU/DAU as of September 2020, positioning it as one of the high traffic social platforms with strong user engagement.

Largest shareholder: Tencent. Tencent is the largest shareholder of Kuaishou with a 17.7% interest (Post-IPO, excluding allotment exercise) held through Tencent related companies including Tencent Mobility Limited, Morespark Limited, Parallel Nebula Investment Limited, Image Frame Investment (HK) Limited, and TPP Follow-on I Holding F Lim. Tencent is an internet company focusing on social communication and online games. It operates WeChat – the largest social communications platform in China with 1 billion+ MAUs. It is also the largest game developer and publisher in China.

Monetisation model. Kuaishou hosts a nationwide short video and live streaming platform with high user traffic through three apps, namely Kuaishou Flagship, Kuaishou Express and Kuaishou Concept. It primarily monetises its traffic via (i) sale of virtual gifts on live streaming, (ii) online marketing services and (iii) e-commerce, with revenue contributions of 62.2%/32.8%/5% respectively in 9M20.

9M20 Revenue breakdown by product segment (%)



Source: IPO Prospectus, DBS HK

Business partners. Kuaishou works with advertisers and advertising agencies in connection with its online marketing services. It also collaborates with various content business partners such as multi-channel networks (MCNs) game developers and knowledge-sharing content providers for enriching the platform content. In 2018, it started receiving commission from thousands of merchants after tapping into e-commerce.

Sector outlook

Mobile entertainment upgrade in China. Short videos and live streaming have become the fastest growing mobile entertainment format in China, thanks to 4G expansion, combined with the advantages of easier content creation and stronger user engagement. The rapid development of short video and live streaming is led by China. It has the world's largest user base in short video and live streaming, representing approximately 80%/50% of short form/live streaming platforms globally in 2019, according to iResearch. We believe further penetration of mobile internet and advancements in mobile infrastructure, particularly expansion of 4G and introduction of 5G, will continue to spur the growth of short video and live streaming. Percentage of China mobile internet users' average daily time spent online on short video and live streaming platforms is expected to reach 25.1% by 2025 from 15.6% in 2019.

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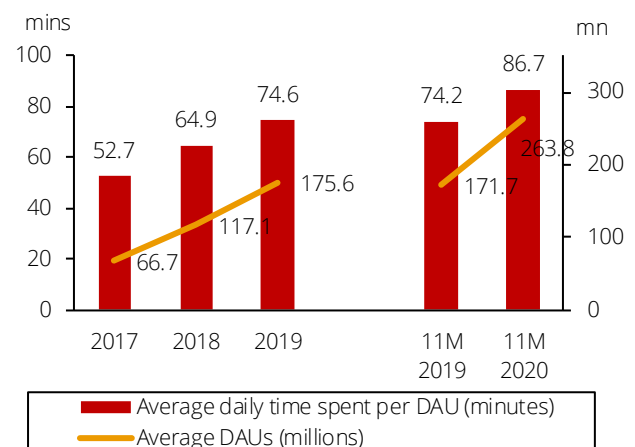
Multiple monetisation levers for video-based social platforms. Social platforms with features of short video and live streaming generally have more vibrant ecosystems, allowing real time user engagement over a wide range of topics. Virtual gifting and online marketing services are currently the initiatives adopted to monetise short video and live streaming platforms. New market opportunities from multiple industries such as e-commerce, online game, online education will eventually rise as user needs evolve. Platforms with stronger social attributes and interactions will give rise to stronger network impact and have higher potential of nurturing a trusted ecosystem, an essential factor in capturing monetisation opportunities.

Competitive strengths

First mover advantage in short video and live streaming. As the first mover in short video and live streaming social platforms, Kuaishou's DAU expanded at a CAGR of 62.3% in 2017-19, positioning it as one of the high traffic social platforms. Its continuous investment in technology ranging from video production to personalised recommendation engines further improved user engagement with an active user accessing the Kuaishou app more than 10 times a day on average, a similar level to WeChat, China's largest social messaging app.

Highly engaged user base with wide content variety. Different from its competitor, Douyin, Kuaishou initially focused more on social engagement in the early days. Its community sharing and social interactive features on its short video and live streaming platforms drove daily time spent per DAU to 86.7 mins as of November 2020 from 52.7 mins in 2017. Fostering community relationship among content creators and users also expanded the content base organically with over 1.1 billion average monthly short video uploads and over 1 billion average monthly short video uploads resulting in better user retention and wider content variety.

Kuaishou's average time spent per DAU and average DAU trend

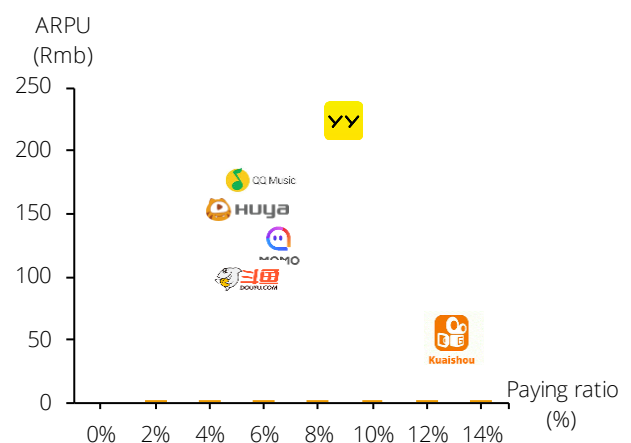


Source: IPO Prospectus, DBS HK

Solid social community circle across verticals

Kuaishou ranks number one in terms of interaction of its content community among the top video-based social platforms in China, with content creators constituting c.26% of average MAUs on Kuaishou app in 1H20 according to iResearch. Unlike other peers, Kuaishou tends to allocate traffic to a broad range of content creators instead of key opinion leaders or other popular celebrities to diversify its content. On the back of AI-based recommendation engine and social communication features, a wider content variety results in a more solid interest community with diversity, leading to better monetisation potential.

Live streaming paying rate and ARPU versus peers



Source: IPO Prospectus, DBS HK

Flash Note

Key drivers

Multiple growth engines: Live streaming, online advertising and e-commerce. Kuaishou has expanded its revenue stream through a variety of traffic monetisation initiatives, ranging from selling virtual gifts in live streaming, to online marketing and e-commerce. The robust platform traffic has led to rapid growth in online marketing business. Revenue contribution from online marketing has grown to 32.8% in 9M20 from 5% in 2017. In addition, Kuaishou started tapping into live streaming e-commerce since 2018 and is now the second largest live streaming e-commerce platform after Alibaba (9988 HK) in terms of gross merchandise volume (GMV) in 9M20.

Margin improvement with turnaround potential. We believe declining net profit trend is temporary as Kuaishou has been investing in brand promotions and technology, such as AI and big data, to solidify Kuaishou's leadership. Traditionally, net margin from online marketing and e-commerce segments are higher than the sale of virtual items in live streaming by c.10ppts. Margins should improve in 2021 from (a) rising contribution of higher-margin online marketing and e-commerce revenue and (b) decline in sales-and-marketing expense-to-sales ratio after its large-scale brand promotions made in 2020. We expect Kuaishou's earnings to turnaround by 2022 as it achieves greater operating efficiency and stronger brand recognition.

Financials

Highlights: Robust revenue growth with turnaround potential.

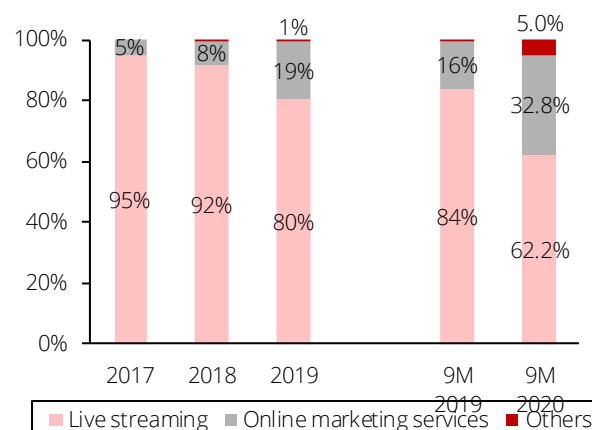
Kuaishou's revenue grew by 117% CAGR during 2017-19 to Rmb39,119m in 2019, mainly driven by increase in live streaming gifting (+99%; 80.4% of total revenue and online marketing services (+336%; 19% of total revenue).

In 9M20, revenue growth was at 49.2% y-o-y, while growth in live streaming and online marketing services are 104% and 213% respectively.

Its adjusted net profit margin contracted from 9.3% in 2017 to 3.4% in 2019, and fell to -17.8% in 9M20, as the result of investments in brand promotions and technology, such as AI, big data and softer advertising demand due to COVID-19. We believe such investments are necessary to increase the competitiveness of Kuaishou in the long run.

We expect Kuaishou's earnings to turnaround by 2022 supported by increasing contribution from higher margin online marketing and e-commerce segments benefiting from higher brand recognition, and achieving greater operating efficiency and economies of scale.

Revenue by segment (2017-2019, 9M19 VS 9M20)



Source: IPO Prospectus

Gross profit. Kuaishou's gross profit margin increased 4.8ppts to 36.1% in FY19 from 31.3% in FY17, due to rising contribution from higher-margin online marketing services. In 9M20, gross profit margin expanded by 2.9ppts to 37.6% due to a change in product mix favouring online marketing services.

Selling and marketing expenses. Kuaishou's selling and marketing (S&M) expenses primarily consists of promotion and advertising expenses. S&M expenses-to-total revenue increased by 8.8ppts to 25.2% in FY17-19, as the company made aggressive moves to raise its brand recognition, leading to expansion in user base and online marketing services. We believe S&M expenses as percentage of revenue will moderate ahead after the series of brand promotions done in 2020.

Net profit. The company's net loss contracted marginally from Rmb20bn in FY17 to Rmb19.7bn in FY19. Excluding amortisation of intangible assets from business acquisitions, share-based compensation expenses, fair value changes of convertible redeemable preferred shares, net fair value (gains)/losses on financial assets, adjusted net profit CAGR reached 31.7% over the same period. In 9M20, Kuaishou recorded net loss of Rmb97.4bn due to investments in S&M and technology such as AI and big data.

Financial position. Kuaishou held net cash of Rmb7,403m as of 9M20 (cash of Rmb7,703m less bank borrowings of Rmb300m) (Dec-19 net cash was Rmb3,996m). We forecast Kuaishou should remain in net cash position at Rmb40,442m after IPO, supported by proceeds of Rmb\$33,039m (assuming mid-point of IPO range and excluding the exercise of the over-allotment Option). The company does not have a pre-determined dividend payout ratio.

Flash Note

Summary data of cash flow and balance sheet

FY Dec (Rmb m)	2017	2018	2019	9M19	9M20
Net cash from operating activities	2,055	1,819	8,020	6,112	(768)
Net cash used in investing activities	(2,287)	(5,623)	(10,149)	(8,359)	(15,570)
Net cash from financing activities	2,358	6,033	698	(152)	20,067
Net change in cash	1,517	2,230	(1,430)	(2,399)	3,728
Cash beginning	1,301	2,689	5,370	5,370	3,996
Cash end	2,689	5,370	3,996	3,098	7,703
Non-current assets	2,052	5,696	15,103	20,639	
Current asset	5,641	10,783	17,311	30,880	
Non-current liabilities	27,348	48,142	72,770	56,369	
Current liabilities	29,879	52,184	88,143	143,492	
Total equity	(22,185)	(35,704)	(55,729)	(148,341)	

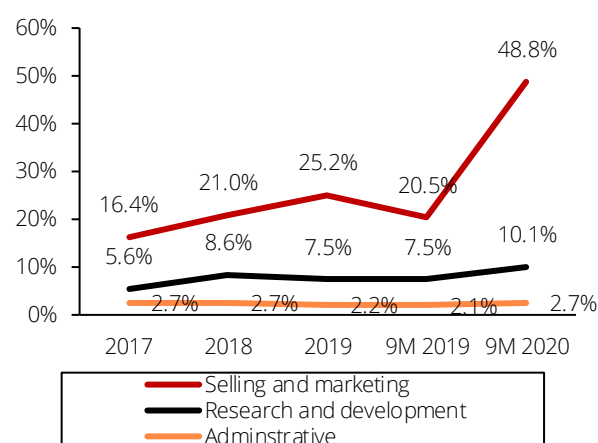
Source: IPO Prospectus

Use of proceeds

Assuming mid-point of the IPO price range, Kuaishou plans to raise net proceeds of HK\$39.5bn (US\$5.1bn), barring no over-allotment. The proceeds will be used as follows:

- 35% for enhancing Kuaishou's ecosystem
- 30% for technology investment
- 25% for merger and acquisitions
- 10% for working capital

Operating expenses trend

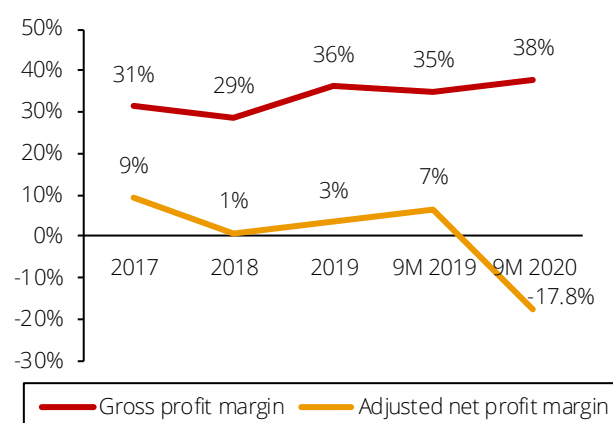


Source: IPO Prospectus

Key risks

Tightening regulatory policies. The PRC government has tightened its regulations in short video and live streaming industries in China over the past few years. The regulators such as State Council, Ministry of Industry and Information Technology, have the authority to issue and implement regulations governing various aspects in short video and live streaming. Licenses or approvals from regulators are required for business operations. Any failure in licence renewals or application approvals will have a negative impact on sales or even result in suspension of business operations.

Gross profit margin and net profit margin trend



Source: IPO Prospectus

Further outbreak of COVID-19. Since the outbreak of COVID-19, the government has implemented strict measures to control the outbreak in China, including business closures, transport bans, and workplace shutdowns. The travel restrictions resulted in the reduction in size or even cancellation of offline events, which temporarily adversely affected the company's marketing activities and businesses. It also led to regulatory approval delays due to government-imposed lockdowns and workplace closures. Any further material outbreak of COVID-19 will have a negative impact on sales as well as content in 2021.

Flash Note

Competition from well-funded competitors. The internet market is highly competitive, particularly in content-based social platforms, online marketing businesses and e-commerce platforms in China. Irrational subsidies from well-funded competitors will affect the profitability or even result in losses for Kuaishou.

Brand reputation. As Kuaishou's users rely on trusted social experiences broadcast on the platform, any inappropriate content or frauds or user misconduct will affect Kuaishou's brand image, leading to negative impact on sales and user engagement.

Peer comparison table

Company Name	Code	Currency	Price	Mkt Cap	Fiscal Yr	EPS growth		PE	PE	Yield	Yield	EV/EBITDA		ROE	ROE	PS	PS	PEG	PEG
						21F	22F					21F	22F						
Bilibili ADR 1:1	BILI	USD	127.8	44,402	Dec	n.a.	n.a.	n.a.	1300.5	0.0	0.0	(108.1)	111.2	(37.2)	(4.0)	16.7	12.3	n.a.	n.a.
Joyy ADR 1:20	YY	USD	90.88	7,360	Dec	35.5	31.4	16.2	12.4	0.0	0.0	9.9	7.3	6.0	7.9	1.7	1.4	0.5	0.4
Momo ADR 1:2	MOMO	USD	15.72	3,268	Dec	6.6	19.1	8.1	6.8	0.0	0.0	4.0	3.6	15.4	18.2	1.3	0.6	1.2	0.4
Tencent Msc.Entm. Gp.ADR 1:2	TME	USD	26.1	43,784	Dec	18.4	27.1	48.5	38.2	0.0	0.0	25.1	20.1	11.3	12.7	4.0	6.6	2.6	1.4
Alibaba Group Holding ADR 1:8*#	BABA	USD	265.49	718,319	Mar	36.3	48.9	163.5	109.8	0.0	0.0	166.9	122.4	19.6	21.5	4.9	3.6	4.5	2.2
Alibaba Group Holding*#	9988	HKD	265	92,490	Mar	34.0	48.1	19.6	13.3	0.0	0.0	21.8	15.6	21.0	22.9	5.0	3.7	0.6	0.3
Pinduoduo ADR 1:4*	PDD	USD	170.96	209,653	Dec	n.a.	69.7	91.8	54.1	0.0	0.0	88.0	49.1	53.5	52.7	4.1	3.4	n.a.	0.8
Jd Com 'A'*	9618	HKD	364.2	73,062	Dec	73.4	44.8	32.5	22.4	0.0	0.0	23.6	17.6	23.4	28.6	1.1	0.9	0.4	0.5
Jd Com ADR 1:2*	JD	USD	95.31	148,220	Dec	73.4	44.8	65.8	45.5	0.0	0.0	47.9	36.1	23.4	28.6	1.1	0.9	0.9	1.0
Facebook Class A	FB	USD	267.48	761,774	Dec	12.3	23.3	25.5	20.7	0.0	0.0	14.6	12.2	22.1	21.2	7.3	6.1	2.1	0.9
Snap 'A'	SNAP	USD	52.2	77,777	Dec	n.a.	173.0	227.0	83.1	0.0	0.0	123.3	52.2	(2.4)	17.8	22.3	16.5	n.a.	0.5
Twitter	TWTR	USD	47.6	37,859	Dec	n.a.	26.1	52.9	41.9	0.0	0.0	21.6	17.6	6.2	6.7	1.7	1.5	n.a.	1.6
Vipshop Holdings Sponsored Ads 5:1	VIPS	USD	29.83	17,742	Dec	23.3	14.9	18.5	16.1	0.0	0.0	11.1	9.6	21.9	20.8	1.0	0.9	0.8	1.1
Tencent Holdings*	700	HKD	679.5	840,942	Dec	39.8	15.3	29.7	25.8	0.3	0.3	22.7	18.4	36.5	38.4	9.1	7.4	0.7	1.7
Netease	9999	HKD	173	15,421	Dec	17.2	17.2	25.2	21.5	0.9	1.1	17.7	14.0	19.1	19.4	1.2	1.0	1.5	1.2
Netease ADR 1:5	NTES	USD	112.95	78,051	Dec	17.2	15.7	26.0	22.5	0.9	1.0	19.2	16.0	18.7	18.8	5.8	5.1	1.5	1.4
Iqiyi Ads 1:7	IQ	USD	21.14	16,563	Dec	n.a.	n.a.	n.a.	n.a.	0.0	0.0	(53.4)	31.8	(21.6)	4.3	3.2	2.8	n.a.	n.a.
Archosaur Games	9990	HKD	22.1	2,325	Dec	93.8	24.0	13.4	10.8	1.0	n.a.	9.8	7.5	34.6	29.9	4.4	3.3	0.1	0.5
Comge Technology Group	302	HKD	3.07	994	Dec	26.8	19.6	5.7	4.7	5.5	n.a.	4.8	4.1	20.3	21.2	1.2	1.0	0.2	0.2
Huya ADR 1:1	HUYA	USD	23.22	5,510	Dec	35.9	30.7	20.9	16.0	0.0	0.0	15.9	11.3	15.2	16.5	2.6	2.2	0.6	0.5
Douyu International Holdings ADR 10:1	DOYU	USD	12.69	4,029	Dec	57.0	32.9	18.7	14.1	0.0	0.0	7.0	4.8	15.8	17.4	2.2	1.9	0.3	0.4
Cheetah Mobile ADR 1:10	CMCM	USD	2	280	Dec	127.9	8.8	11.4	10.5	0.0	0.0	n.a.	n.a.	n.a.	n.a.	1.4	1.1	0.1	1.2
Spotify Technology	SPOT	USD	331.41	62,085	Dec	n.a.	n.a.	n.a.	n.a.	0.0	0.0	1566.9	286.0	(14.3)	(7.5)	5.3	4.4	n.a.	n.a.

FY21: FY22; FY22: FY23

Source: Thomson Reuters, *DBS HK

Flash Note

DBS HK recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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Sources for all charts and tables are DBS HK unless otherwise specified.

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