Alibaba: They Don't Ring A Bell At The Bottom

Feb. 08, 2024 8:48 PM ET**Alibaba Group Holding Limited (BABA) Stock**, **BABAF Stock**JD, JDCMF82 Comments30 Likes

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Summary

- Alibaba has struggled to grow as housing bubble fallout continues.
- Forward estimates for BABA continue to be revised down gradually, and we think there are some more to come.
- We tell you why we are holding our nose and upgrading this to a Buy.
- I am Trapping Value, and have over 20 years of experience generating options income while also focusing on capital preservation. Together with others, I run the Investing Group Conservative Income Portfolio, which features two income-generating portfolios and a bond ladder.

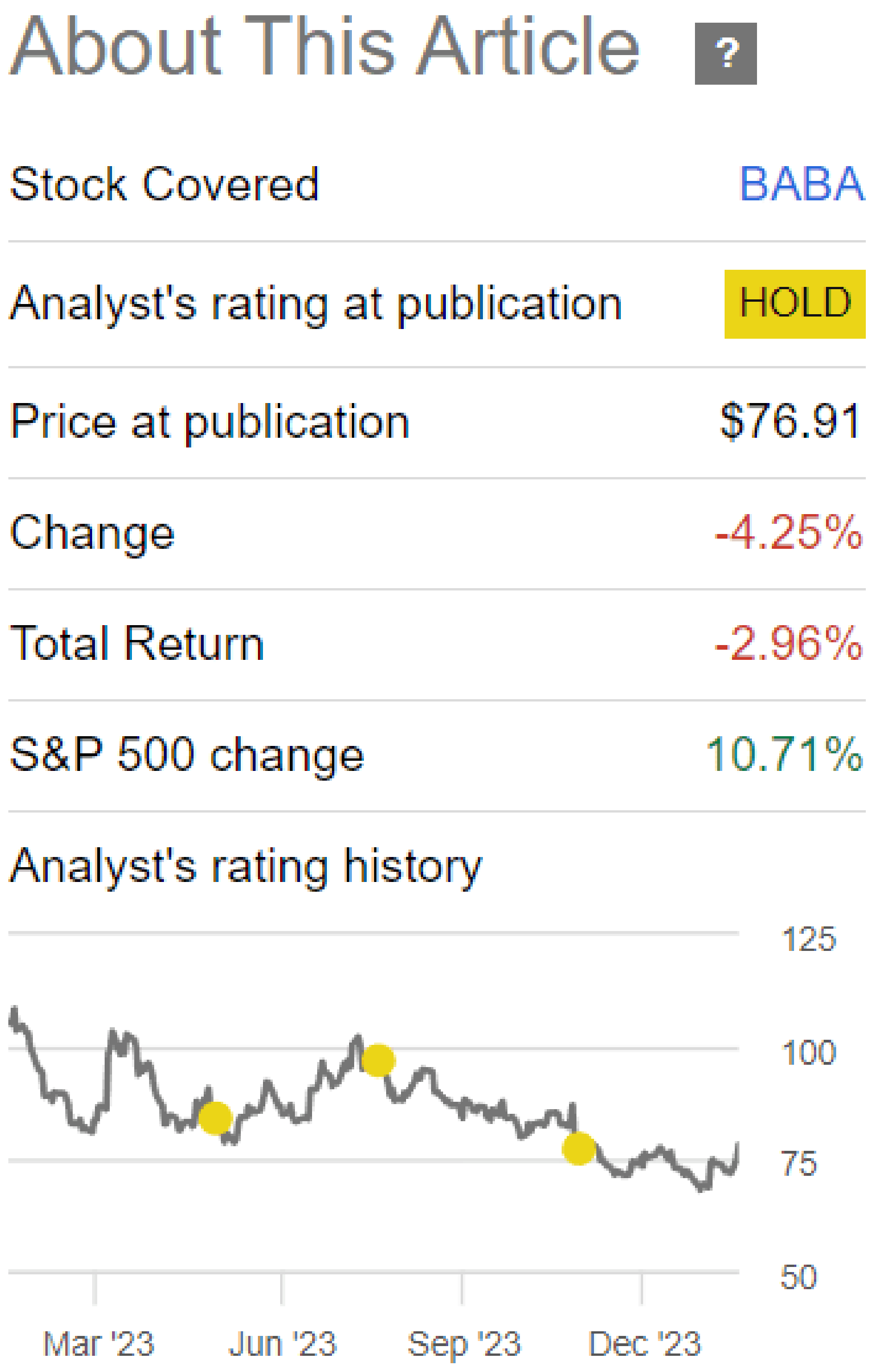
Jack Ma Trying To Find A New Bull Market In China

Chesnot/Getty Images News

On our last coverage of Alibaba Group Holdings Limited. (NYSE:BABA) we told you how the growth stock had morphed into a value play. While the temptation was strong, we stayed with a "hold" rating and did not buy. Our chief concern was the imploding housing bubble.

We think this being the largest bubble known to man, the fallout will span at least a decade as assets get repriced to consumer income. Retail sales remain vulnerable in such an environment. BABA maintains consistent profitability and high margins, relative to other online retailers like JD.com (JD). But that might be a problem in a weak economy as people turn price conscious. BABA's estimates here still look optimistic for what we see ahead. More disappointments are in store for 2024.
Source: You Either Die A Growth Stock, Or Live Long Enough To Become A Value Play

We did not regret sitting out.



Seeking Alpha

We now look at the recent results and update our thesis.

Schrodinger's Estimates?

This was one of those unusual cases where both the bulls and bears felt they were right.

Meanwhile, revenue grew about 5% year-over-year to RMB260.35B ($36.67B), beating estimates available at Seeking Alpha but missed analysts' expectations according to reports from Bloomberg News and Reuters.
Source: Seeking Alpha

Regardless of the actual numbers in relation to estimates, it is clear that forward estimates continue to be walked down gradually.

Annual Estimates Revisions

Upcoming Fiscal Year End - Revisions for Last 3 Months

EPS # of Up Revisions	EPS # of Down Revisions	Revenue # of Up Revisions	Revenue # of Down Revisions
6	24	5	40

Seeking Alpha
That is a lot of down revisions over the last 3 months. The cumulative impact has been modest on the front end, but heavier on some of the later years.

Fiscal Period Ending	Revenue Estimate	YoY Growth	1M Trend	3M Trend	6M Trend
Mar 2024	$129.97B	5.27%	-1.60%	-3.11%	-2.16%
Mar 2025	$142.56B	9.69%	-0.49%	-2.82%	-1.91%
Mar 2026	$154.12B	8.11%	-0.76%	-3.51%	-3.38%
Mar 2027	$165.24B	7.21%	-0.89%	-1.77%	0.59%
Mar 2028	$172.45B	4.36%	-0.31%	-2.70%	-12.84%
Mar 2029	$189.06B	9.63%	-1.76%	0.50%	-8.71%
Mar 2030	$186.15B	-1.54%	-0.67%	-15.96%	-16.26%
Mar 2031	$195.61B	5.08%	-0.67%	-17.15%	-17.42%
Mar 2032	$205.02B	4.81%	-0.67%	-18.26%	-36.07%

Seeking Alpha
Those are of course just guesstimates at best as probably no analyst is realistically forecasting a 9.63% growth in 2028 followed by a 1.54% decline in fiscal 2030. But we are now getting to a point where estimates are in the zip-code of realistic. We still need some more downgrades to the point where analysts basically throw in the towel on any growth. That will really setup BABA to surprise on the upside.

The Macro

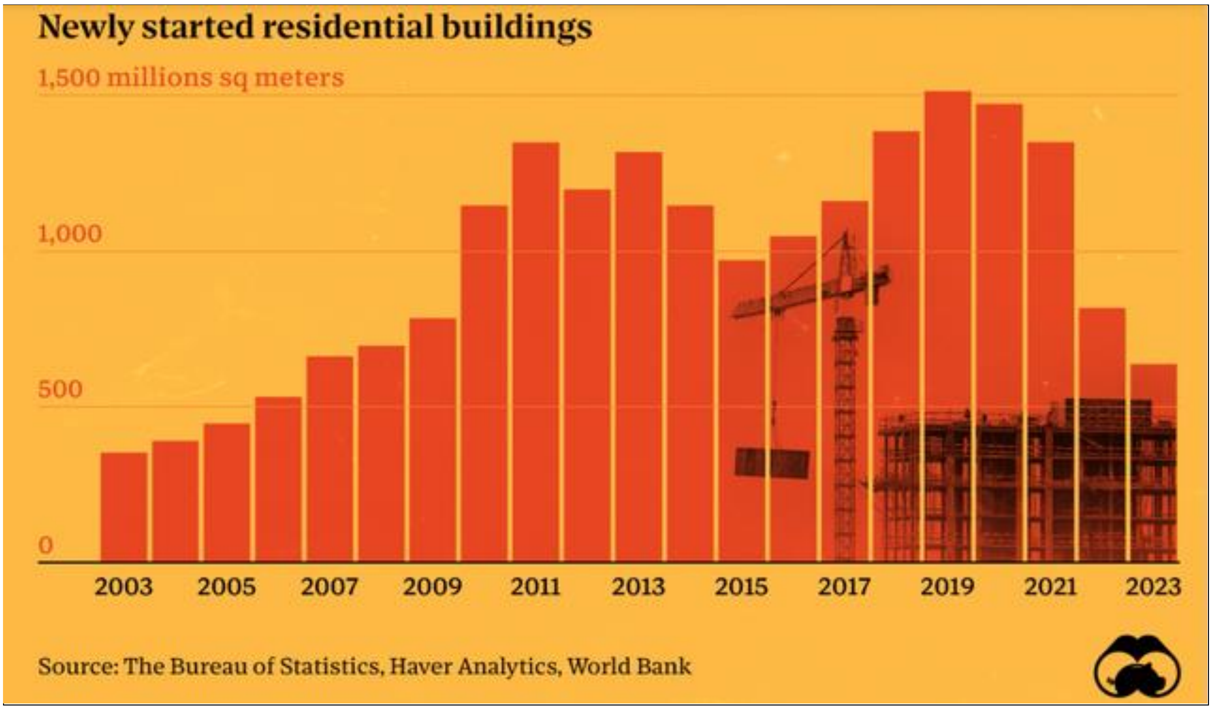
For the macro, there are two key parts. The first being the housing bubble update. It is not looking good to say the least and here is IMF jumping in with their thoughts.

"Home prices became significantly stretched relative to household incomes in the decade before the pandemic, in part because consumers preferred to invest their considerable savings in real estate given the scarcity of attractive alternative savings options," the IMF researchers said.

But expectations for ongoing price increases for land and homes led to overextended developers that borrowed too much and overpromised, which has ultimately fueled a collapse in real estate activity.

Housing starts have plunged by more than 60% compared to pre-pandemic levels, the IMF said, and weak confidence among homebuyers has led to a sharp drop-off in sales. ***The collapse has transpired at "a historically rapid pace only seen in the largest housing busts in cross-country experience in the last three decades," researchers said.***
Source: [Business Insider (Emphasis Ours)]

Shockingly, even after that big decline, China is building a lot of real estate that nobody will want.



Visual Capitalist

Apparently they were not clued in to the updated Field Of Dreams line "If you build it, they will sit empty."

This remains a big problem for investing as a lot of employment is tied to housing and a lot of wealth is also tied to this asset class. So you get the 1-2 punch here as deflation hits the sector. Chinese state and local governments are up to their eyeballs in debt and unless the Central Government steps in, things look bleak for the next decade.

The good news for BABA bulls is that the Central Government has decided that it needs to at least stop destroying what little consumer wealth is tied to the stock market. Just look at these headlines.

Financial Times

China removes head of market regulator as it battles stock meltdown

10 hours ago

Bloomberg.com

China Replaces Top Markets Regulator as Xi Tries to End Rout

14 hours ago

Google Search

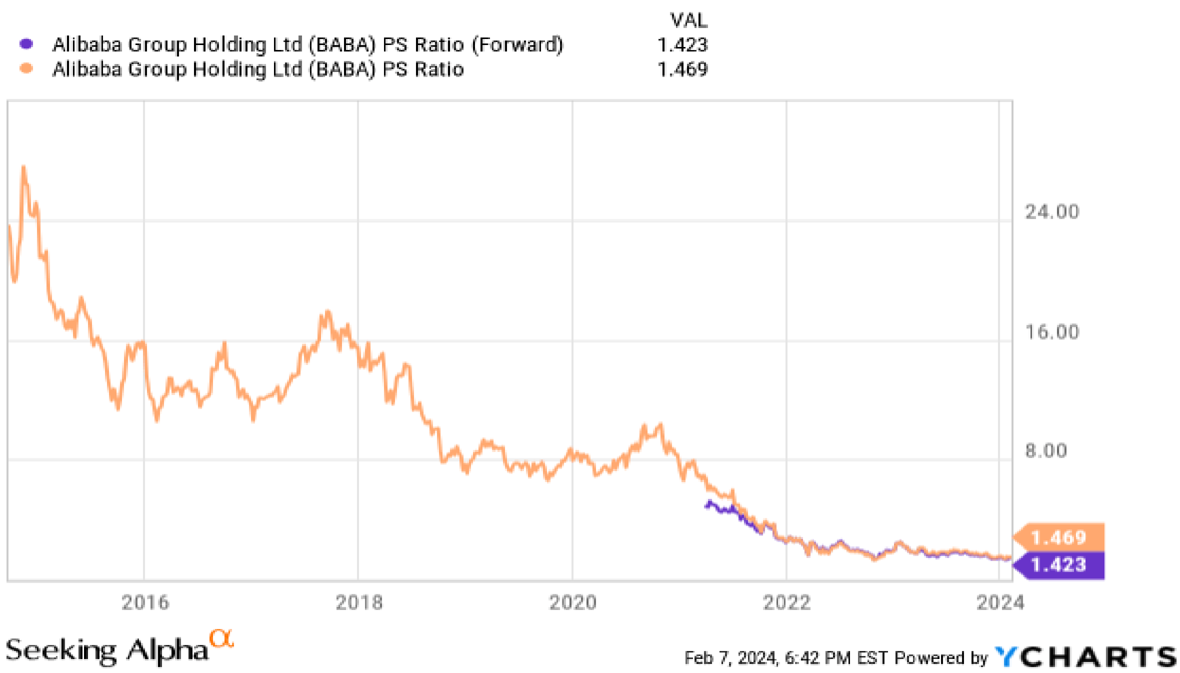
Yeah, China is trying to stop the stock market crash it created by vilifying all the mega cap companies. This may seem strange, but in essence this is a very big policy shift and the headlines have been raining in for at least 2 weeks. Will they succeed? Who knows. But at a minimum they are no longer aiming to bash everyone who made money and are trying their best to inflate a new bubble to deal with the fallout of the last one. Sentiment on Chinese stocks is abysmal and it is being called "uninvestable".

In the wake of Chinese authorities' desperate attempts to curtail a massive $2 Trillion stock market loss, over 40% of investors surveyed at a Goldman Sachs conference in Hong Kong deemed China "uninvestable." A decade of steady foreign inflows has given way to three years of losses, undermining confidence. While some Wall Street banks predict a rebound, global investors, wary of economic struggles, property crises, and diplomatic tensions, remain skeptical. The MSCI China index is down 60% from its 2021 peak, prompting questions about whether low valuations are enough to lure back hesitant investors.
Source: Biz News

There you have it. 60% down and 40% calling it uninvestable adds up to a 100% chance of success. Ok, the math does not work that way, but you get our point.

Verdict

BABA is cheap and has gotten cheaper since our last update.



Data by YCharts

It is of course the beauty of paying 24X sales at one point which has created the harrowing 10 year returns we see today. But this is cheap and even P/E ratios and price to tangible book value are screaming the same thing. Beijing is also on its side. The extremely large $25 billion buyback can materially swing things if it is executed. The key risk to the bull thesis is if profitability disappears when things get worse. It would be extremely unlikely for BABA, with the margins they have, but a recession does make it possible. But assuming they can hit their estimates below, we see material upside to the stock.

Fiscal Period Ending	EPS Estimate	YoY Growth	Low	High	# of Analysts
FQ4 2024 (Mar 2024)	1.23	-19.10%	1.23	1.23	1
FQ1 2025 (Jun 2024)	2.27	-5.68%	2.09	2.47	6
FQ2 2025 (Sep 2024)	2.19	1.48%	1.63	2.41	6
FQ3 2025 (Dec 2024)	2.85	7.91%	2.45	3.09	6

Seeking Alpha

We are raising this to a Buy, with a $90 price target in one year.

Please note that this is not financial advice. It may seem like it, sound like it, but surprisingly, it is not. Investors are expected to do their own due diligence and consult with a professional who knows their objectives and constraints.

Editor's Note: This article discusses one or more securities that do not trade on a major U.S. exchange. Please be aware of the risks associated with these stocks.

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