Q4 2017 Earnings Call

Company Participants

- Ruiyu Li, Director, Investor Relations
- Sidney Huang, Chief Financial Officer

Other Participants

- Alex Yao, Analyst
- Alicia Yap, Analyst
- Eddie Leung, Analyst
- Ella Ji, Analyst
- Jamie Shen, Analyst
- Jerry Liu, Analyst
- Jin Yoon, Analyst
- John Choi, Analyst
- Natalie Wu, Analyst
- Ronald Keung, Analyst
- Scott Devitt, Analyst
- Thomas Chong, Analyst
- Tian Hou, Analyst
- Wayne Wang, Analyst
- Wendy Huang, Analyst

Presentation

Operator

Hello, and thank you for standing by for JD.com's Fourth Quarter and Full-Year 2017 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 would now like to turn the meeting over to your host for today's conference, Ruiyu Li.

Ruiyu Li {BIO 19135837 <GO>}

Thank you, operator, and welcome to our fourth quarter and full-year 2017 earnings conference call. Joining me today on the call are Richard Liu, our CEO; and Sidney Huang, our CFO. For today's agenda, Mr. Huang will discuss highlights for the fourth quarter and full-year 2017. Following the prepared remarks, Mr. Liu and Mr. Huang will answer your questions.

Before we continue, I refer you to our safe harbor statements in the earnings 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.

Now, I would like to turn the call over to Sidney.

Sidney Huang {BIO 20098238 <GO>}

Thank you, Li. Hello, everyone. Thank you for joining us today. We are pleased to report another quarter of strong top line growth, healthy core e-commerce profitability and exciting new strategic initiatives. During the fourth quarter 2017, our net revenues grew 38.7%, with solid performance on top of an exceptionally strong fourth quarter in 2016.

Our direct sales revenues grew 37%, led by home appliances, food and beverage, cosmetics, home furnishing and baby products. Revenues from services and others grew 55% year-over-year, the highest growth rate in the past six quarters, driven by third-party supply chain management and advertising services.

For full-year 2017, our net revenues increased over 40%, and revenues from services and others grew nearly 50%. Gross margin in the fourth quarter was 13%, compared to 13.7% in the fourth quarter last year. The margin reduction was mainly due to impacts from new businesses, which included JD Logistics third-party business, technology services and overseas operations. Excluding new businesses, JD Mall gross margin was slightly higher than the same quarter in 2016 and second quarter 2017.

On a full-year basis, non-GAAP gross margins improved 42 [ph] basis points from 13.4% in 2016 to 13.8% in 2017, reflecting economies of scale from the third-party business and accelerating advertising revenue growth, partially offset by the investments in new businesses.

During the fourth quarter, we invested heavily in logistics, marketing and technologies. Most notably, we continued to expand our warehouse network during the quarter. It will take a couple of quarters to reach full capacity utilization. We added 81 warehouses during the quarter to a total of 486 nationwide, with over 10 million square meters in total space at the end of 2017, up over 70% from 12 months ago.

This capacity expansion efforts affected the gross margin for the third-party business, as well as our expense ratio for the core e-commerce business. The fulfillment expense ratio increased 35 basis points from the same quarter last year. However, we believe these investments are worthwhile for our supply chain management services and have created both, service revenue and the margin upside for 2018 and beyond. Our successful JD

Logistics fundraising, backed by a group of top domestic and international institutions, clearly validated the largest of these investments.

Our non-GAAP marketing expense ratio was 4% in Q4, comparable to the same quarter last year and the second quarter 2017, when we ran very similar marketing campaigns. Our R&D expense ratio increased to 1.9%, up 38 basis points from the same quarter last year, as we hired the top talent in AI, big-data and cloud-based solutions, as well as forming partnerships around the world to enhance technological innovation across our front-end platform and backend infrastructure.

On the other hand, our G&A expense ratio reduced to 20 basis points, as we continue to benefit from operating leverage. Similar to the second quarter 2017, we essentially reinvested part of the excess profits in the prior quarter back into the business in the current quarter, especially during the Double 11 promotion season, when we returned the excess profit back to our consumers. As a result, non-GAAP operating margin was a negative 0.5% in the fourth quarter.

Now, excluding new businesses, the non-GAAP operating margin for JD Mall was a positive 0.6%, down 32 basis points from the same quarter last year, mainly due to accelerated logistics capacity expansion in the R&D investment.

On a full-year basis, however, non-GAAP operating margins improved to 0.8%, up from 0.6% in 2016 and non-GAAP operating margin for JD Mall improved to 46 basis points, from 0.9% in 2016 to 1.4% in 2017. On a full-year basis, non-GAAP net income attributable to ordinary shareholders was approximately RMB5 billion, an increase of 140%, from RMB2.1 billion in 2016. The net margin was 1.4% in full-year 2017, up 57 basis points from 0.8% in 2016. All-in-all, it's a very healthy year of bottom line improvements.

Our free cash flow was negative 1.2 billion during the quarter, compared to negative 2.2 billion in the same quarter last year. Free cash flow for full-year 2017 was a positive RMB15.7 billion, up from 13.5 billion in 2016. As we communicated 12 months ago, our CapEx in 2016 had been behind the schedule, which began to catch up in the second half of 2017. CapEx totaled RMB11.4 billion, up from 4.3 billion in 2016.

Of the RMB7.1 billion increase, over RMB6 billion was due to land acquisition and construction of warehouses. As we mentioned in the past, given JD's contribution to the local economies, we're in a unique position to acquire land at a very attractive economic terms. The warehouse facilities we have built are also highly sought-after assets and may be monetized for liquidity with large financial gains.

We continue to believe such land and warehousing investments are highly accretive to our shareholders. Excluding the CapEx, our operating cash flow, excluding JD Finance impact, totaled RMB27 billion in 2017, up 52% from 18 billion in 2016.

Now, I would like to highlight a few key strategic developments since our last earnings call. Over the past three months, we formed a number of highly strategic partnerships. For example, the joint investments with Tencent in Vipshop and joint venture with Meili group are both designed to expand our product selections and the long-tail merchant base, which in turn will improve our customer experience and attract the female users and new customers in lower-tier cities and lower-income segments.

The joint investments with Tencent in Wanda group and Better Life group will also help expand our customer and product reach through omni-channel store tech solutions as part of our Boundaryless Retail strategy. We are very excited about these partnerships and expect to create win-win synergies, strengthen our consumer mind share and better serve our joint customers in 2018.

Now, let's discuss our financial outlook. We expect Q1 2018 net revenue growth to be between 30% and 33% on a year-over-year basis, taking into account the increasing seasonality effect of our business, excluding any impacts on JD Finance for both current and prior year periods. For full-year 2018, we expect our non-GAAP net margin to be between 1% and 2%, which reflects our commitment to margin improvement, while maintaining flexibility to reinvest for future growth.

This concludes my prepared remarks. And we can now move to the Q&A session.

Questions And Answers

Operator

(Operator Instructions) Our first question comes from the line of Jin Yoon from Mizuho. Please ask the question.

Q - Jin Yoon {BIO 16293072 <GO>}

Hey. Good evening. Thanks for taking my question. Sidney, did I hear you right? You said net income margin was going to be 1% to 2%. With the midpoint being about 1.5%, that means we're going to see very little, if any, operating or net income margin leverage. Can you just kind of talk about the drivers and potentially the seasonality behind that and potentially, what your CapEx budget is for the year? Thanks.

A - Sidney Huang {BIO 20098238 <GO>}

Yeah, sure. I mean, obviously, this is the beginning of the year. When we -- no one can expect what happens ahead. I think the guidance is, as I mentioned, it's a reflection of our commitment to improve margins, but at the same time, maintain enough flexibility to reinvest for future growth.

As I mentioned earlier on the call, as you can see, we invested quite a bit in new businesses in the fourth quarter, including JD Logistics third-party business. Some of those investments may take a few quarters to be fully utilized and we'll then have operating leverage. So, this is a very preliminary outlook for the full year.

Operator

Thank you. Our next question comes from the line of Ronald Keung from Goldman Sachs. Please ask the question. Ronald Keung, your line is now open.

Q - Ronald Keung {BIO 15432736 <GO>}

Hello. Thank you, Richard, Sidney and Ruiyu. Thanks for taking my questions and thank you for the guidance that you mentioned just then. My question is more on the next growth drivers and I think particularly your strategy with Vipshop and with Meili. Can you just mention -- just go through a few things? Firstly, the Vipshop cooperation, when do you think the level -- or access on your app will begin? And what are you expecting sort of the contribution of GMV growth or apparel contribution from the Vipshop tie-up?

And the other part is the WeShop, which is your joint venture with Meili. Can you just go through how many merchants so far have signed up and just rough launch times? And whether this JV will be counted as a investment, so it will not be consolidated, also the longer-term prospects of this joint venture? Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

Sure. So, both partnerships will actually be launched within March. So, you will see the super store from Vipshop on JD within this month. And as we mentioned, when we announced the deal that we do expect great synergies between the two platforms. Vipshop has great product selections and very complementary customer base, especially the female customer base.

So, we do expect the collaboration will be a win-win effort, that will bring both products to JD customers. At the same time, bring traffic and sales to Vipshop, obviously, which will benefit both platforms. For the Meili joint venture, you will also start to see the launch during launch on the level one entry point of JD in WeChat. It's a very decentralized model.

So, I would probably let you look at the actual development rather than elaborating too much on the details.

It's -- we will not consolidate the joint venture, but it was targeted to attract a long-tail merchant base and we already have so far recruited over 50,000 small long-tail merchants obviously, including some well-established merchants as well. And we'll enable those merchants to form their own customer base through the WeChat ecosystem. It will be very interesting experiment that you will begin to see in the near future.

Operator

Thank you. Our next question comes from Natalie Wu from CICC. Please ask the question.

Q - Natalie Wu {BIO 19852429 <GO>}

Hi. Good evening, management. Thanks for taking my question. My question is regarding the overseas market exploration. We think that you've entered OA [ph] and you've entered Europe. Just wondering what kind of the role JD is preparing to play globally? And what's the related investment scope we should expect in the -- in next year? Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

(Foreign Language)

So, right now for international operations, we have announced in the past, in Southeast Asia, mainly Indonesia and Thailand. And for North America and the Europe, we have been really -- we said we have set up local offices, for example in LA, to purchase -- to really develop local brand relationship and bring the US product to China. But we will, beginning this year, to start to consider ways to serve the local customers. But right now at this point, no immediate plan has been set up.

Operator

Thank you. Our next question comes from the line of Wendy Huang from Macquarie. Please ask the question.

Q - Wendy Huang {BIO 15034507 <GO>}

Thank you. Can you talk about, for your existing major product categories, such as home appliance and also consumer electronics, what kind of scale should they reach this year? And also is there any further potential for this existing product category to see the margin expansion?

A - Sidney Huang {BIO 20098238 <GO>}

Sure. So the home appliance and electronics, those are our leading categories. As Richard mentioned in the past, in a retail business, when you become a market leader on a first-party basis, not only you can realize economies of scale through supplier relationships' joint brand efforts whereby you are increasing the margin, but you will also, because of the consumer mind share, continue to grow faster in many cases than the industry. So, this is what we have seen exactly in 2017. Even though we had been the largest player, we continue to see very, very robust growth way ahead of the industry average.

Operator

Thank you. Our next question comes from Eddie Leung from Merrill Lynch. Please ask the question.

Q - Eddie Leung {BIO 15234642 <GO>}

Hi. Good evening, Richard and Sidney. I'm curious on your advertising pieces. It sounds going pretty nicely. Could you talk a little bit about the drivers behind it? What's the main driver for the exploration as you mentioned? Are we talking about better click-through rate, higher pricing or increased ad load? Any color on that front, that would be great. Thanks.

A - Sidney Huang {BIO 20098238 <GO>}

Yeah. Our advertising is mainly driven by technology. And we have -- and I mentioned in the last quarter that increasingly using AI technology, the conversion for our merchant and brands are seeing meaningful improvement over the past several quarters. So, when the brands see better results, better conversion, they are more and more willing to spend more advertising dollars on our platform.

So, this has been the main driver. We didn't increase, for example, the advertising inventory, didn't increase the positions on our platforms. So, it's really driven by technology. And we see continued momentum going forward. I just quickly want to mention that, in the fourth quarter, our advertising revenue growth was also the highest in the past five quarters.

Q - Eddie Leung {BIO 15234642 <GO>}

Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

(Foreign Language)

Yeah. So, Richard is basically adding that, if you look at the advertising revenue at the percent of GMV, the percentage both -- for JD is substantially lower than our industry peer. And this is because in the past, we did not provide enough advertising tools to our merchant groups.

So, we have been improving over the past several quarters and we'll continue to do so and providing more and more back-end solutions and advertising product to our merchants, so they can have better control over their own promotional needs. So the potential is still huge and we are seeing some from our actual results.

Operator

Thank you. Our next question comes from the line of Alicia Yap from Citigroup. Please ask the question.

Q - Alicia Yap {BIO 15274658 <GO>}

Hi. Good evening, Richard, Sydney and Ruiyu. Thanks for taking my questions. Questions regarding the margins on gross margins. So, I'm not sure if my calculation is correct. But is seems like the 1P gross margins declined about 90 basis points year-over-year. It's [ph] true, it suggested the competitive situation seems to be worsens a little bit in the fourth quarter. How should we think about the 1P gross margins for 2018, especially during the seasonally strong quarter?

And then related to your 1% to 2% net margin guidance for this year, can you share with us where would you be spending the most of the investment area that we have to be cautious and be mindful of modeling? Is that more on the logistic or is that more on sales and marketing, branding, if you can share some of the color, that would be great? And lastly, on the housekeeping, how many of these 100 brands that previously left JD, now have returned to your platform? Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

Okay. So, let me take one-by-one. So, for gross margin, I mentioned earlier that if you exclude the new businesses, the JD Mall gross margin was actually slightly higher than the same quarter last year and also second quarter 2017. So, it was generally still healthy. A second reason we also mentioned in the past that our business was managed on a full-year basis.

So because of the excess returns in the first three quarters, our business managers were encouraged to return part of the profit back to our consumers during big promotions. We believe these are very worthwhile investments. And so, you can't look at one quarter, any single quarter to extrapolate the profitability trend, just as I questioned in the third quarter that you should not extrapolate that for the future quarters .

So, I would strongly encourage our investors to look at the full-year trend, which I mentioned is still on the rise.

The 1% to 2%, I mentioned about the new businesses, I think, in 2018, we'll continue to invest in JD Logistics mainly to third-party services, supply chain management integrated to warehouse and delivery services, not only to our merchants but also to third parties outside of JV business.

So, those -- and then beside, there will be our technology services, we've developed cloud-based solutions and we are actually seeing the business taking off, that would, in a short term, will be loss making but we do see huge potential in the technology services area. Overseas expansion is another one, as I mentioned earlier. So if you exclude those, the core e-commerce business, which implied the core e-commerce business will actually see quite meaningful margin expansion.

And the last question on the brands, we do start to see brands coming back. And I think more interesting data I would like to share with you is the key accounts for our apparel segment, actually for -- basically consisted of the merchants, the top merchants staying with us through last year, and the merchants came back at the end of last year. We saw over 100% increase in the first two months in the transaction volume. So very, very encouraging results.

We do believe there will be more merchants coming back. But as we mentioned on the last earnings call, we may take two to three quarters, but we are already seeing very, very encouraging trend and the ones that did come back see triple-digit growth over the past two months already.

Operator

Thank you. Our next question comes from Alex Yao from J.P. Morgan. Please ask the question.

Q - Alex Yao {BIO 16818860 <GO>}

Hi. Good evening, management, and thank you for taking the call. I want to follow-up with the Alicia's question a little bit more. I understand that logistic is one of the key investment initiative for 2018 and potentially beyond that. Can you give us a little bit color in terms of where exactly do you want to invest into this area, is it more on the labor sides, equipment sides, the warehousing sides?

And also given the incremental investment on there, how should we think about the next couple of quarters of margin trend versus the previous years? And then the mid to longer-term outlook for this business, where shall we expect this business to be more meaningful in terms of revenue generation from third-party vendors or merchants versus our own business? What kind of the timeline are you looking at this business in terms of a profitability generation? Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

(Foreign Language)

So the two -- the investments in logistics area will be comprised of two major areas, one is in the fixed assets, which include land and equipment and warehouses; and two is on logistics technologies.

(Foreign Language)

So, you need to understand the first areas of investment. I would elaborate a bit more on logistics technologies. We have launched, first, a fully automated warehouse in Shanghai, and we have also completed two weeks ago, the unmanned delivery station and also in the near future, you will see automated delivery robots in numerous campuses in Beijing.

(Foreign Language)

And we expect to receive license for the drone operations in 10 provinces this year.

(Foreign Language)

We have also tested the self-driving truck for over six months. So, these investments will probably not yield any near-term immediate operating or financial benefits, but we believe, as the technology continue to advance and labor cost are expected to increase, so these investments will be very valuable at certain inflection point that will continue to put JD Logistics at the forefront of both operational efficiency and technical sophistication.

(Foreign Language)

And so, we formed a separate autonomous -- relatively autonomously operated subsidiary for JD Logistics. We've seen great operational results over the past few months, and we do expect over the past -- over the next three to five years, the external revenue will reach 50%.

(Foreign Language)

So, these third-party revenues will not only come from our third-party merchants on our platform, but also from customers from outside of the JD Mall business and we have seen those -- many of those already using our services.

Operator

Thank you. Our next question comes from Jerry Liu from UBS. Please ask the question .

Q - Jerry Liu {BIO 17515547 <GO>}

Hi, guys. Thank you for your time. My question is about gross and net margins. If we were to separate JD Mall from the areas of investment, do we think in 2018, JD Mall margins will improve because of apparel brands coming back and FMCG scale, et cetera? And then on the areas of investment, is this a full-year of investment? Could margins declined before things get better?

A - Sidney Huang {BIO 20098238 <GO>}

As I mentioned earlier, because of the investments in new businesses and we do continue to commit for overall margin improvement, which in turn will imply that our core business will see rather meaningful margin expansions. That could come from actually all categories, not only the apparel and FMCG you mentioned, but also from our strong categories, in home appliance and electronics. And so we do see -- and obviously on the services side, whether it's advertising or logistic services. So, we do see potential for margin expansion across multiple areas.

Operator

Thank you. Our next question comes from the line of John Choi from Daiwa. Please ask the question.

Q - John Choi {BIO 16529883 <GO>}

Good evening, guys, and thanks for taking my question. I have a few questions here. First of all, I'd like to touch base on your product revamp strategy in 2018. I understand, JD has a plan to kind of revamp their mobile app with more personalization features, how's that coming through? And also your merchant services, what is the status here? Should we be expecting more merchant services related revenue through your third-party revenue going forward?

And secondly, little bit on your free cash flow. As we see, I understand free cash flow has been improving over the -- a period of time. So, as you go into 2018, should this trend continue along with your CapEx? So if you can kind of reduce on a relative basis, so that will be helpful. And lastly, if Richard could give us a little bit more color on the recent JV with Meilishuo, is this going to be a game changer for JD when it comes to collaboration with Meili and also for Tencent? Thanks.

A - Sidney Huang {BIO 20098238 <GO>}

Okay. So let me see if I can remember all that. So, for the personalized recommendation, we do have -- it is one of our top priorities this year that we want to create personalized user interface. And we do expect our first major launch In the second quarter, which could be still on a soft testing basis, but you'll start of see that happening and probably more on a fully scale -- a full scale in the second half.

Merchant services is another top priority. We have introduced many new products to our merchants, including the advertising product and tools, the data analytics tools and those are all provided to our merchants and also to our suppliers, which we believe will enhance the ability to better market and fill their products on our platform.

On the free cash flow and the CapEx, so CapEx is a little tricky, that we are expecting to invest in more land acquisition and warehouse facilities. But I also mentioned that there are a number of institutions, have been chasing us for partnership and collaboration. So, there is a possibility that we could have our partners to invest part of those CapEx through the partnership that we can continue to maintain certain control over the assets, but at the same time, leveraging third-party's financial resources. So, we do want to have somewhat of a lighter model going forward, especially given that there will be -- that we are taking opportunities to secure land as many local governments are approaching us for collaboration.

Again, these are all governments, approaching us because when JD set up a warehouse in the jurisdiction, it brings job opportunities, brings local activities and local taxes. So -- and we are working with many of those governments. And so there is -- it's a very exciting opportunity. We're just looking for ways to manage both the opportunities, at the same time, manage the appropriate level of CapEx. So, we'll give you more update, hopefully in the second quarter.

Operator

Thank you. Our next question comes from the line of Scott Devitt from Stifel. Please ask the question.

Q - Scott Devitt {BIO 4757000 <GO>}

Hi. Thanks. First, just wondering if you could give the third-party mix as either a percentage of units or GMV, and also what portion of the third-party GMV is being fulfilled by JD? And then a bigger picture question. JD is still a very young company, building a business for the next many decades. And I'm wondering why you think there is such a hyperfocus on margin progression of the business at this stage of the development, whether you think that focus is the way -- right way to assess value creation by the company? And how you think investors should measure the company and profits, given that you don't seem to be focused on optimizing for profits still for many years? Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

Sure. So, on our third-party logistics services, revenue did increase very significantly in the fourth quarter on a triple-digit rate. So, part of -- a majority of that growth came from supply chain management, which does -- also which in turn is helping our merchant inexperience. So, we -- in terms of percentage of orders contribution, it is in the low-teens and are rising quite quickly.

And on the margin, it's a very interesting question. As we mentioned that in the past quarters, more often than not, the margin came out without trying to manage it. So if we don't do anything, margins would improve and we have saw that -- we have seen that both in Q1 last year and Q3 last year. And we normally were making effort during big promotion season to return part of that margin back to our consumers.

And because of this -- so -- which, basically indicates that our scale is at such a level that it's -- the profitability was quite natural and improving margins should be quite natural. But just as you mentioned that it is still --

we're still in a very early stage of a very, very long-term growth trajectory.

So, our focus has been on growth, and we also made very intentional effort to reinvest part of that profitability back into the business, whether through return to consumers or investing in the technologies, as Richard mentioned also in complementary businesses. So, that's exactly what we're doing to reinvest and -- but at a current scale, I think, margin expansion should be a quite natural result as well.

Operator

Thank you. Our next question comes from the line of Thomas Chong from Credit Suisse. Please ask the question.

Q - Thomas Chong {BIO 21155199 <GO>}

Hi. Thanks for taking my questions. I have a quick question on 7Fresh. Can management provide some highlights about the expansion for this year and our target number of stores in the next few years? Thanks.

A - Sidney Huang {BIO 20098238 <GO>}

Yeah. So, for 7Fresh, it's really an experiment. I think for us it's omni-channel store tech experiment that we try to create our own model of offline business that can realize very, very high sales per square meters. Because not only the products and the services, the technology in the store can attract a lot of traffic, but at the same time with the online angle through our open -- our Dada-Jingdong Daojia network, so you can essentially realize a much, much higher same-store sales.

So -- but our intention is not to open many, many stores. I think we used this store to develop the omni-channel store tech solutions, so that we can use those solutions to enable our partners. I mentioned about our investments in some of the offline stores and the offline retailers. So, those solutions that we develop through 7Fresh will be used to strengthen our partnership with those offline partners.

(Foreign Language)

Yeah. So, we will open more stores in Beijing just to test and validate the model. And once the model is validated, we will expand through franchise and also -- not just to work with our partners, to enable their stores to adopt the same model. The unique advantage for JD in moving into the offline fresh supermarket is that we already have a very well established supply chain system. And with that system, we can move very fast once the model is established.

(Foreign Language)

Yeah. So, in this regard, even for the top [ph] retailers for over 20, 30 years, they still can only cover some of the cities in China. But with our supply chain management system, we can already cover the entire China.

Operator

Thank you. Our next question come from the line of Tian Hou from T.H. Capital. Please ask the question.

Q - Tian Hou {BIO 20458526 <GO>}

Hi, Sidney and Richard. I have two questions. One is related to the investment in the Vipshop. So, would you please elaborate, how in the near term, JD is going to benefit from such investment? So, that's number one.

Number two, looking at the P&L of Q4, the costs of the revenue were not a lot. And so, I wonder how much has it come from the constant traffic -- the traffic acquisition cost, so -- which you guys started in this year, advertising alliance in Q3. So, that's my two questions. Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

(Foreign Language)

So, to address the first question on the Vipshop, in the short term, I think it's really complementary to both platforms through our complementary products, mainly, for example, Vipshop is specialized in apparel and other long-tail categories, with female customers in the lower tier cities, where JD is actually stronger in the other categories and also male customers in Tier one, Tier two cities. So, very, very complementary from both product selection and user base.

(Foreign Language)

So in the long term, we are looking to create more synergies on the supply chain, also on the logistics. For example, we can share some of the warehouses or delivery stations, some of those infrastructures, so that we can save costs and create more efficiency for both companies.

And then on your second question about costs, whether it included the acquisition costs, most of the traffic acquisition cost will be in the marketing expense line. The only related items in cost will be the cost for our advertising revenue, which is actually quite small. So, that's not the main reason. I main reason, I mentioned earlier is because of the new business for JD Logistics, third-party service because of a pretty massive build-out of warehouse facilities, including cold chain facilities that were not fully utilized in Q4 and also in technology services when we are still building up that business.

Operator

Thank you. Our next question comes from Ella Ji from Renaissance. Please ask the question.

Q - Ella Ji {BIO 16168552 <GO>}

Hi. Good evening, Richard, Sidney and Ruiyu. My question is still about the margins. First of all, looking at the -- maybe relatively near term for 2018, Sidney, if I hear you correctly, you said that JD Mall alone in last year, the OP margin actually improved to 46 bps year-over-year. So if we back that out, the new businesses drag on your OP margin is about 28 bps.

So, how should we think about the magnitude of your new businesses drag in 2018? Is it going to be bigger or at similar levels? And then relating to that, can you also comment on the long-term margin target on a company-blended basis and then for JD Mall, both? And can you also comment on the timeframe, please? Thank you.

A - Sidney Huang {BIO 20098238 <GO>}

First, so for the new business, it's also -- because it's new, so we do have an internal budget, actually quite aggressive budget. But it's evolving and it depends on a lot of dynamic during the year. So, all I can tell you is, in our budget, we have a quite aggressive budget for the new businesses, essentially to -- kind of, to reiterate my point earlier that at our scale, our core business should naturally generate increasing profitability and we want to use at least part of that to reinvest.

And so it is also relatively flexible as we progress through the year. And so, it's tough to pinpoint any more detailed number at this point. Long-term, we mentioned about the core retail business, as a scale, continue to improve. As you can see, our gross margins still has huge potential comparing to offline biggest retailers, for example, our JD Mall more operating margins continue to enjoy an advantage despite of heavy investment in technology.

So, margin trend should be very promising for established business. It's a matter of how much we will invest, and the reinvestment will be also depending on what kind of opportunities we see that are complementary to our core business and that are accretive to our shareholder value.

Operator

Thank you. Our next question comes from the line of Wayne Wang from HSBC Global Research. Please ask the question.

Q - Wayne Wang {BIO 20257563 <GO>}

Thank you, management, for taking my question. I have a follow-up on the traffic acquisition strategy. So, what's our, like key traffic acquisition strategy in 2018, aside from the like traffic or partners in 2017? And also another question regarding to the technology and the common [ph] cost. You are thinking 4Q, the cost is relatively high, is this mainly due to one-off or will that be a continuing effort? Thank you very much.

A - Sidney Huang {BIO 20098238 <GO>}

Yes. I think for traffic acquisition, we have, in all of the conventional channels that we will continue to use. Clearly, we have established a great relationship with all of the major traffic sources. And then the alliance we talked about with top Internet companies, obviously including Tencent, 360 and a number of others. So, we will see actually more of those partnerships and effectively using (inaudible). For the technology and R&D spending, this will be a long-term trend or at least the medium-term trend that will continue to step up investments.

So, this is not one-time. We'll continue to invest in hiring those top talents around the world. We expanded our Silicon Valley office, for example, from over 10 people to now over 100 people, hired really the top talent from really the best Internet companies in the United States. We do expect that investment to continue.

Operator

Thank you. Our last question comes from the line of Jamie Shen from Bank of China International. Please ask the question.

Q - Jamie Shen {BIO 19057125 <GO>}

Hi, management. I have a question on the third-party marketplace GMV growth. Based on my very rough calculation, I think the GMV growth have picked up meaningfully in the last quarter compared to the third quarter. Just wonder what are the drivers behind? And also looking forward into 1Q, as management just commented on some apparel brands coming back, should we be expecting the apparel categories to revive growth in the first quarter? Thanks.

A - Sidney Huang {BIO 20098238 <GO>}

Yeah. So, we no longer discuss details about GMV because the metric now is really for industry comparison only. But the underlying net GMV growth was actually still under pressure for the marketplace business in the fourth quarter. We mentioned on the last earnings call, it would take two to three quarters to begin to see recovery.

So, on apparel in particular, I mentioned about a key account growth. So, we do have -- we still have the right customer base and the right platform. So, it's just a matter of time, we believe, for the remaining merchants, at least majority of them coming back. And we're also working with many of those merchants to establish new sub-brands and also new talents, new brand designers.

So, there will be multiple means to improve this category and we are actually quite optimistic. But I do not expect a very quick fix. And we don't necessarily see a major pickup in Q1. But in the next several quarters, you should see gradual recovery.

Operator

Thank you. We are now approaching the end of the conference call. I will now turn the call over to JD.com's Ruiyu Li for closing remarks.

A - Ruiyu Li {BIO 19135837 <GO>}

Thanks, operator, and thank you for joining us today. Please feel free to contact us if you have any further questions. We are looking forward to talking with you in the coming months. Thank you. Bye-bye.

Operator

Thank you for your participation in today's conference. This concludes the presentation. You may now disconnect. Good day.