

### 111, Inc.

#### YI: Profitable Amid Macroeconomic Challenges

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#### KEY POINTS

- 111 remains profitable despite macroeconomic headwinds.** China's 2Q24 GDP growth of 4.7% was noticeably softer than general expectations of 5%, with consumption being a particular weak spot of the economy. Consumer spending growth has been decelerating since 1Q23, slowing to 2% in June 2024, its weakest level since the end of pandemic restrictions in December 2022. Offline pharmacies have not been immune to tightening consumer purse strings. Consequently, 111 could not prevent a modest 1.5% Y/Y drop in revenue for the quarter to \$3.4 billion. Still, these headwinds failed to prevent the company from achieving its goal of maintaining operating profitability. 111 duly reported an operating profit for the second consecutive quarter: Non-GAAP RMB8.5 million and GAAP RMB3.3 million versus reported losses of RMB17.2 million and RMB41.4 million, respectively, for the year-ago quarter.
- Profitability primarily driven by enhanced efficiency.** Ongoing improvements in operational efficiency have been supported by consistent technology-driven enhancements across nearly all business functions. These include data-driven merchant bidding tools to enhance procurement efficiency, the optimization of algorithms to improve supply chain fulfillment efficiencies, and the application of AI for increasing accuracy in product matching. 111's success in delivering efficiency improvements was again evident in 2Q24. Gross margin was up to 6.1% from 6% in 2Q23, and despite the shrinkage of revenue from its small B2C business, gross margin saw a 220-bp Y/Y improvement to 24%. This matches or betters the gross margin reported by the larger established players in this segment of the e-market. Meanwhile, total operating expenses accounted for 6% of net revenue, a decrease of 120 bps from the previous year, and a 70-bp improvement when excluding share-based compensation. Improved cost ratios were recorded across all expense items.
- The positive structural thesis for 111 remains intact.** In view of the prevailing macroeconomic environment, we have toned down our forecasts for 3Q24, for which we now expect another quarter of flattish revenue over the previous year rather than the 4% Y/Y growth we had previously projected. We expect 111 will continue to be operationally profitable (Figure 1). The company is deploying another seven fulfillment centers to increase its product range to provide a one-stop shopping experience for its customers. Notwithstanding the short-term headwinds, there remain positive structural trends in the healthcare industry that present valuable opportunities for 111's business model, led by China's commitment to healthcare reforms, for which a key goal is the acceleration of transitioning drug sales and prescriptions to retail pharmacies, which offer a more accessible and transparent alternative to the traditional hospital system.
- Please join us for a fireside chat on September 5, 2024, at 11:00 am ET with CEO Junling Liu for a post-results update. Click [here](#) to register.**

#### KEY STATISTICS

Ticker:Exchange	YI:NASDAQ
Current Price	\$0.68
52-Week Range	\$0.60-\$2.81
Average Volume (30-Day)	112,593
Shares Outstanding (MM)	85.7
Market Cap (\$MM)	\$58.3
Fiscal Year-End	December

#### PRICE PERFORMANCE



**Figure 1: Financial Projections to 2027**

RMB Million	1Q24A	2Q24A	3Q24E	4Q24E	2024E	2025E	2026E	2027E
<b>Revenue</b>								
B2B	3,452	3,354	3,575	4,100	14,481	15,929	17,521	20,150
<i>YoY growth</i>	-4%	-1%	0%	2%	-1%	10%	10%	15%
B2C	76	71	67	75	289	304	322	341
<i>YoY growth</i>	-32%	-20%	-24%	-15%	-23%	5%	6%	6%
<b>Total</b>	<b>3,528</b>	<b>3,424</b>	<b>3,642</b>	<b>4,175</b>	<b>14,770</b>	<b>16,232</b>	<b>17,843</b>	<b>20,491</b>
<i>YoY growth</i>	<b>-4.6%</b>	<b>-2%</b>	<b>-1%</b>	<b>2%</b>	<b>-1%</b>	<b>10%</b>	<b>10%</b>	<b>15%</b>
<b>Gross Profit</b>								
B2B	191	191	197	230	808	948	1,139	1,511
<i>Margin</i>	5.5%	5.7%	5.5%	5.6%	5.6%	6.0%	6.5%	7.5%
B2C	18	17	16	19	80	70	74	78
<i>Margin</i>	23%	24%	24%	25%	28%	23%	23%	23%
<b>Total</b>	<b>209</b>	<b>208</b>	<b>213</b>	<b>249</b>	<b>888</b>	<b>1,018</b>	<b>1,213</b>	<b>1,590</b>
<b>Gross Margin</b>	<b>5.9%</b>	<b>6.1%</b>	<b>5.8%</b>	<b>6.0%</b>	<b>6.0%</b>	<b>6.3%</b>	<b>6.8%</b>	<b>7.8%</b>
<b>OPEX</b>								
Fulfilment	(89)	(88)	(97)	(110)	(383)	(402)	(434)	(469)
<i>% of Revenue</i>	2.5%	2.6%	2.7%	2.6%	2.6%	2.5%	2.4%	2.3%
Selling & Marketing	(80)	(80)	(81)	(88)	(329)	(316)	(348)	(382)
<i>% of Revenue</i>	2.3%	2.3%	2.2%	2.1%	2.2%	1.9%	2.0%	1.9%
General & Administrative	(19)	(17)	(16)	(19)	(73)	(80)	(84)	(88)
<i>% of Revenue</i>	0.5%	0.5%	0.4%	0.4%	0.5%	0.5%	0.5%	0.4%
Technology	(18)	(18)	(18)	(20)	(75)	(83)	(87)	(92)
<i>% of Revenue</i>	-0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.4%
Other	1.5	(0.1)	-	-	-	-	-	-
<b>Total</b>	<b>(205)</b>	<b>(204)</b>	<b>(212)</b>	<b>(237)</b>	<b>(860)</b>	<b>(881)</b>	<b>(953)</b>	<b>(1,031)</b>
<b>% of Revenue</b>	<b>5.8%</b>	<b>6.0%</b>	<b>5.8%</b>	<b>5.7%</b>	<b>5.8%</b>	<b>5.4%</b>	<b>5.3%</b>	<b>5.0%</b>
<b>GAAP Operating Income</b>	<b>3.7</b>	<b>3.3</b>	<b>0.9</b>	<b>12.5</b>	<b>20</b>	<b>137</b>	<b>260</b>	<b>559</b>
<b>Margin</b>	<b>0.1%</b>	<b>0.1%</b>	<b>0.0%</b>	<b>0.3%</b>	<b>0.1%</b>	<b>0.8%</b>	<b>1.5%</b>	<b>2.7%</b>
Share-Based Compensation	5.2	5.2	4.3	4.0	18.7	22.2	25.0	25.0
<b>Operating Expenses ex-SBC</b>	<b>(200)</b>	<b>(199)</b>	<b>(208)</b>	<b>(233)</b>	<b>(841)</b>	<b>(859)</b>	<b>(928)</b>	<b>(1,006)</b>
<b>% of Revenue</b>	<b>5.7%</b>	<b>-5.8%</b>	<b>-5.7%</b>	<b>-5.6%</b>	<b>-5.7%</b>	<b>-5.3%</b>	<b>-5.2%</b>	<b>-4.9%</b>
<b>Non-GAAP Operating Income</b>	<b>8.9</b>	<b>8.5</b>	<b>5.2</b>	<b>16.5</b>	<b>39</b>	<b>159</b>	<b>285</b>	<b>584</b>
<b>Margin</b>	<b>0.3%</b>	<b>0.2%</b>	<b>0.1%</b>	<b>0.4%</b>	<b>0.3%</b>	<b>1.0%</b>	<b>1.6%</b>	<b>2.8%</b>

Source: Water Tower Research

#### ABOUT THE ANALYST



**Robert Sassoon**

Senior Research Analyst

Robert Sassoon has been an equity analyst for more than three decades, focusing primarily on global special situations. During his career, Robert has worked for several sell-side institutions in London, Hong Kong, and New York, including Credit Suisse, NatWest Capital Markets, and Societe Generale. In 2017, Robert founded AlphaSituations, an independent idea-generating event driven/special situations investment research service, which produced comprehensive research on early stage/emerging publicly traded and privately owned companies with the goal of telling an underappreciated or unknown story to relevant investors.

Robert has developed a uniquely broad and deep knowledge base in multiple industries from a global perspective and has achieved top five rankings in various analyst surveys, including the Extel and Greenwich surveys. Robert holds an MSc in Economics from the London School of Economics and Political Science, and has held FINRA licenses Series 7, 63, 86, 87, and 24.

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