[DDL] Dingdong (Cayman) Limited
Q4 2022 Earnings Conference Call
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Executives:
Changlin Liang, Founder and Chief Executive Officer
Le Yu, Chief Strategy Officer
Nicky Zheng, Director of Investor Relations

Analysts:
Joyce Ju, Bank of America Securities
Ashley Xu, Credit Suisse
Thomas Chong, Jefferies
Robin Leung, Daiwa

Presentation

Operator: Good morning and good evening, ladies and gentlemen. Thank you for standing by, and welcome to the Dingdong Ltd. Fourth Quarter 2022 Earnings Conference Call. (Operator Instructions). Please note that this event is being recorded.

I will now turn the conference over to the first speaker today, Nicky Zheng, Director of Investor Relations. Please go ahead.

Nicky Zheng: Thank you. Hello, everyone, and welcome to Dingdong's fourth quarter 2022 earnings call. With us today are Mr. Changlin Liang, our founder and CEO, and Ms. Le Yu, our CSO.

You can refer to our fourth quarter 2022 financial results on our IR website at ir.100.me. You can also access a replay of this call on our IR website when it becomes available a few hours after its conclusion.

For today's call, management will provide their prepared remarks first, and then we will be hosting a question-and-answer session.

Before we continue, I would like to refer you to our safe harbor statement in our earnings press release, which also applies to this call, as we will be making forward-looking statements. Please note that all numbers stated in the following management's prepared remarks are in RMB terms, and we will discuss non-GAAP measures today, which are more thoroughly explained and reconciled to the most comparable measures reported in our earnings release and filings with the SEC.

I will now turn the call to our first speaker today, the founder and CEO of Dingdong, Mr. Liang.

Changlin Liang: (Speaking foreign language).

(Translated). Thank you, everyone, and welcome to Dingdong's fourth quarter 2022 earnings conference call. Let's first review the quarter's operational results.

Our revenue of 6.2 billion reflected 13.1% year-over-year growth. We recorded GAAP net profit for the first time of 49.88 million, with non-GAAP net profit of 116 million.

Within 1.5 years, we grew from a net loss margin of 37.2% to a net profit margin of 1.9%. It is a result of our dedication and validates the strategy of Efficiency First with due Consideration of Scale.

Meanwhile, our operating net cash inflow in Q4 was 0.68 billion. We also achieved positive operating cash flow for the full year of 2022. As of December 31, 2022, our cash and cash equivalents were 1.86 billion, and short-term investments were 4.64 billion. We believe that this strong cash position speaks volumes about our resilience in adversity. We also firmly believe that we will be able to realize our vision and mission, create value for our consumers and society, and create long-term and sustainable value for our shareholders.

In addition, we also advanced our product development capability through direct sourcing, contract farming, in-house R&D and production, and private labels, forming a flywheel effect.

In 2022, we kept growing existing strong categories, such as prepared food and children's food (i.e., Mom's Choice), forming a number of differentiated Dingdong-exclusive products with monthly sales of over 3 million RMB each. Moreover, foreseeing the clean labeling trend in the food industry, we created about 320 quality products with clean labeling attributes. We refined our customer profiling according to consumption scenarios and built the “Qingyang Planet” page for younger-user cohorts to meet the increasingly precise needs of the millennials and Gen Zs in body management, nutrition, and health.

Next, I would like to share with you my thoughts and ideas. Dingdong is a startup that is dedicated to providing safe, healthy, and delicious food while innovating to improve people's lives. We firmly believe in building a better life and creating value for consumers and society, instead of engaging in a zero-sum game with our peers for users and market share.

As the Seed Theory suggests, an infinite number of small things combine to create the universe. Therefore, we dream big and start small while remaining resilient to counteract vulnerability and entropy. During this process, we stay true to our roots and remain disciplined while keeping an easy mind. These beliefs and convictions go beyond profitability. They are what fuel our passion and drive us forward, guaranteeing our achievements today and in the future.

I would also like to discuss our plans for 2023. In early January, the company held its annual management meeting, where we summarized the experience and lessons we have learned since our inception and made plans for the longer-term future. We also agreed that we would hold course on our current development strategy while remaining innovative. Specifically speaking, we will deepen our penetration into existing markets and continuously tap into our users' needs to achieve profitability. At the same time, we will emphasize innovation, particularly in food products, to develop and launch new food products catering to a broader range of users.

In 2023, given the increased demand for healthier food products post-pandemic, we plan to promote product innovations across several areas to address the changing needs. These areas include the increased use of clean labeling, nutritional upgrades, and customizing health food products for specific demographics. Specifically speaking, we will first develop healthier prepared food that is not only delicious, but cooked with little or no oil and are low in calories, salt, and sodium. We will take the lead in promoting products with clean labels.

Second, we will improve the nutritional value of foods and beverages. For example, we will bring out low-GI rice and pasta, low-carb bakery products, low-carb beer, high-fiber beverages, and low-fat and low-sodium seasonings. Third, we will develop powerful functional foods and nutrition products for children, middle-aged and senior citizens. Finally, for millennials and Gen Z who are weight-and-health conscious, we have launched the “Qingyang Planet” page that can quickly generate a healthy diet plan that matches individual needs with calculated and archived calorie data.

Another one of our goals for 2023 is to strengthen our strategic cooperation with our suppliers. In late February, we will hold a supplier conference to commend our product developers, suppliers, and service providers for their excellent products. We are highly aware that it takes a large number of exceptional companies to meet the ever-changing needs of consumers in a market as vast as China's. Dingdong is willing to be an enabler that connects great companies to create value for consumers and society.

2023 marks the end of 3 years of the pandemic. We expect drastic changes in consumer demand. Nonetheless, we will respond proactively and strengthen our capabilities in product development, service provision, and supply chain building. Based on our current operating situation, we expect to maintain non-GAAP profitability for both Q1 and the full year of 2023.

Today is February 13th, and spring has come. Everything is sprouting and growing despite the cold weather, just like the situation in China. We are fully confident in the recovery and growth potential of the post-pandemic economy in our country and in our cause.

This concludes my speech.

Next, I would like to invite Ms. Yu Le, CSO of the company, to introduce the financial results. Thank you all.

Le Yu: Thank you, Mr. Liang, and hello, everyone. Before I walk you through our detailed financial results, please note that all numbers stated in the following remarks are in RMB terms.

Product development capability has become Dingdong's core strength and primary growth driver since we implemented the strategy of “efficiency first, with due consideration of scale” in Q3

2021. As a result, we maintained quality growth in 2022, with annual revenue of 24.22 billion, up 20.4% year-over-year.

Meanwhile, we significantly optimized our operating efficiency, gross margin, and net loss margin. The conversion rate from GMV to revenue was 92.3%, increasing by 3.7 percentage points from a year ago.

Non-GAAP net loss margin was 2.4%, a substantial improvement of 28 percentage points year-over-year. We also achieved positive operating cash flow for the full year of 2022.

Looking ahead to 2023, we are confident that we can achieve a full-year non-GAAP break-even.

Now, let's look at the financial results of Q4 2022. Our revenue reached 6.2 billion, up 13.1% year-over-year.

We are also pleased to report a record positive net margin of 0.8% under GAAP, and a non-GAAP net margin of 1.9%, both significantly exceeding the forecast made in Q3. Since we shifted our strategic focus to Efficiency First in Q3 2021, our non-GAAP net margin has improved by 33.8 percentage points from a net loss of 31.9% to a net profit of 1.9%, which was achieved in less than a year and a half. Such a rapid and significant optimization is a testament to the vitality and profitability of the frontline fulfillment grid model in fresh grocery e-commerce. It also shows the effectiveness of deeply developing and engaging our supply chain and centering on product development capability. We expect to stand by these strategies for a long time to come.

In Q4, the gross margin was 32.9%, up 5.2 percentage points from a year ago, and the gross profit was 2.04 billion, up 34.2% year-over-year. We deepened our partnerships with many upstream producers to advance our fresh grocery products. For the non-fresh groceries, we focused on building private labels, in-house R&D, and self-production and processing in our assembly lines. We also offered door-to-door delivery services, capturing higher downstream margins. Such extensive coverage of the whole supply chain generated a stable gross profit margin for the company.

The fulfillment expense ratio in Q4 was 24.1%, down 8.5 percentage points year-over-year, reflecting Dingdong's higher operational efficiency in Q4.

The sales and marketing expense ratio in Q4 was 1.5%, down 5.1 percentage points, driven by our product development capability that generated continuous organic traffic. Consumers came and stayed for the differentiated Dingdong-exclusive products, which also lowered the acquisition cost per new transacting user by 47.7% year-over-year and 26.1% quarter-over-quarter.

G&A expense ratio remained stable at 2.4% compared to the same quarter last year. Benefiting from the scaling effect, we optimized the R&D expense ratio to 4.2% from 5.2% year-over-year. As always, we will keep investing in the infrastructure R&D, such as food development, agricultural technology, and technical data algorithms, which will forge a greater advantage for the company.

In Q4, we achieved a positive GAAP net margin of 0.8% for the first time, optimized by 20.8 percentage points from a year ago, and a non-GAAP net margin of 1.9%, optimized by 20.7 percentage points year-over-year, significantly exceeding the forecast.

Additionally, Covid-19 had only mildly impacted our covered cities and regions in October and November, and our Q4 entered a trajectory of profitability in October. To break it down monthly, we achieved a positive non-GAAP net profit in October and a positive GAAP net profit in November and December.

It's been 5 years since Dingdong was founded in 2017, and we are pleased to see our efforts pay off and our business model proven.

The operating cash inflow in Q4 was 682 million, and the actual operating cash inflow was increased to 906 million through the introduction of supply chain finance. As of the end of Q4, the balance of cash, cash equivalents, restricted cash, and short-term investments was 6.5 billion.

According to CIC, the size of China's food and other groceries market was 11.9 trillion in 2021. Let's take Shanghai as an example. With a residential population of about 25 million, Shanghai's annual food consumption expenditure is about 10,000 per capita. In 2022, our GMV in Shanghai was over 12 billion. That translated to a 5% penetration rate in Shanghai's food consumption market. We are confident of doubling that number in the long term, generating annual revenue of over 20 billion in the city alone. In addition, the total consumption of our current cities and regions is about 5x that of Shanghai, which, in the long term, would create 100 billion in annual revenue. That is why Dingdong has a high-growth ceiling.

As we move ahead to 2023, we would like to discuss our outlook. Q1s are typically affected by seasonality, according to our track record, with lower revenue and profitability. In Q1 2023, we expect a slow season for urban fresh grocery consumption due to the pent-up urge to return home and travel during the Chinese New Year. Nevertheless, despite the seasonality impact and extra frontline labor costs on holidays, we are confident of achieving non-GAAP breakeven for both Q1 and the whole year of 2023.

This concludes our prepared remarks for today. Operator, we are now ready to take questions.

Questions and Answers

Operator: We will now begin the question-and-answer session. (Operator Instructions). Joyce of Bank of America Securities.

Joyce Ju: (Speaking foreign language). Congrats on the profit-making this quarter. As we all know, in the past couple of months, there were actually a lot of constraint in terms of social activities because of the pandemic. Just trying to understand to what extent the profitability this quarter was because of the pandemic control. How should we expect the profitability outlook for this year or going forward? Is this going to be at the same trend of profit making?

Changlin Liang: (Speaking foreign language).

(Translated). Ms. Yu, please take the question.

Le Yu: (Speaking foreign language).

(Translated). Thank you, Joyce, for your question. First of all, since Q3 in 2021, Dingdong has been committed to efficiency, firmly moving towards profitability step-by-step. Our gross profit margin in Q4 of 2022 was up nearly 15 percentage points compared with Q3 in 2021, which was achieved within 1.5 years. More than 13 percentage points have been optimized in the fulfillment expense ratio, and over 5 percentage points in the marketing spending ratio. As mentioned in the prepared remarks, our non-GAAP net profit margin went up more than 33 percentage points. The ability to optimize the P&L so efficiently has validated the vitality and profitability of Dingdong's business model.

Now let's look at the Q4 results. In Q4, over 80% of our entered cities achieved positive operating profit at the city level. On a monthly basis, in November 2022, when the pandemic had a mild impact on our covered cities and regions, we achieved a GAAP net profit of more than 10 million. Moreover, we expect this profitability to be sustainable and stable, allowing us to achieve non-GAAP breakeven in Q1 of 2023, and even the whole year of 2023.

Now, if we look at the structure of our P&L, gross profit margin and fulfillment expense ratio are two key elements. Their optimization is because we have been committed to the construction of the supply chain and our product development capability for a long time to build our strength. Such long-term investment has objectively improved our gross profit margin over time. Meanwhile, within 1.5 years, the delivery riders' efficiency has increased by more than 25%; the frontline warehouse staff efficiency has grown by more than 40%, with utility bills down by more than 20% year-over-year, which in turn led to the rapid optimization of our fulfillment expense ratio. These are the fundamental drivers of our P&L optimization.

Regarding the pandemic as an impetus to the business, it was more on the overall online penetration rate. Because during the pandemic, the insufficient supply in the traditional market gave users a good opportunity to experience Dingdong's differentiated products in depth. On the other hand, our operation experienced many challenges in the face of the pandemic control, such as the unsmooth supply chain, relatively difficult recruitment, restricted order fulfillment and some additional expenses incurred for pandemic prevention. These difficulties will be resolved when the pandemic control loses out.

In summary, the above-mentioned results have validated that Dingdong's business model is welcome in the market, and can generate value for users and society. Therefore, our profitability is sustainable. Thank you.

Operator: Ashley Xu of Credit Suisse.

Ashley Xu: (Speaking foreign language). We have seen it's reported that Dingdong Guyu has been developing and manufacturing food products. Would management share more color on this?

Changlin Liang: (Speaking foreign language).

(Translated). Thank you for your question. Dingdong is a start-up committed to providing healthy, delicious and innovative food products to improve people's lives. We firmly believe that product development capability is our core strength. Therefore, in addition to jointly developing quality and differentiated foods with partners, Dingdong is also innovating, developing and producing processed food products. This is what Dingdong Guyu is doing.

Currently, Guyu's sales accounted for 11.4% of Dingdong's GMV. For the past 2 years, Guyu has created many popular brands such as Daily Fresh, Dingdong Damanguan, Boxing Crayfish, Black Diamond Family and Bao's Bakery. Product quality has always been a priority in Guyu. In 2022, the moderate or bad reviews on Guyu's products were 40% less than the whole company's. Guyu's products also had a 100% passing rate for inspection. In December 2022, Guyu had 80 SKUs with monthly GMV exceeding 1 million each.

Compared with 2021, Guyu's GMV has more than doubled in 2022. Guyu is growing rapidly, and is expected to have higher revenue, which will add greater value to the company's product development capability. Thank you.

Operator: Thomas Chong of Jefferies.

Thomas Chong: (Speaking foreign language). Just in the prepared remarks, management talked about and summarized the experiences and lessons that we learned since we started business. Can management share about these experiences and lessons?

Changlin Liang: (Speaking foreign language).

(Translated). Thank you for your question. At the management meeting in January, we summarized our experience of the past 6 years, and realized that the times and environment were changing. Dingdong has also entered a different stage of development; we must learn from the past practices to avoid future mistakes. We have the following three conclusions: First, we have achieved a scale of sales resulting from our previous hard work. By leveraging the scale, we can serve and understand our customers better. With a deeper understanding of the consumers, we can also develop and innovate food while enabling our partners to create value for consumers and society with us together.

Second, unlike our peers, we have never been indecisive regarding specific business models. While our peers constantly doubted their existing model, switching things up and trying to find the optimal solution, we knew that the essence of our business was to serve consumers more conveniently with better products. So we adopted the simplest and most convenient frontline fulfillment grip model. Sometimes the best way is the most straightforward, not the strangest or the most surprising one.

Third, based on the understanding of our business model, we have been deeply engaging the supply chain. These efforts include direct sourcing, contract farming, food R&D and processing, building regional centers, establishing a quality control mechanism and so on. The construction of the supply chain is time consuming, and the investment is relatively large, so it may not be able to produce outcomes immediately. However, in the long run, it will allow us to serve consumers better and form a competitive moat.

At the same time, we have also summed up the mistakes to avoid, which were born out of an aggressive user base and scale expansion by using low prices and excessive marketing to attract bargain hunters. These activities brought false prosperity to the company that didn't last. Haste makes waste. The business we are engaged in is very grounded and requires us to be more patient. We need to cultivate the supply chain and product development capability for the longer run without haste.

Operator: Robin Leung of Daiwa.

Robin Leung: (Speaking foreign language). Management mentioned in the prepared remarks that I think they will strengthen the collaboration with our partners. Could management share more on these partnerships?

Changlin Liang: (Speaking foreign language).

(Translated). In the huge market with ever-changing consumer needs, we need to expand our partnership to create value for users. Therefore, we will break through the traditional party A and party B relationships between suppliers and retailers and support each other in depth.

Regarding the business model, we will allow joint operation on certain categories with our partners to leverage everyone's strengths. On the technology side, we'll actively contribute to big data and IT technology to improve cooperation, efficiency in the partnership. Furthermore, we'll develop and innovate supply chain finance more vigorously at a financial level to support our partners. At the same time, we'll proactively consider investing in certain excellent partners. In addition, Dingdong itself is a startup that has always been innovative. That's why we plan to support actively innovating partners in areas such as user surveys, testing, initial product iterations, and marketing among others.

In the nearly 6 years of Dingdong's operation, we have also established very good cooperative relationships with many excellent companies; this is because we share similar values, mutual trust, support and responsibility.

Especially during the 3 years of the pandemic, we overcame many difficulties together to fulfill the promise to consumers. These excellent partners are a reliable guarantee for Dingdong's continuous progress, and they are also valuable resources that we have accumulated in the past 6 years. In 2023, we'll partner with more exceptional companies around the world. Thank you.

Operator: As there are no further questions at this time, I'd like to hand the conference back to our management for closing remarks.

Nicky Zheng: Okay. Thank you for joining our call today. If you have any further questions, please feel free to contact us or request through our IR website. We look forward to speaking with everyone in our next earnings call. Have a good day.

Operator: The conference has now concluded. Thank you for attending today's presentation and you may now disconnect.