

## Baidu, Inc.

October 23, 2017

### The Business Is Turning For the Better; Upgrade To BUY With A Price Target of \$290.00

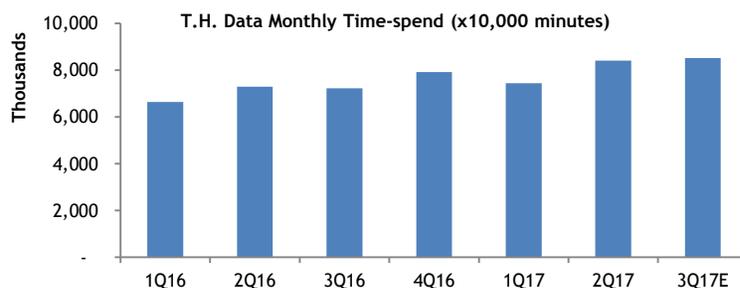
BIDU is at a turning point in its business. The company has established its new strategy – all in AI, which we believe has played into BIDU’s strength. BIDU now has all it needs to become a leader in AI applications in China. For its upcoming 3Q17 earnings report on Thursday (October 26th after the market closes followed by an 8pm EST conference call), based on our data and calculations, we believe BIDU is likely to deliver 3Q17 top line at RMB23.683B, at least in line with or slightly higher than consensus at RMB23.547B; its guidance is between RMB23.130B – RMB23.750B. The better performance is driven by iQiyi video views that remained at a high level; b) its news feed business is performing well, and 3) margins can be better as its investment in O2O has been stalled. BIDU is making changes in the right direction and we have already seen results. As such, we upgrade the stock from HOLD to BUY with a price target of \$290.00.

- **Expect at least in line 3Q17 topline** – Based on our data and calculations, BIDU’s total revenue is likely to be RMB23,683M, at least in line with or slightly better than consensus at RMB23,547M (29.0% Y/Y growth). Based on our proprietary data: 1) total monthly time-spend on Baidu increased 17.9% Y/Y to 85.2B minutes in 3Q17E (*Figure 1*). The total monthly unique devices reached 396.9M in 3Q17E, an increase of 14.0% Y/Y, and total monthly uses reached 7.5B in 3Q17E, an increase of 16.1% Y/Y (*Figure 2*); 2) iQiyi video views grew significantly - in 3Q17E, the total actively viewed contents increased 37.5% Y/Y to 17,314, and the average daily video views increased 14.9% Y/Y to 1,384M (*Figure 3 & 4*); 3) mobile products downloads increased Q/Q - for BIDU’s own apps products, newly added downloads increased 57% Q/Q and 22.4% Y/Y to 2.3B in 3Q17E; including video apps at 740M, Search apps at 613M, Map and Navigation apps at 326M, Tools apps at 236M, App Store apps at 221M and Security apps at 25M (*Figure 5*). For the bottom line, we believe EPS is likely to be at least in line with or slightly better than consensus at RMB10.77.

- Please see page 2 for a discussion of risks and valuation.

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

Figure 1: Baidu Search - Monthly Time-Spend by Minutes, 1Q16 – 3Q17E



Source: iResearch and T.H. Data (www.thdata.com)

**BIDU: Buy (was Hold)**

**Price: \$264.90**

**Target Price: \$290.00**

**52 Week Range: \$159.54 - \$274.97**

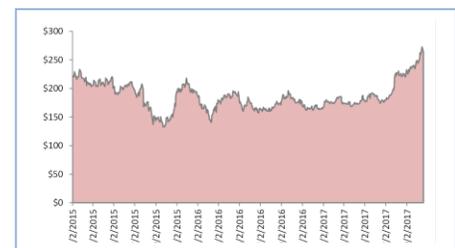
**Market Cap: \$91.9B**

**Avg. Daily Vol. (100 day): 2,995,490**

**Net cash per share: \$33.40**

FY (Dec)	2016A	2017E	2018E
Q1	15,821A	16,891A	20,511E
Q2	18,263A	20,874A	24,854E
Q3	18,253A	23,536E	28,844E
Q4	<u>18,212A</u>	<u>22,829E</u>	<u>30,259E</u>
Revenue*	70,549A	84,129E	104,469E
Q1	5.38A	4.63A	6.05E
Q2	6.57A	11.31A	12.08E
Q3	8.51A	10.73E	16.53E
Q4	<u>11.40A</u>	<u>9.78E</u>	<u>18.43E</u>
GAAP EPS	31.86A	36.44E	53.10E
P/E	57.7x	49.3x	33.8x

\*Indicates total revenue including sales tax.  
All figures in RMB millions unless otherwise noted



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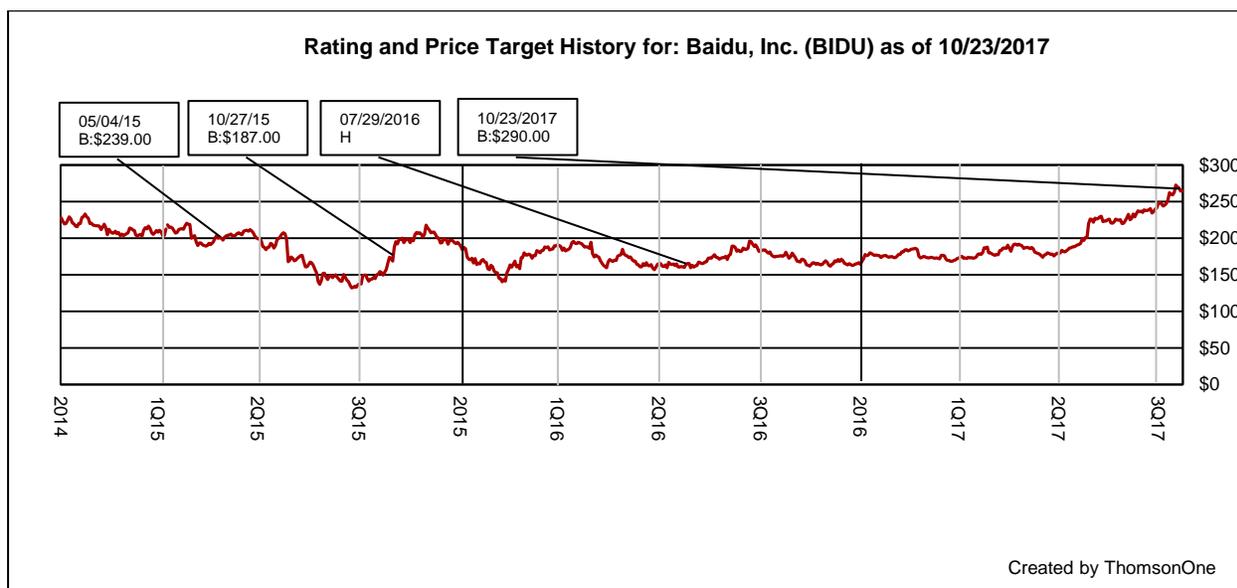
- **Upgrade to Buy from Hold rating** – BIDU is at a turning point in its business. BIDU has established its new strategy – all in AI, which we believe has played into BIDU's strength and the company has all it needs to become a leader in AI applications in China. While we haven't seen meaningful monetization from AI initiatives (besides in finance), we believe that in the China market, BIDU has all it needs to lead the AI market. We apply a 25.3X PE multiple to our 2019 EPS estimate of \$11.47 and come out with price target at \$290.00.
- **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; 6) AI market fails to take off.
- **Dial-in information** – BIDU will report 3Q17 results on Thursday, October 26th after the markets close followed by an 8pm EST conference call, which can be accessed by dialing (845) 675-0437 with the passcode 98359218.

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