Q3 2019 Earnings Call

Company Participants

- Jia Dong, Investor Relations Associate Director
- Lei Xu, CEO, JD Retail
- Richard Liu, Chairman & Chief Executive Officer
- Sidney Huang, Chief Financial Officer
- Zhenhui Wang, CEO, JD Logistics

Other Participants

- Alicia Yap, Analyst
- Eddie Leung, Analyst
- John Choi, Analyst
- Natalie Wu, Analyst
- Ronald Keung, Analyst
- Thomas Chong, Analyst
- Tina Long, Analyst

Presentation

Operator

Hello, and thank you for standing by for JD.com's Third Quarter 2019 Earnings Conference Call. At this time, all participants are in a listen-only mode. After management's prepared remarks, there will be a question-and-answer session. Today's conference is being recorded. If you have any objections, you may disconnect at this time.

I'd like to turn the meeting over to your host for today's conference, Jia Dong.

Jia Dong {BIO 16469954 <GO>}

Thank you, and welcome to our third quarter 2019 earnings conference call. Joining me on the call today are Mr. Richard Liu, JD.com Group CEO; Mr. Lei Xu, CEO of JD Retail; Mr. Zhenhui Wang, CEO of JD Logistics; Sidney Huang, CFO; and Jon Liao, our Chief Strategy Officer.

For today's agenda, our CFO, Sidney Huang, will discuss highlights for the third quarter 2019 followed by Richard Liu, our CEO. Other managements will join the Q&A session.

Before we continue, I refer you to our Safe Harbor statement in the earnings press release, which applies to this call as we will make forward-looking statements. Also, this call includes discussions of certain non-GAAP financial measures. Please refer to our earnings release, which contains a reconciliation of non-GAAP measures to the most directly comparable GAAP measures. Finally, please note that unless otherwise stated, all figures mentioned during this conference call are in RMB.

I would now like to turn the call over to our CFO, Sidney Huang.

Sidney Huang {BIO 20098238 <GO>}

Thank you, Jia. Hello, everyone. Thank you for joining us today.

We are very pleased to report another strong set of results for the third quarter 2019. Our net revenue growth continued to reaccelerate, reaching 28.7%, the highest growth rate in the past five quarters, driven by our lower tier city penetration strategies. In particular, the growth rate for electronics and home appliance categories in lower-tier cities was more than double that of Tier 1 and Tier 2 cities. And most other top 25 categories saw higher and accelerated growth rates in lower-tier cities as well. Overall, over 70% of new customers in Q3 came from lower-tier cities, which is a new record, and the growth rates for both purchase orders and GMV in lower-tier cities reached the highest levels in the past six quarters.

In terms of traffic, due to innovative marketing activities and better user engagement through our upgraded mobile interface, the JD mobile MAU grew 36% in September, the highest growth rate in the past eight months, while our mobile DAU grew 35% in Q3, the fastest in five quarters. This may surprise some people who are not familiar with China's lower-tier city consumers and think they are only interested in low priced, low quality products, which have seemingly flourished on other platforms. The reality is that consumption upgrade has been quietly occurring in these regions where average consumers may have relatively lower absolute income, but have somewhat similar or even higher disposable income than Tier 1 city residents due to significantly lower housing costs. As these consumers learned to shop online, they gradually discovered the different value propositions unique to different e-commerce platforms.

For JD.com, our obsession with customer experience since day one continued to help us to win over the better half of middle class consumers even in those lower-tier cities. It is a universal truth that middle class customers value quality assurance, everyday low prices and first-class services, especially for high-value products such as 3C and home appliances or products where consumers pay particular attention to the quality such as food, baby products, home furnishings, cosmetics and healthcare products. For that we thank our competitors for not only introducing e-commerce to many first-time users, but also providing easy benchmarks for us to readily differentiate and secure the most valuable customers. This can be validated by our average ticket size of over RMB200 in lower-tier cities, very important indicator for the quality and sustainability of our customer base.

Thanks to lower-tier city consumers, our market leading position in the electronics and home appliance categories has been further strengthened with the revenue growth rate accelerating to 22% in the third quarter, the fastest in the past five quarters amid everlasting competition and a slowing industry which grew in low single-digits in Q3 according to China's National Bureau of Statistics. In other words, we have been taking tremendous market share during the quarter.

Some of you may wonder what happened to all the subsidies that people have been raving about from our competitors. Well, this time our arch rival itself confirmed publicly that subsidies cannot bring sustainable business. This it has learned the hard way from its own costly experience over the years. Hundreds of millions of people may happily spend RMB0.99 on an impulse and they may spend RMB0.99 every day on petty items just for fun.

But for serious purchases, most consumers don't just look at price alone. They will evaluate at least two other elements before any large purchase decisions. The first is trust. Can I trust the sellers on the platform? Are you selling authentic products? Will I get what I see or will I end up on a wait list for months before getting that discounted item? The answers are mixed at best on the overcrowded marketplace platforms.

The second is service. Do you have professional in-store service for large appliances, and I'll return it easily if I don't like the product. People may not care about a service when they buy a RMB0.99 petty item because they can just throw it away. But when they are buying large ticket products, they definitely care.

Here comes the hard truth. It takes years of heavy-lifting to build the supply chain expertise, service capabilities and fulfillment infrastructure needed to perfect the customer experience in those categories and in that process to optimize operating efficiency while solidifying our competitive moat. The best example is, three years ago, when the largest marketplace platform listed the largest offline home appliance and electronics retailer in China to jointly attack us with massive subsidies throughout the past three years. But they have failed rather miserably as we predicted three years ago, now widely reported in the Chinese press. So anyone still worrying about subsidies hurting our core categories should refresh their memory and think again. It's driven by the same retail fundamentals that we have reiterated all these years. There is no shortcut in this business.

By the same token, our general merchandise categories enjoyed accelerated growth of 36% in Q3, led by FMCG products, another extremely difficult category for pure marketplace operators to reach meaningful scale with or without significant subsidies.

We are also pleased to see that net service revenue grew 47% year-over-year, the fastest in the past four quarters, and contributed 11.9% of our overall revenues, driven by strong momentum from third-party logistics and advertising revenues. External revenue has now contributed 40% to JD Logistics' total revenues on a stand-alone basis, up from less than 20% just two years ago. It has grown more than 300% from the same quarter of 2017 when we decided to expand logistics into a self-sustaining business, supported by its consistently top-ranked customer satisfaction scores in the industry.

In the third quarter, our gross margin was 14.9% compared to 15.4% in the same quarter last year. This reflects the reinvestment of the first half one-time gains that I mentioned on our last earnings call. Yet, we have reinvested roughly 40% of the RMB1.8 billion non-recurring gains from the first half through the gross margin in Q3 to drive our lower-tier city strategy. It worked very well, and you have to admit it's a much more effective strategy than the massive subsidies by some of our peers.

The higher sales we achieved will give us further economies of scale in both procurement and operating efficiency, which will afford our customers even more pricing benefit, setting an even higher bar for competitors while driving our further growth and margin expansion next year. This is the beauty of our 1P business model, a self-reinforcing virtuous cycle that has worked extremely well for all the number one third-party retailers either by country or by category around the world. You have to be number one to enjoy this virtuous cycle and you have to have a lower cost structure than everyone else. JD.com is number one in China and in multiple categories and the snowball is just beginning to roll.

Another aspect of the snowball effect is operating leverage. During the third quarter, our fulfillment expense ratio improved by 91 basis points to 6.5% compared to 7.4% in the same quarter last year. The improvement was driven by economies of scale as JD Logistics expanded its external order volume rapidly enabling both its 3P operating margin and JD's 1P procurement expense ratio.

Our marketing, R&D and G&A expense ratios also improved meaningfully in the same quarter, driven by highly effective management and operating leverage from higher sales. As a result, non-GAAP operating margin reached 2.2% in the third quarter, setting a new record. JD Retail, in particular, achieved a record segment operating margin of 3.3%, and it was achieved in a quarter of heavy reinvestment. I hope this solid performance can begin to shed light on our path to our committed high single-digit long-term profit margin for the JD Retail business.

Our free cash flow also increased significantly year-over-year during the quarter, driven by lower CapEx and the proceeds from the phase one closing of the GIC logistics Core Fund. In our free cash flow table, as I mentioned in recent quarters, this JD Logistics, JD Property Management Group was formed to pursue financial returns as separately [ph] managed business. We have broken out related CapEx into a separate line specifying the available for sale nature, which has been reported net of related proceeds on the sales. This is the second time when we recorded a net cash inflow on this line following the first time in Q1 this year. We hope to see more cash inflows from this business in the future. For the trailing 12 months, our free cash flow was RMB15.6 billion, 50% higher than our non-GAAP net income in the same period, which was another bright spot in our business.

Now let's discuss our fourth quarter financial outlook. We expect net revenues to grow between 21% and 25% on a year-over-year basis in light of a highly successful Singles' Day promotion season, while taking into account the potentially slowing national retail sales growth based on the NBS report published yesterday.

On the bright side, our October growth remained resilient and we are clearly gaining market share. Finally, with the better than expected earnings in the third quarter, we are raising the full year non-GAAP net income guidance to be between RMB9.8 billion and RMB10.5 billion, reflecting Q4 seasonality and the continued reinvestment of the first half one-time gains discussed earlier. At the midpoint of this guidance, we would grow our 2019 non-GAAP net income by over 200% from the 2018 level and grow at CAGR of 43% from the 2017 level.

More importantly, this robust earnings growth is on top of our ongoing reinvestment in our core business, which positions JD.com to enter 2020 with tremendous growth momentum.

This concludes my prepared remarks, and I will now turn the call to Richard for a few quick remarks.

Richard Liu {BIO 17167866 <GO>}

(Foreign Language) Thank you, Sidney. Hello, everyone. I would like to take this opportunity to give you a brief introduction on our strategy plan in 2020. And for this year, as you have seen that we have achieved promising results in terms of our revenues, net margin, as well as free cash flow. And for the next year, based on the achievement of the previous three factors, we will continue to work on increasing our GMV customer base as well as technology services. And we believe that only by improving every aspect of the six aspects elements, we'll achieve full quality growth of the whole company.

(Foreign Language) And in the past six years, we have been invested heavily on technology services, and this has been quite larger than the growth of our revenues. And we will -- and for this year, you have seen significant growth on the revenues of our technology services, and we have [ph] actually achieved three-digit growth this year. For the next five years, (Foreign Language) we (Foreign Language): our technology services revenue growth will continue to out pace our total revenue growth. And we believe the technology services revenue will be the key engine for the increase of our revenues and net income.

(Foreign Language) We have two strong beliefs. And no matter, at our JD Retail, Logistics and JD Digits, the technology is our key driving forces. Only through technology will bring us a long-term core competitiveness.

(Foreign Language) Technology will always help us to bring up our users' experience, lower the costs and improve our operating efficiency.

(Foreign Language) And the second belief is that we strongly believe the income from technology services will bring even further benefits and returns and profits for our stakeholders.

(Foreign Language) And overall, we believe for the next year, no matter it's on the revenues and/or the profits, we will achieve even better results.

Thank you, everyone.

Sidney Huang {BIO 20098238 <GO>}

We can now move to the Q&A session.

Questions And Answers

Operator

The question-and-answer session of this conference call will start in a moment. (Operator Instructions) Your first question comes from the line of Ronald Keung from Goldman Sachs. Please ask your question.

Q - Ronald Keung {BIO 15432736 <GO>}

Thank you. Thank you, Richard, Xu Lei, Wang, Jon, Sidney Huang [ph] and Jia. Very strong results and further accelerating of revenue, particularly for the 1P retail and profitably. So would love to hear just your thoughts, particularly as Richard talked about the 2020 strategy. Just what do we see as the positive and maybe less positive drivers just into the 2020 1P growth? I can think of a larger base, I can think of 5G. So anything that you see are the drivers for next year's 1P growth, particularly for electronics appliances and FMCG? My sense is mostly whether we are targeting a similar growth as last year, sort of above 20%. Any color on that would be great. Thank you, management.

A - Lei Xu {BIO 21705778 <GO>}

(Foreign Language) Xu, Lei of JD Retail. Let me -- just to give you two reasons for the positive development of our 1P business. First, JD's retailing company, based on the capacities of our very strong supply chain, no matter in the past, now or in the future, we will continue to improve our ability on the supply chain and working together with our partners to increase our efficiencies and lower the cost on the supply chain side to provide unique advantages to this market.

And secondly, we attach great importance to users' experience, and we believe as a retailer ensuring users' [ph] experience is a must and for this year we have done a lot of work overall across the company to ensure the enhancement of users' experience. And through our NPS monitoring, we have seen users' experience has very tangible progress. And we are continuing our investments on improving the users' experience not only on the new customers and also our existing customers, we are looking on every front to ensure they have unique experience shopping on our platform. So in all, supply chain and our commitment to our users' experience has ensured our 1P business' fast development.

Q - Ronald Keung {BIO 15432736 <GO>}

Thank you.

Operator

Your next question comes from the line of Eddie Leung from Bank of America. Please ask your question.

Q - Eddie Leung {BIO 15234642 <GO>}

Hi. Good evening, guys. Thank you for taking my questions. Two quick questions about the lower-tier city competitions. Number one, about the users. I'm just wondering are we seeing similar users using different apps, but buying different products? Or are we seeing a more unique user segment that's coming to JD? And then secondly, how our cooperation with Weixin and the offline retail partner network can help us in the competition in the lower-tier cities? Thank you.

A - Lei Xu {BIO 21705778 <GO>}

(Foreign Language) Since our Jingxi platform, which is mainly the new channel we target the lower-tier city customers, has been introduced online by the end of October, and so it has been less than two weeks since live online, so based on the current results I would just share a few observations.

(Foreign Language) And for the Jingxi platform, it includes two access points. One is the first-level one entry point on WeChat and another is the stand-alone app we introduced a month ago.

(Foreign Language) The characteristics of the users on Jingxi, the majority of them are coming from the lower-tier cities and their shopping behavior, it's more a social e-commerce and have a very high conversion rates. But in terms of their average ticket size, ARPU, it's relatively low compared to the main site.

(Foreign Language) And in terms of the product, Jingxi platform product is quite different from our main site. On JD's main site, the products is mainly brand products. On Jingxi platform, we are developing products based on China's strong manufacturer potential, now we're working with over a hundred of industrial belts [ph] and in the future it's going to develop into 1,000 industrial belts, to identify the high quality manufacturers and help them to bring products on those Jingxi platform to reach out to the customers from the lower tier cities.

(Foreign Language) And also we realized the Jingxi users, their shopping preferences is rather complicated. They like to be more interactive and having more [ph] entertainment factors in their shopping behavior. It's not rather a very simple buying habit. So by using these features, we will work on our own progress as well as WeChat module functions [ph]to enhance their buying behaviors on our platform.

(Foreign Language) We also want to share with the development and expansion of JD platform, we've also identified the quality products and for instance, who have very premium service ability to give them more presence on our main site and we believe there is a group of lower-tier city customers that are also having the willingness and need to shop on the main site in the long run.

(Foreign Language) And I just want to respond a little bit more on our relationship with Tencent. Tencent is our shareholder and very important partners. And some of you have realized, at the end of October, WeChat has made certain rules to prevent some over-promotional activities to impact the social interaction behaviors on WeChat. And these rules I think for the long-term is a good sign, because for us, we always emphasize on the users' experience, and this will help us to guarantee these aspects.

A - Sidney Huang {BIO 20098238 <GO>}

So I just add one more point on Eddie's first question, whether users are -- lower-tier city users are buying from different apps for different categories or just stick to one app. Our survey before we got more data from Jingxi, our survey in the lower-tier cities suggest that majority of the lower tier city users do use multiple apps from -- basically use multiple platforms and they will pick the platform based on the categories they are buying. So that's the current observation.

In the Tier 1, Tier 2 cities, you may see relatively more users stick to one app for majority of their purchases. Now, with our Jingxi application, basically we are creating a dual-brand strategy where our main app, JD app, will continue target the higher income consumers in the lower-tier cities, while the Jingxi app will target the relatively lower income customers in those regions, and we can also then gain more insight on the lower-tier city consumers so that we can better target them for promoting our JD main app our core category of products.

Q - Eddie Leung {BIO 15234642 <GO>}

That's very helpful. Thank you, guys. See you soon.

A - Sidney Huang {BIO 20098238 <GO>}

You're welcome.

Operator

Your next question comes from the line of Alicia Yap from Citigroup. Please ask your question.

Q - Alicia Yap {BIO 15274658 <GO>}

Hi, good evening, management. Thanks for taking my questions and congratulations on the strong set of results. My questions is related to your C2M initiative on the appliance brands. What are some of your differentiator on attracting the brands to partner with JD? And given the C2M model is also getting more competitive, if competitors going after the same brands, will that have any negative impact to JD margins? And for the -- related question is that for the same appliance brands, is the C2M SKU has a higher or lower margin than the standardized SKU? If you could share also roughly the percentage of GMV coming from C2M category this quarter and how much you expect that to grow into? Thank you.

A - Lei Xu {BIO 21705778 <GO>}

(Foreign Language) Let me share with you some and achievements that we have made on C2M so far.

(Foreign Language) Two to three years ago, we have started our C2M model, and this started in the categories of IT products and have achieved amazing success. And on these IT categories, actually on our platform over 70% of products are C2M through JD, and these has not only impacted our platform, but actually have a quite deep influence to the China's IT industries, online and offline.

(Foreign Language) And for this year, we have also made our strategic proposals through further categories, especially on the two categories on home appliances and FMCG products.

(Foreign Language) And compared with other online platforms, I believe there are two advantages to produce C2M products on JD platform. First of all, we are a company driven by technologies. We have a vast data in returns of our users' comments and searching and viewing data, and combining all these data and working together with our partners will help us to generate the most tailor-made products in a timely manner.

(Foreign Language) And secondly, per se, JD is a retail platform and especially our 1P business, so this give us advantage to work closely together with our brand partners together on producing those C2M products. And in between, we have our capacities and the supply chain. These give us better responsibility and the capacity to produce the most effective product together with the partners, and the partners will become more and more willing to work with us to reach success.

(Foreign Language) And so we have realized that for different categories and industries, the purpose to produce C2M products will be different and some of them are doing C2M products to avoid price conflicts. And by doing C2M and more tailor-made products will help them to reduce the complex -- conflict opportunities. And for some other brand partners, they want to go deeper into China's market to the lower-tier cities, and we know that based on our traditional supply chain, this is not an easy way. And for JD, we would like to be the company on this process with our partners to together reach new users in the lower-tier cities together. That's why, based on our powerful supply chains, it will be very unique opportunity for the partner -- for our brand partners to work with us to be more attractive with our customers in the lower-tier cities.

(Foreign Language) And in terms of the margins, because different brands have different goals and different formats, it's very difficult to give a unified measurement. But generally speaking, the C2M price is very competitive, and there is always ways we can also make a reasonable interest, the benefit and profit out of that. And overall, you have already seen the success we made on the IT categories, and it has occupied a strong market share and we believe this will be copied in other categories as well.

(Foreign Language) And in the future, we'll continue our efforts on C2M and increase the proportion of products on our platform. Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

So just to put in layman's terms, just to give you an example on C2M margin, it's a triple win situation. So for example, for -- because a lot of the brands will try to protect their offline retail network, so they will monitor the sales price, which limit our ability to give more value to consumers. So for select -- only very large brands can do that. And then at the same time, they would also resist giving us even lower procurement price just to prevent us from selling lower price to consumers. So by C2M, we can really break through both. One is that because it's a customized product, so we wouldn't disrupt the brand's offline retail channels, so we can price the products lower to give consumers more benefit. Two is that because of that same reason, and we tend to buy a very large volume for the C2M products, so we can get at even lower procurement price, so we can also maintain very healthy margins and while we can also support the brands to sell a much larger volumes through our powerful channel. So it's a triple-win situation for the C2M model.

Q - Alicia Yap {BIO 15274658 <GO>}

Thank you.

Operator

Your next question comes from the line of Thomas Chong from Jefferies. Please ask your question.

Q - Thomas Chong {BIO 21155199 <GO>}

Hi, good evening. Thanks management for taking my questions. I have a question about JD Logistics. Can management comment about the strategy in 2020 and how should we think about the top line and the margins as we go through this year [ph]? Any color would be great. Thank you.

A - Zhenhui Wang {BIO 21020367 <GO>}

(Foreign Language) Zhenhui Wang of JD Logistics.

(Foreign Language) Next year, our JD Logistics strategy will continue to focus on the efficiency increase and users' experience enhancement.

(Foreign Language) And we'll also step up efforts on reaching the lower-tier markets by expanding our logistic network.

(Foreign Language) And we'll also work further on improving our products and our capacity to further open the external market.

(Foreign Language) And we will also invest for the -- we'll also step up efforts on our technology deployment, and the revenues from technology will continue to grow next year.

(Foreign Language) And for our external revenues from external orders have accounted for over 40% of the overall revenues of JD Logistics. For the next year, the proportion will continue to grow revenue mix. We will seek steadily improvement of profit in the future.

(Foreign Language) As you've seen the results from this quarter, our fulfillment ratio has been dropped, thanks to our increasing scale.

(Foreign Language) And since we are continuing to going down into the lower-tier cities, (Technical Difficulty) will have some short-term impact fulfillment expenses. But in the long run, we believe the fulfillment fee will -- we're still having the space to improve. Thank you.

Q - Thomas Chong {BIO 21155199 <GO>}

Thank you.

Operator

Your next question comes from the line of John Choi from Daiwa. Please ask your question.

Q - John Choi {BIO 16529883 <GO>}

Good evening and thank you for taking my question and congratulations on a great set of results. I have a question on the user growth. And obviously, as we go into lower-tier cities, yes, we started to see user growth acceleration. Can management give some color on what kind of user growth momentum we'll further see throughout 2020 and onwards? How much opportunity do you see if you compare to yourself and your peers? And secondly, just quickly, Richard I think mentioned about the technology. Given that industrial Internet is one of the key themes that a lot of the other Internet companies are talking about, can you provide us how this will change our business strategy for JD and what are the areas that we are looking into? Thank you.

A - Lei Xu {BIO 21705778 <GO>}

(Foreign Language) On the question about users' growth.

(Foreign Language) And as I mentioned in last quarter's call, we are targeting our efforts for the user growth on the growth field, customers acquisition and old customers' maintenance. On the first half of the year, we have done a series of internal organization optimization.

(Foreign Language) And on the existing customers, we are setting up efforts on their operations to increase their activity on our platform and their maintenance on our core platform, the ARPU and satisfaction rates keeps going up.

(Foreign Language) And also I want to emphasize that we focus on benevolent growth of our users, and we won't [ph] surprise users through fragmented space and unsustainable way and we believe that eventually the quality of the users will be manifested through our careful and healthy fostering process.

(Foreign Language) On the maintenance of our users, what we pursued is the indicators approving all aspects is not only a mere number improvement to see how many users we have acquired in a short period of time. Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

So, Richard is traveling. So I don't know if he has heard the question. But I can quickly share that the technology services we have in mind is more about the retail structure that we have accumulated over the years. Recall, we had retail as a service concept. So much of the technology know-how and -- is already being transformed into solutions and we have seen demand from the industry for these solutions. So those could be clearly the starting point. There will be more in the pipeline that we will discuss more when we have products available.

Operator

Your next question comes from the line of Tina Long from Credit Suisse. Please ask your question.

Q - Tina Long {BIO 21068620 <GO>}

Hi, thank you, management for taking my questions. And congratulations again on the results. I have one quick follow-up on Jingxi first. So I want to know for -- I know that we recently launched it. But I want to know, in 2020, have we earmarked like a meaningful amount of sales and marketing expense to promote it? Will that have any impact on the overall sales and marketing ratio? And my main question is actually on the GP margin. I understand that third quarter GP margin was impacted because of reinvestment of first half one-off gain. So I want to know after we reinvest all the gains for the remainder of the year, in 2020, are we going to see a uptrend of GP margin from a year-on-year perspective? Yes. Thank you.

A - Lei Xu {BIO 21705778 <GO>}

(Foreign Language) Xu Lei of JD Retail. On the question about Jingxi. The Jingxi platform is one of our business model to reach broader market. And, as I mentioned that we will seek different ways and different models to grow our market. So the Jingxi platform will not make a great impact of our marketing fee next year. As I just said in our last question, we are seeking a comprehensive improvement on the indicators. So we won't just pursue like one indicator growth for that.

A - Sidney Huang {BIO 20098238 <GO>}

And so on the second question, generally you know, obviously we haven't done our 2020 budget process, so I can't give you a definitive answer. But in general, all else being equal, gross margin should expand for the same categories because of the economies of scale as we mentioned in the past. But I just wanted to also point out that the gross margin and expense line, sometimes you should look at holistically. I'll give you one example. And sometimes -- and more often than not, lower price, if used effectively, can be the best marketing spending. In other words, you can save marketing costs by promotion, and so sometimes lower gross margin could mean lower marketing expense as well. Clearly, that's what happened in Q3. Our marketing expense ratio actually decreased by 0.6%, more than compensates the gross margin shortfall. So you really have to look at this gross margin and expense lines in a holistic fashion.

Q - Tina Long {BIO 21068620 <GO>}

Thank you.

A - Lei Xu {BIO 21705778 <GO>}

(Foreign Language) Just to add a few things from Xu Lei.

(Foreign Language) Xu Lei. I just want to add that since the end of last year we have made our strategies to grow our business based on quality development and sustainability. So you have seen from all the numbers of the past three quarters this year, these are all the demonstrations of our commitment on quality growth. And in the future, we will stick to this principle to achieve quality and sustainable growth. Thank you.

Operator

Your next question comes from the line of Natalie Wu from CICC. Please ask your question.

Q - Natalie Wu {BIO 19852429 <GO>}

Hi, good evening. Thanks for taking my question and congratulations on very solid results. Just curious, can you share something with us about the incremental margin profile on your lower-tier city orders? And also about the take rate on Jingxi, I wonder if they're different relative to your JD platform? Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

Yeah. Let me quickly answer the first question. We haven't really internally analyzed in a very detailed way. But we have the same price in lower-tier city and higher-tier cities, and cost structure is also similar. So, in general, the cost structure and the margin profile should be a lot similar. But there are differences in, for example, category consumption pattern that might be different. So we -- but we have not analyzed this in more detail. But they should be more or less similar.

Q - Natalie Wu {BIO 19852429 <GO>}

So what about the fulfillment expenses?

A - Sidney Huang {BIO 20098238 <GO>}

Fulfillment expenses in terms of order density, clearly Tier 1 city will enjoy most benefits. But we have covered 99% of counties and district and we don't necessarily have the same fulfillment promise in the very remote areas. We do cover 90% -- roughly 90% of the orders within 24 hours, and they tend to be in Tier 1, Tier 2 cities and in major town areas in the most populated lower-tier cities. So it's actually well designed to optimize the cost structure in the lower-tier city as well.

A - Lei Xu {BIO 21705778 <GO>}

(Foreign Language) Just to add on this question, it is true that different categories will have different performance in the lower-tier cities. For example, for iPhone and Huawei smartphone, the growth mainly come from the lower-tier cities. And for the big size refrigerators lower city customers like them pretty much very much because they have a larger house. And also for the luxury products, the lower-tier city customers buying more and more on our platform because the traditional channels do not support their purchase needs. But all these examples now cannot get to conclusion that the lower-tier cities like the big ticket products. So we have to really analysis it with different categories. Thank you.

Q - Natalie Wu {BIO 19852429 <GO>}

Understood. What about the take rate on Jingxi?

A - Sidney Huang {BIO 20098238 <GO>}

Right now, it's 0.6% covering the payment costs.

A - Lei Xu {BIO 21705778 <GO>}

(Foreign Language) And for the take rate in the Jingxi platform in general, we will have a very low take rate to encourage merchants on our platform. Most of the products will have 0.6% and for some of the products will be above 1-point.

Q - Natalie Wu {BIO 19852429 <GO>}

Very helpful. Thank you.

A - Lei Xu {BIO 21705778 <GO>}

Thank you.

Operator

We are now approaching the end of the conference call. I will now turn the call over to JD.com's Jia Dong for closing remarks.

A - Jia Dong {BIO 16469954 <GO>}

Once again, thank you for joining us today. Please don't hesitate to contact us if you have any further questions. Thank you for your continued support and we look forward to talking with you in the coming months.

Operator

Thank you for your participation in today's conference.
