

PDD HOLDINGS INC

KWEB rebalancing may provide a good opportunity to accumulate further

We expect rebalancing selling by KWEB (KraneShares CSI China Internet ETF, which tracks CSI Overseas China Internet Index that covers most leading China Internet-related companies) after market close on December 8. The expected selling will be around US\$240m, or 22% of PDD's average daily trading value over the past one month, based on our calculation. The percentage suggests that the impact to the share price should be manageable. Any share price correction for PDD due to this event, instead of fundamental factors, would offer a good opportunity to accumulate further, in our view, especially after the 21% share price rally since its 3Q23 result (vs. KWEB -4%). OW.

- **What's new: KWEB US will need to dispose of a portion of PDD shares by December 11.** KWEB held 5.5mn shares of PDD US, equivalent to US\$790mn, accounting for 14.4% of total net assets as of December 5, 2023, according to its official website ([link](#)). This has surpassed the 10% weighting threshold of this index, which we believe is mainly due to PDD's strong stock outperformance recently (PDD US up 30% in the past month, vs. KWEB down 2%). As a result, KWEB will have to dispose of over 25% of its total holdings of PDD US as of December 11, the next factor-adjusting day.
- **KWEB index methodology recap.** Based on the rulebook of KWEB, each component stock is weighted using 10% capping methodology, i.e. no constituent's weight should exceed 10% at each rebalance, and top 5 constituents are capped at 40%. The index constituents are adjusted semi-annually, on the next trading day post the second Friday in June and December each year, while weighting factors are adjusted monthly, on the next trading day post the second Friday in each month.
- **A more comfortable accumulation opportunity for long investors likely in the near term.** As passive indexes need to adjust their holdings when the market closes on December 8 to have the appropriate amount of shares in their portfolio by the next trading day, we believe the share disposal will create non-fundamental correction, offering a more comfortable accumulation opportunity for long investors, especially after the 21% share price rally since the much-better-than-expected 3Q earnings result (vs. KWEB -4%).

Overweight

PDD, PDD US

Price: \$143.46

05 Dec 2023

Price Target: \$180.00

PT End Date: 31 Dec 2024

Internet

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Investment Thesis

We expect PDD's share price in the next six to 12 months to continue the outperformance, as more investors switch the valuation framework from P/E to a sum of the parts (SOTP) or simply assign a higher group P/E, because its international business Temu has emerged as the second growth curve that few major China Internet peers have secured. Our confidence to price in Temu's valuation is based on our analysis that supports Temu's GMV to grow at a 50%+ CAGR during 2023-27E and turn profitable with a 3% net margin by 2027. We believe PDD's consistent market-share gains in China on a value-for-money proposition should ensure its China profit maintains a 20% CAGR in the next two years, which would support the valuation/share price before there are more datapoints confirming Temu's GMV growth/unit economics (UE) improvement. OW.

Valuation

Our Dec-24 PT of US\$180 is based on 18x 2024E P/E for China business (in line with leading China Internet peers that don't face risks of market-share loss/revenue decline) and 20x 2027E P/E for Temu (discounted at 15%). Our PT also translates to 25x 2024E P/E, at the high-end of all major China Internet peers' range, based on Bloomberg consensus estimates.

Risks to Rating and Price Target

Key downside risks to our rating and price target include: 1) a worse-than-expected deceleration of revenue growth due to competition and/or the macro environment; 2) more aggressive investments in Temu without matching ROI; and 3) resurfacing ADR delisting risk due to US-China tensions.

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PDD HOLDINGS INC (PDD, PDD US) Price Chart



Date	Rating	Price (\$)	Price Target (\$)
20-Jan-21	OW	168.79	200
19-Mar-21	OW	141.82	190
27-May-21	OW	123.57	160
12-Aug-21	OW	89.61	130
29-Nov-21	OW	68.46	105
14-Mar-22	UW	32.13	23
23-Mar-22	UW	47.53	27
16-May-22	OW	37.72	55
29-May-22	OW	48.30	65
30-Aug-22	OW	66.04	100
29-Nov-22	OW	74.05	110
30-Aug-23	OW	93.22	120
30-Nov-23	OW	141.73	180

Source: Bloomberg Finance L.P. and J.P. Morgan; price data adjusted for stock splits and dividends.
Initiated coverage Jul 09, 2019. All share prices are as of market close on the previous business day.

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