

Operator:

Ladies and gentlemen, good day everyone and welcome to Vipshop Holdings Limited's second quarter 2017 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 second quarter 2017 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 chief executive officer, and Donghao Yang, our chief financial officer. 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 2017 earnings conference call. We delivered robust operational results in the past quarter. Our total active customers for the trailing twelve months ended June 30, 2017 grew by 32% year over year, reaching 58.8 million. Further, our efforts to manage the lifetime value of both new and old customers are bearing fruit, as shown by the 7% year-over-year increase in average revenue per user in the second quarter.

We continued to add popular domestic and international brands to our platform to enrich our product offerings. Our daily average SKUs online increased to 2.7 million from 0.8 million in the second quarter of 2016. Further, as our global brand awareness continues to improve, more and more brands are keen to partner with us, giving us opportunities to help brands enter the China market.

We are also delighted to announce that we have made additional progress with our new Super VIP paid membership program. In the second quarter, we increased the number of trial members by ten times, and phase two test results continued to show major improvement in average revenue per user.

We are actively expanding our offerings for our customers. Recently, we selectively added some SKUs in the Vipshop life channel to increase cross sell, which we believe will drive increased shopping frequency and average spend on our platform. We intend to grow this new

category gradually, and therefore, do not expect it to meaningfully impact our growth and profitability in the near future.

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 second quarter of 2017, we made solid progress in a number of our strategic initiatives, particularly in the exploration of the Internet finance spin-off and the enhancement of our logistics capabilities. Additionally, excluding impact from the Internet finance business, our free cash flow for the trailing twelve months ended June 30, 2017 improved significantly year over year, from a free cash outflow of 93.3 million to a free cash inflow of 1.96 billion.

During the second quarter, we added four local warehouses in a number of strategic locations, namely Nanning, Urumchi, Jinan, and Harbin, China. This brings our total number of local warehouses to eleven, in addition to our five regional warehousing centers. In the past quarter, we also expanded our warehousing space home and abroad. Currently, we have approximately 2.2 million square meters of warehouses total, of which 1.4 million square meters are owned by our company.

We added around 4,000 last mile delivery staff and around 700 delivery stations in the second quarter, bringing the total number of delivery staff to approximately 27,000 and the total number of delivery stations to approximately 3,500. We delivered 95% of our orders through our proprietary last mile network in the second quarter, up from 91% in the prior year period. Our national delivery footprint is a critical component of our overall ecosystem, which will continue to improve our logistics efficiency, increased our customer satisfaction, lower our cost, and drive our long term growth.

Earlier this year, we announced that our Board of Directors authorized for us to explore a proposed spin-off of our Internet finance business into a dedicated entity, aiming to improve our cash flow and strengthen our earnings. We are pleased to announce that we have officially launched the spin-off of the Internet finance business, which initiated a Series A financing in the second quarter.

Operationally, our Internet finance business is delivering solid results as well. In the second quarter of 2017, 4.4 million active customers used our consumer financing products, representing a 179% increase from 1.6 million in the prior year period. As of June 30, 2017, the total balance of credit outstanding to customers was around 3.3 billion RMB and the total balance of credit outstanding to suppliers was 823 million RMB. While this new business is growing extremely fast, we are pleased to see that our over 180 days default rate remains very low.

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 2017 increased by 30.3% to 17.52 billion, primarily attributable to a 22% year-over-year increase in the number of active customers to 28.1 million and a 23% year-over-year increase in total orders to 84.8 million.

Gross profit for the second quarter of 2017 increased by 19.1% to 3.86 billion, primarily driven by the expanding scale of the business. **Gross margin** for the second quarter was 22.0% as compared with 24.1% in the prior year period, primarily attributable to our investment in promotional activities for market share gain.

- **Fulfillment expenses** for the second quarter of 2017 were 1.64 billion, as compared with 1.15 billion in the prior year period, primarily reflecting an increase in sales volume and number of orders fulfilled. As a percentage of total net revenue, fulfillment expenses were 9.4% as compared with 8.6% in the prior year period, primarily attributable to our expansion to support an increase in our last mile business outside of the Vipshop platform.
- **Marketing expenses** for the second quarter of 2017 were 752 million, as compared with 672 million in the prior year period, reflecting our strategy to strengthen our brand awareness, attract new users, and expand our market share. As a percentage of total net revenue, marketing expenses decreased to 4.3% from 5.0% in the prior year period, primarily attributable to our strategic balance between promotional activities and our broader marketing efforts.
- **Technology and content expenses** for the second quarter of 2017 were 448 million, as compared with 392 million in the prior year period, reflecting our continuing efforts to invest in human capital, advanced technologies, and our Internet finance business. As a percentage of total net revenue, technology and content expenses decreased to 2.6% from 2.9% in the prior year period.
- **General and administrative expenses** for the second quarter of 2017 were 579 million, as compared with 434 million in the prior year period. As a percentage of total net revenue, general and administrative expenses were 3.3% as compared with 3.2% in the prior year period, primarily attributable to an increase in share based compensation as well as the impact from building out our Internet finance business.

Our **income from operations** was 622 million for the second quarter of 2017. **Operating margin** was 3.5% as compared with 4.8% 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 6.0% to 888 million from 837 million in the prior year period. Non-GAAP operating income margin was 5.1% as compared with 6.2% in the prior year period.

Our **net income attributable to Vipshop's shareholders** for the second quarter of 2017 was 386 million as compared with 452 million in the prior year period. **Net margin attributable to Vipshop's shareholders** was 2.2% as compared with 3.4% in the prior year period. Net income per diluted ADS was 0.64 RMB as compared with 0.76 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, and amortization of intangible assets

resulting from business acquisitions and equity method investments, increased by 7.5% to 728 million from 678 million in the prior year period. **Non-GAAP net margin attributable to Vipshop's shareholders** was 4.2% as compared with 5.0% in the prior year period. Non-GAAP net income per diluted ADS increased to 1.18 RMB from 1.12 RMB in the prior year period.

As of June 30, 2017, our company had cash and cash equivalents and restricted cash of 4.20 billion and held-to-maturity securities of 343 million. For the second quarter of 2017, net cash used in operating activities was 0.27 billion.

Looking at our business outlook for the third quarter of 2017, we expect our total net revenue to be between 14.9 billion and 15.4 billion, representing a year-over-year growth rate of approximately 24% to 28%.

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.