

Is mobile payment too important to miss?

China Internet pulse: Baidu joins competition in mobile payment

Baidu recently launched a payment solution, Baidu Wallet, following Tencent's launch of Weixin Payment seven months ago. Baidu's entrance indicates that all of the heavyweight Internet platforms view mobile payment as too important to miss. We believe mobile payment is one of the most important ingredients for success in mobile commerce and online-to-offline (O2O) activities, as it: (1) allows platforms to build scalable revenue models (revenue share, commission, etc.); (2) increases platforms' bargaining power as volume grows; and (3) allows platforms to collect and analyze user data and behavior. While the competitive landscape in China's mobile payment market might continue to evolve, we expect the entrance of Baidu, along with the incumbent, to further drive consumer and merchant adoption of mobile payment. This will enable Internet names to tap opportunities in mobile commerce and O2O. **Maintain OW on Baidu and Tencent.**

How mobile payment fits into Baidu's and Tencent's mobile ecosystems. We believe mobile payment enables Baidu to expand its scope from a pure traffic generator on mobile Internet into the facilitation of actual transactions, potentially through two approaches: (1) closed-loop transactions enabled by mobile search, light apps and payment solutions, e.g., users could search for train tickets on Baidu mobile, select/purchase tickets within light apps and make payment via Baidu Wallet; (2) LBS transactions from Baidu's O2O initiatives, e.g., points of interest from map search and group buy (Nuomi). For Tencent, Weixin Payment solutions were integrated into the vertical services from level one access such as Didi Dache and Dianping, which enables in-app payment; Tencent also offers Weixin Payment to its 2+ million public accounts to facilitate transactions within Weixin.

Promoting user adoption of mobile payment. We witnessed Internet companies' more aggressive push for user adoption of mobile payment through offline campaigns and more innovative approaches, such as: (1) subsidies in key O2O apps, e.g., taxi-hailing; (2) event promotion, e.g., Baidu Nuomi claimed a Rmb100 million promotion on March 7 (Girl's Day in China) to offer special discounts on group buy products, including KTV, movies, restaurants, etc.; (3) bundling with online virtual items, e.g., passengers who use Didi Dache and make payment via Wechat 10 times per week receive a Wechat game "WeFly" gift package; and (4) utilizing social networks to enable social sharing, e.g., Weixin users can now share their locations on "Moments," which shows the specific restaurant users are at.

Bring merchants on board with attractive fee structure. Baidu and Tencent are offering attractive fees to bring merchants on board. As shown in Table 1, Weixin Payment charges a 0.6% fee from transaction value. Baidu Wallet claims to be free of charge on PCs and charges 12% off the lowest fee in the industry on mobile, which translates into a 0.528% fee using Weixin Payment as a benchmark.

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Internet

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China Internet top picks

Stock	Rating	Price (LC)	PT (LC)	P/E (x)	
				14E	15E
Tencent	OW	509.5	640	28	21
Qihoo	OW	90.8	165	37	23

Source: J.P. Morgan estimates, Bloomberg.

Stock views

	Ticker	Rating	Price (LC)	PT (LC)
Baidu	BIDU US	OW	151.0	210
Sina	SINA US	OW	55.3	92
Tencent	700 HK	OW	509.5	640
SouFun	SFUN US	OW	13.9	19.6
Qihoo	QIHU US	OW	90.8	165
Phoenix New Media	FENG US	OW	10.0	16
YY	YY US	OW	69.2	105
Vipshop	VIPS US	OW	142.6	200
Forgame	484 HK	OW	40.1	58
Ctrip	CTRP US	OW	55.5	52
Sohu	SOHU US	N	62.1	68
NetEase	NTES US	N	67.2	73
Youku	YOKU US	N	25.0	26
Sungy Mobile	GOMO US	N	20.9	17
Dangdang	DANG US	UW	12.9	7.5

Source: J.P. Morgan estimates, Bloomberg. Prices are as of April 8, 2014.

Offline incumbent that is likely to be disrupted. China's offline clearing and settlement market is dominated by UnionPay. In 2013, the clearing house processed Rmb32 trillion of China's inter-bank settlement and clearing transactions. We believe the prevailing offline POS terminal payment solution will see increasing challenges from mobile payment, given the latter's attractive fees for merchants (Tables 1 and 2 compare fee structures) and better user experience for customers. However, we believe regulatory risk remains a near-term overhang for mobile payment operators.

Table 1: Payment fee structure comparison between Baidu and Tencent

Company		PC payment				Mobile payment		
Tencent	PC basis pricing (Tenpay)			PC package-based pricing (Tenpay)				Weixin payment pricing
	Transaction value	Fees (%)	Deposit	Transaction allowance	Implied fees (%)	Excess fees (%)	Transaction value	
	0	Any amount	1.00	480	50K	0.96	1.00	
				1680	200K	0.84	1.00	
				3750	500K	0.75	1.00	
				7000	1mn	0.70	1.00	
Baidu	PC pricing (Baidu Wallet)			Mobile pricing (Baidu Wallet)				Weixin payment pricing
	Transaction value	Fees (%)	Deposit	Transaction value	Fees (%)	Deposit	Transaction value	
	0	Any amount	0	0	Any amount	0.528 ⁽¹⁾		

Source: Company data, J.P. Morgan. Note: All amounts in Rmb. (1) Baidu Wallet claims to charge fees 12% off industry-lowest fees on mobile; we use Weixin's 0.6% as a benchmark.

Table 2: POS machine charging structure

Category	Total fees (%)	Fee split (%)		
		Card-issuing bank	Acquiring bank	UnionPay
Meal/entertainment: Catering, Entertainment, Jewelry, Crafts, Property, Auto, etc.	1.25	0.9	0.22	0.13
General goods: Department stores, Wholesale, Social training, Agents, Attraction tickets, etc.	0.78	0.55	0.15	0.08
Livelihood of people: Supermarkets, Hypermarkets, Utilities, Refueling, Transportation tickets, etc.	0.38	0.26	0.08	0.04
Public Welfare: Public hospital, public school, etc.	0	0	0	0

Source: NDRC, J.P. Morgan.

Companies Discussed in This Report (all prices in this report as of market close on 08 April 2014, unless otherwise indicated)

Baidu.com (BIDU/\$150.96/Overweight), Qihoo 360 Technology Co. Ltd (QIHU/\$90.84/Overweight), Tencent (0700.HK/HK\$523.50[09 April 2014]/Overweight)

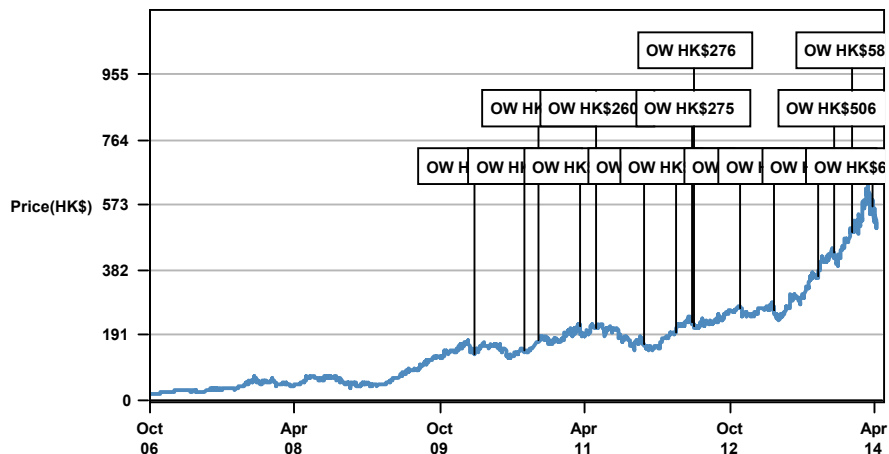
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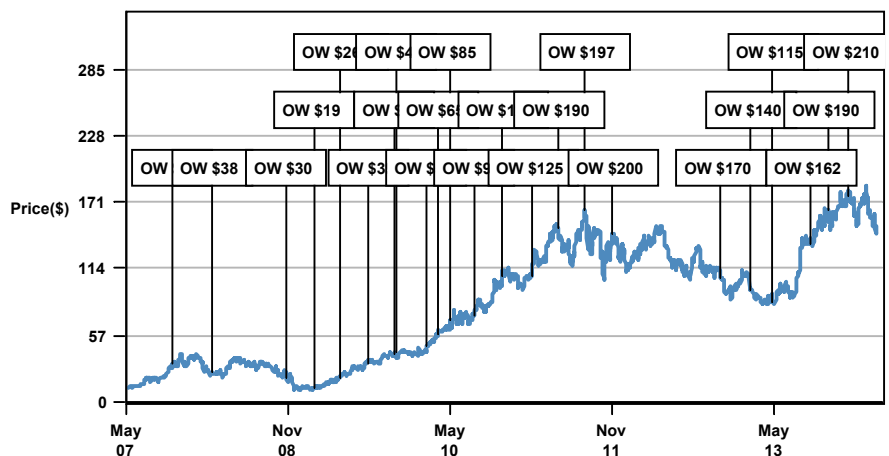
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Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.
Initiated coverage Feb 07, 2010.

Date	Rating	Share Price (HK\$)	Price Target (HK\$)
07-Feb-10	OW	137.70	180.00
12-Aug-10	OW	148.70	175.00
10-Oct-10	OW	176.10	205.00
17-Mar-11	OW	216.80	240.00
12-May-11	OW	209.80	260.00
10-Nov-11	OW	164.90	230.00
15-Mar-12	OW	200.60	240.00
08-May-12	OW	230.80	275.00
17-May-12	OW	219.60	276.00
10-Nov-12	OW	270.60	306.00
21-Mar-13	OW	262.80	300.00
30-Aug-13	OW	361.80	433.00
27-Oct-13	OW	433.00	506.00
07-Jan-14	OW	494.00	580.00
20-Mar-14	OW	567.50	640.00

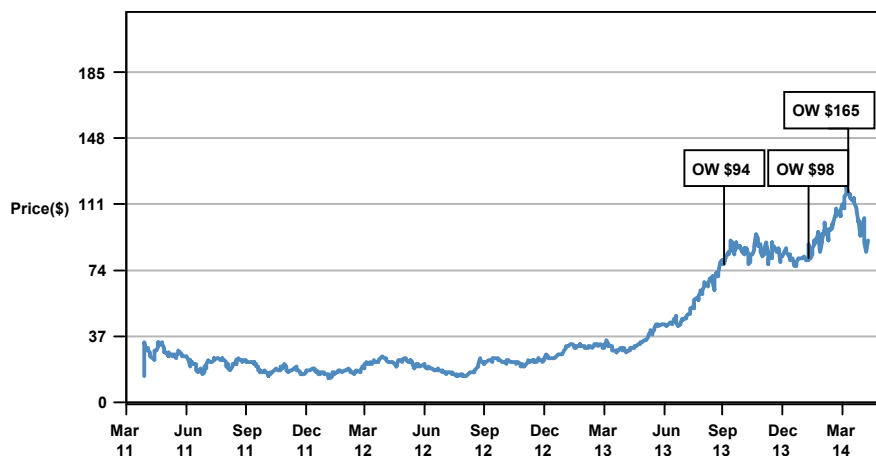
Baidu.com (BIDU, BIDU US) Price Chart



Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.
Initiated coverage Oct 02, 2007.

Date	Rating	Share Price (\$)	Price Target (\$)
02-Oct-07	OW	32.06	40.00
14-Feb-08	OW	26.45	38.00
23-Oct-08	OW	21.25	30.00
23-Jan-09	OW	11.20	19.00
23-Apr-09	OW	20.83	26.50
24-Jul-09	OW	33.26	39.00
22-Oct-09	OW	41.56	48.00
27-Oct-09	OW	43.30	46.00
10-Feb-10	OW	48.21	54.00
23-Mar-10	OW	57.97	65.00
29-Apr-10	OW	70.99	85.00
22-Jul-10	OW	73.31	90.00
22-Oct-10	OW	107.28	120.00
02-Feb-11	OW	108.63	125.00
28-Apr-11	OW	148.25	190.00
26-Jul-11	OW	164.36	197.00
28-Oct-11	OW	144.62	200.00
30-Oct-12	OW	106.73	170.00
05-Feb-13	OW	96.37	140.00
26-Apr-13	OW	85.02	115.00
30-Aug-13	OW	135.53	162.00
30-Oct-13	OW	164.93	190.00
07-Jan-14	OW	176.63	210.00

Qihoo 360 Technology Co. Ltd (QIHU, QIHU US) Price Chart



Date	Rating	Share Price (\$)	Price Target (\$)
30-Aug-13	OW	77.93	94.00
07-Jan-14	OW	81.40	98.00
10-Mar-14	OW	118.31	165.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.
Initiated coverage Aug 30, 2013.

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