

## Baidu, Inc.

October 27, 2015

### The Quarter Can Be Overwhelmed by O2O Initiatives; Maintain BUY Rating but Lowering PT

We believe BIDU almost has no alternatives but to invest in food delivery as well as group-buy business in order to overcome constrains of its past success in PC search, which is that BIDU does not require users to register. In the mobile era, its peers Tencent (700-HK, HK\$149.10 – Intraday, Not Rated) captures millions of mobile users with its communications tools, mobile QQ and WeChat, and Alibaba (BABA, \$79.71, Buy) with its Alipay while BIDU had nothing to accomplish such task. In the PC era, the internet entry point can be search but in the mobile era, it has become the individual mobile user. We believe that with BIDU's rich cash position, map, data and its determination, there is a chance that food delivery and group-buy can enable the company to accomplish such goal. Therefore, while we believe 3Q15 earnings can be overwhelmed by these newer initiatives, the level of uncertainties has already been mitigated, in our opinion. As such, we maintain our Buy rating but lower our price target to \$187 from \$239. BIDU will report 3Q15 results on Thursday, October 29th after the close of the market followed by an 8pm EST conference call.

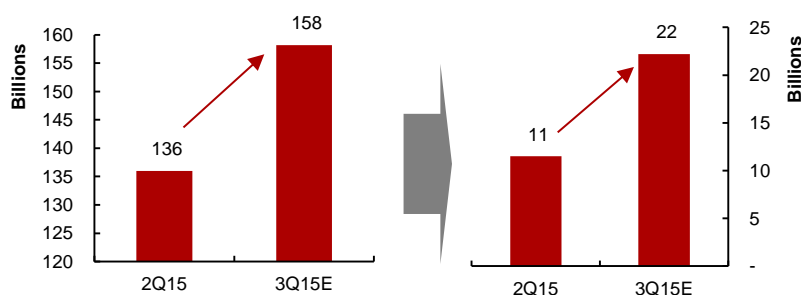
- Expect 3Q15 revenue to be at least in line with consensus** – We believe BIDU is likely to report 3Q revenue results in line with the Street at RMB18,393.1M driven by stable PC search, strong mobile search as well as its new O2O initiatives. We do not expect any upside surprises to its revenue in 3Q due to the slowdown in China's overall economy and slowing internet finance sector compared to prior quarters as well as possible less ad budgets due to market consolidations. In terms of the bottom line, due to the expected increase in sales & marketing spend, we do not see any upside to the bottom line and believe EPS is likely to be in line with the Street at RMB7.23.

3Q15	Guidance	Consensus	TH Capital
Revenue	RMB18,170M – RMB18,580M	RMB18,393.1M	RMB18,371.3M
GAAP EPS		RMB7.23	RMB7.24

- Please see page 2 for valuation and risks.

For the full version of this note, please contact TH Capital.

Figure 1: Cumulative downloads (LHS) and newly added downloads (RHS) of BIDU's mobile app store, 2Q15 – 3Q15E



Source: T. H. DATA (www.thdata.com)

**BIDU: Buy**

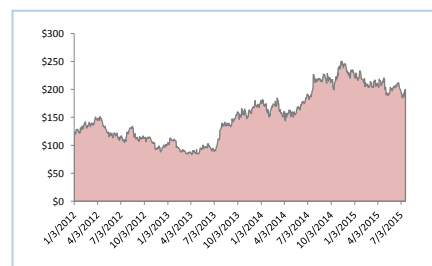
**Price: \$170.86 (Intraday)**

**Target Price: \$187.00 (was \$239.00)**

52 Week Range:	\$251.99 - \$100.00
Market Cap:	\$60.1B
Avg. Daily Vol. (100 day):	4,970,930
3-Yr. Est. EPS CAGR:	24%
Net cash per share:	\$18.20

FY (Dec)	2014A	2015E	2016E
Q1	\$1,528A	\$2,053A	\$2,799E
Q2	\$1,932A	\$2,673A	\$3,428E
Q3	\$2,203A	\$2,890E	\$3,767E
Q4	\$2,265A	\$2,976E	\$3,914E
Revenue*	\$7,906A	\$10,476E	\$13,908E
Previous Rev.	N/A	\$10,834E	\$14,711E
Q1	\$1.16A	\$1.09A	\$1.15E
Q2	\$1.63A	\$1.64A	\$2.00E
Q3	\$1.79A	\$1.14E	\$2.17E
Q4	\$1.45A	\$0.93E	\$2.16E
GAAP EPS	\$6.01A	\$4.74E	\$7.49E
Previous EPS	N/A	\$7.44E	\$10.31E
P/E	28.5x	36.1x	22.8x

\* Indicates total revenue including sales tax; Quarters may not add due to currency conversion All figures in millions unless otherwise noted



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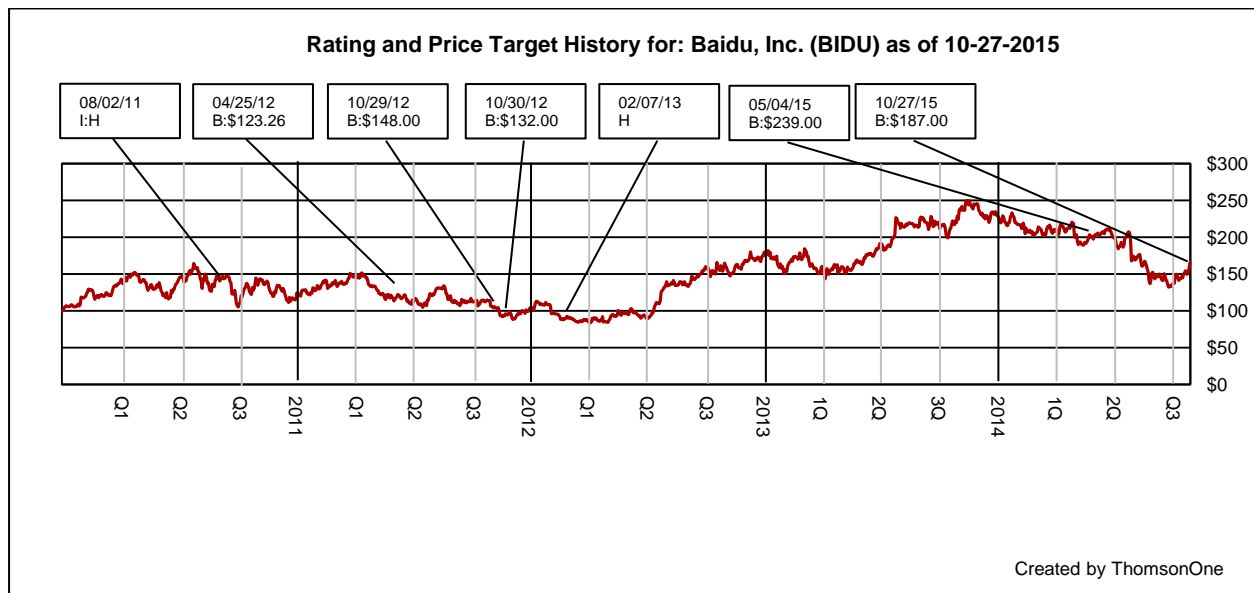
- **Maintain BUY** – We maintain our Buy rating but lower our price target to \$187 from \$239. Our new price target of \$187 is based on a 23X PE multiple to our new 2016 non-GAAP EPS estimate of \$8.14. The 23X PE multiple, we believe, can be supported by the average growth rate of its earnings in three years from 2015 – 2017 at 24%. We believe such multiple can be conservative compared with its historical 12-months forward PE at 26X. The stock is currently trading at an 18.0x PE multiple to our 2016 non-GAAP EPS estimate of \$8.14.
- **Risks** – 1) Mobile search revenue may not ramp up as rapidly as the company expected; 2) Possibilities of failure in O2O business; 3) Losing its edge in mobile search if WeChat's search takes off; 4) PC monetization declines faster than expected; and 5) Macroeconomic slowdown in China.
- **Dial-in information** – BIDU will report 3Q15 results on Thursday, October 29th after the close of the market with an 8pm EST conference call, which can be accessed by dialing (845) 675-0437 with the passcode 59702295.

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