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PRESENTATION

Operator

Good morning, ladies and gentlemen, and thank you for standing by for Baozun's First Quarter 2023 Earnings Conference Call. (Operator Instructions)

I would now like to turn the meeting over to your host for today's call, Ms. Wendy Sun, Senior Director of Corporate Development and Investor Relations of Baozun.

Wendy Sun *Baozun Inc. - IR Director*

Thank you, operator. Hello, everyone, and thank you for joining us today. Our first quarter 2023 earnings release was distributed earlier and is available on our IR website at ir.baozun.com as well as on Globe Newswire services. We have also posted a PowerPoint presentation that accompanies our comments to the same IR website where they are available for download.

On the call today from Baozun, we have Mr. Vincent Qiu, Chairman and Chief Executive Officer; Mr. Arthur Yu, Chief Financial Officer and President of Baozun e-Commerce; and Ms. Sandrine Zerbib, President of Baozun Brand Management. Mr. Qiu will review the business strategy and company highlights, followed by Mr. Yu, who will discuss the business development of Baozun e-Commerce and about our financial outlook; then by Ms. Sandrine to share more about Baozun Brand Management. They will all be available to answer your questions during the Q&A session that follows.

Before we begin, I would like to remind you that this conference call contains forward-looking statements within the meaning of the Securities Exchange Act of 1934 and the U.S. Private Securities Litigation Reform Act of 1995. These forward-looking statements are based upon management's current expectations and current market and operating conditions and relate to events that involve known or unknown risks, uncertainties, and other factors, all of which are difficult to predict and many of which are beyond the company's control, which may cause the company's actual results to differ materially from those in the forward-looking statement.

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It is now my pleasure to introduce our Chairman and Chief Executive Officer, Mr. Vincent Qiu.

Wenbin Qiu *Baozun Inc. - Co-Founder, Chairman of the Board & CEO*

Thank you, Wendy. Hello, everyone, and thank you all for your time. I'm excited about the transformation road map we have lined up for the next 3 years, all illustrated on Slide #2. The expansion of Baozun Group into 3 divisions; BEC, BBM and BZI, is aimed at creating a virtuous ecosystem in which each division brings value to the others. For instance, BEC brings cutting-edge value-added services such as DM, logistics and IT to BBM, while BBM enables BEC to have a deeper understanding of client needs, leading to continuously improved technologies and operations. Meanwhile, BZI facilitates BEC and BBM in the geographic expansion of brands. The 3 divisions

complement and support one another in a healthy ecosystem to provide the most comprehensive one-stop services for our clients.

I want to emphasize that technology is a cornerstone of our business transformation and success. In the past 15 years, we have leveraged our technology to innovate and build-up a portfolio of integrated omnichannel fulfillment platforms. Our technology infrastructure enables our clients to unify their online and offline channels and conduct their business anytime, anywhere and/or any marketplaces. In recent quarters, regional service centers of BEC, supported by our customer service management system, S-ANY, have efficiently expanded to more cities and effortlessly added a wide range of services. RSCs have improved both service quality and cost efficiency for BEC. This is just one example of how technology empowers our business as we now embark on the second growth curve.

Our advances in technology and digitalization form a strong foundation to empower the next generation of retail. Consumers now prefer brands that are modified to Chinese consumers' preferences and community styles. By closely monitoring trends and offering tailor-made updates and iterations, we aim to enable new retail experiences and supply chains that are more responsive to local needs. This empowerment applies to all 3 divisions.

BBM is off to a great start. Since February 1st, we began consolidating Gap China and the initial progress is quite encouraging. In the first quarter, Gap China generated RMB 189 million in revenue and significantly narrowed its operating losses. Sandrine will provide further details about BBM and Gap later. We fully believe that BBM is a game changer.

BZI is also beginning to take shape. In February, we acquired a minority interest along with the Board seat in Branded Lifestyle Asia Limited, a leading premium fashion retailer with a strong brand portfolio that includes Blue Dog and Roots. Baozun and the Fung Group, its parent company, have jointly set up a strategic technology committee to develop an enterprise-wide technology strategy and lead the digital transformation. We have already taken an exciting first step with the launch of an online store, littleground.com.sg for Singapore. We are also in the process of working with Branded Lifestyle for similar solutions elsewhere in Asia. This is an important first step for bringing our battle-tested technology to the global market. Our technology is an important piece of the foundation we are putting in place to build up our presence in the growing e-commerce market in SEA.

Overall, each of our 3 business lines is making solid progress and we are confident in our business transition. My priorities for the next 3 years will be maintaining an appropriate organizational and incentive structure and focusing on our technology, people, and culture. I will also take [the lead in steering our technology journey for BBM] for BZI. Ultimately, our priority at Baozun is to achieve customer-centric, high quality and stable business growth.

Let me now pass the call over to Arthur for an update on BEC and review of our financials.

Arthur Yu Baozun Inc. - CFO

Thank you, Vincent, and hello everyone. Let me do a quick review of the financials of the first quarter of 2023, after which I will discuss our BEC business highlights in more details.

Benefiting from our continuous cost optimization in recent quarters, we were able to achieve better year-over-year profit and cash flows in the first quarter of 2023, as highlighted on Slide #3. During the quarter, our net revenues declined by 5% to RMB 1.9 billion, of which product sales declined by 2% and service revenue decreased by 6% compared to the same period last year.

Please turn to Slide #4. For BEC, revenue for the quarter was still soft due to weakness in consumer confidence in China. The 3 years of pandemic hardship has caused consumers to be more cautious in increasing their spending. And it will take both time and consistent efforts of macro policies to be implemented in order to result a full spending recovery.

We continue to prioritize value-added service in digital marketing and IT services, while reducing low quality product sales. Total product sales of BEC declined by 30% during the quarter, reflecting weaker consumption in the appliance category and our commitment to reduce sales of low profit categories. Luxury continues to deliver double-digit growth and sportswear sustained a positive year-over-year growth trends. Value-added service continued to show strong resilience with total revenue from logistics, IT and digital marketing achieved year-over-year growth on a like-to-like basis.

For BBM, total product sales revenue in the first quarter was RMB 189 million, which is in line with our plan before acquisition. Given that the Gap acquisition was completed in February, the consolidated product sales of BBM for the first quarter only consisted of February and March.

Now turning to Slide #5. In this quarter, our cost of product decreased by 15% to RMB 505 million, mainly due to lower product sales of BEC, partially offset by incremental cost of RMB 82.8 million from Gap. For Gap specifically, its gross margin reached a new record of approximately 55%, representing over 1,000 basis points improvement from a year ago on a comparable basis. Overall, at the Group level, our gross margin improved by 320 basis points to 73.2% due to the acquisition of Gap Greater China.

Our non-GAAP loss from operations was RMB 10 million during the quarter. At this time, we are not fully prepared to report separate cost for BBM and we plan to do so soon in the following quarters once we completed the integration. However, to provide a clearer view of the business trends for each segment, we would like to provide some direction for the profitability of BEC and BBM based on our internal management accounts.

During the quarter, BEC's non-GAAP operating income delivered triple-digit growth, reflecting our high-quality growth strategy and effective cost optimization. The cost optimization efforts included ramping up regional service centers, re-engineering process, improving working capital efficiency and reforming compensation policies. In BBM, we have reduced its operating loss by more than half year-over-year on a comparable basis. Overall, our non-GAAP operating margin was negative 0.5%. Our non-GAAP net loss was RMB 7 million this quarter, a slight reduction compared with the same period of last year due to an expected losses from Gap Greater China.

Turning to Slide #6 about our cash and cash flow status. As of March 31, 2023, our cash, cash equivalents, restricted cash and short-term investments totaled RMB 2.9 billion. We continued to upgrade our back office processes to improve working capital and inventory management. As a result, our total operating cash outflow in this quarter were RMB 207 million, which is an improvement of RMB 338 million from the same period last year.

Now let me provide some insight into our BEC business performance. This quarter, we continued to make progress in our omni-channel initiatives, with 44% of our brands engaging with us on at least 2 channels. Our GMV from WeChat and JD both achieved high-double-digit growth. Moreover, we established a strategic partnership with Little Red Book or Xiaohongshu, which will allow us to acquire incremental traffic and attract new consumers in a more cost-effective way for our brand partners.

Value-added services are crucial in enhancing the user experience and creating value for brand partners. We have implemented new service offerings such as digitalization upgrade, data security enhancement, omni-channel data intelligence and AI-powered customer services. These services enable us to meet the changing needs and expectations of customers, providing a more personalized and seamless experience across all channels. We are also focusing on developing system enhancements and process re-engineering by utilizing the latest AI tools to drive efficiency improvements.

Our new business development for 2023 is off to a good start. Year-to-date, we have established a healthy pipeline with notable wins in the luxury, auto and FMCG sectors this quarter. This strong pipeline also provides us with greater flexibility in optimizing our resources allocation. In addition, we continue to focus on improving our key account management through NPS initiative partnered with Nielsen, which will improve our service quality in a sustainable way going forward.

We also saw an opportunity to grow beyond our traditional areas of strength to capture the growth area of content-driven live streaming e-commerce. In this quarter, we established a new business unit called 'Creative Content to Commerce' to prioritize content-driven e-commerce initiatives. This new business unit is a combination of creative marketing, video content and live streaming units within Baozun. Currently, we are also building our grand live streaming studio with a total area of 4,500 square meters in our Shanghai headquarters. And we target to officially launch this studio this June during our 6/18 promotion period.

Now let me turn the call over to Sandrine to talk about BBM.

Sandrine Zerbib Baozun Inc. - President of Baozun Brand Management

Thank you, Vincent and Arthur, and thank you all for joining us today. It is my great pleasure to speak with you.

Please follow us to Slide #7. As a holistic and well-rounded partner for global brands, BBM aims to unlock their business potential in China by utilizing our technologies and insights to deliver the best seamless omni-channel experience. We integrate the digital and physical at scale and we bridge demand and supply with fast supply chain adjustments through our digital intelligence. Our focus is on growing a portfolio of mid-end and premium consumer lifestyle brands under BBM. We've been very selective in narrowing down to a possible few lifestyle brands, limiting ourselves to only 1 or 2 additional brands in 2023.

Obviously, our focus this year is on Gap. Please turn to Slide #8. In 2023, we are prioritizing the smooth post-acquisition transition of Gap China, refining product and merchandising strategies, building supply chain infrastructures, enhancing back-end systems and developing the right talent pool.

First of all, we are committed to accelerating our transformation from a discount-driven approach to one that focuses on building consumer desire for our brand and products. While this initiative may have some negative impact on price-sensitive customers in the short-term, we believe it is necessary for the brand's long-term positioning.

Another priority is our China-for-China product and communication. It is critical for us to interpret the DNA of the Gap brand in a way relevant for China, rather than simply copying and replicating Gap globally. We've put together a design team with a new art director. We base our designs on more data insights and execute with a much shorter supply chain cycle. The results will start showing in fall and will be fully released in late winter. This will give us the first meaningful and measurable product impact. In terms of communication, we've started with upgrading our store design and we're working hand-in-hand with Gap to create a new store along with a new approach to visual merchandising.

In addition, we are upgrading the supply chain to react quickly to new data and consumer demands. We have identified close to 30 new local manufacturers to fully meet our projected production needs. And except for global IP styles, we aim for 100% local production. We will continue to seek more factories with fast replenishment capability, while ensuring the same quality and lower prices compared to Gap global sourcing.

Now in addition, we've taken a series of quick actions on store efficiency, including changing existing store visual with a focus on mix and match storytelling, strictly controlling discounts and enhancing sales advisor training. Thanks to these actions, our blended gross margin reached approximately 55%, an improvement of over 1,000 basis points from a year ago. This is in our view a major achievement as gross margin increase is key to Gap China's success. Overall, we generated total revenue of RMB 189 million, a decrease of 30% year-on-year on a comparable basis. And there are actually 2 factors that impacted this comparison. First factor is the timing of Chinese New Year, which is normally a peak season for retail. Chinese New Year was in February last year, but in January this year. And the second factor is the different starting points of offline. 86 stores were closed before we took over, which is equivalent to a decline of 40% year-over-year. Therefore, despite our strong comp store growth, our overall sales decreased.

For the remainder of 2023, our overall operating strategy remains unchanged, focused on products and margins, uplift brand image, product and consumer integrated marketing, fast response supply chain and enhanced omni-channel digitalization and customer experience. With these objectives in mind, we have set our store opening plans according to our product cycle. We plan to open about 10 new stores in first-tier cities, covering flagship, adult stores and kids and baby store formats with an upgraded store concept and customer experience by the end of 2023.

Lastly, organizational competency and IT transformation are the 2 foundations that will enable our strategy. We've taken quick actions to build up the talent pool for Gap and future BBM operations. Over the past 60 days, we were able to quickly identify and hire critical positions, included but not limited to, Head of Design and Dedicated Kids and Baby Designer Lead, Head of Supply Chain, new CHRO and new CFO. All of our new hires are local industry experts with vast experience in both well-known leading MNCs and local apparel companies. We have also significantly reduced costs in logistics, marketing and store maintenance. We believe this will accelerate our

business transformation and organizational efficiency.

Now regarding IT transformation, we are making solid progress in transforming the former Gap China siloed, inefficient and outdated system into a fully integrated, flexible and modern architecture. With the help of Baozun technology, we have already completed the overall design for the integrated system transformation of Gap China and we aim to have the new systems in place by Q4 2023. This system transformation will improve our business operation capability and efficiencies across multiple areas, including merchandising, planning, operations, design, production, fast and responsive supply chain, omni-channel inventory management, retail experience enhancements and business intelligence analytics. All of these improvements will be powered by optimized business processes and rules from market-leading practices.

Overall, although there remains quite some way to go in our transformation, we have established a good first step for BBM, and we are firmly determined to accelerate the necessary changes in our first year to set-up a solid foundation for our future growth.

With all this being said, I shall now hand over the call back to Arthur.

Arthur Yu Baozun Inc. - CFO

Thank you, Sandrine. In summary, we are excited about our transformation road map, which focuses on becoming a technology-driven omni-channel e-commerce player. With BEC, we will continue execution of our customer first, high quality growth strategy. And the early progress in BBM reflects our team's high quality execution and agility. We have also taken first steps in BZI, which validates a natural opportunity for us to replicate our China e-commerce success overseas.

That concludes our prepared remarks. Thank you, operator. We are now ready to begin the Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We're now going to proceed with our first question. And the question is coming from the line of Alicia Yap from Citi.

Alicia Yap Citigroup Inc., Research Division - MD & Head of Pan-Asia Internet Research

I have 2 quick ones. One is that can management share with us how are you seeing the consumption demand in April and May? And any qualitative expectation on the upcoming June 18 events? And then what have been the brands' merchants' attitude so far towards the June 18 promotion? And then second is that if management can elaborate your near-term priorities? And would you also plan to explore more acquisitions and investment in other brands if opportunity occurs?

Arthur Yu Baozun Inc. - CFO

I will take the first question about the 6/18 and maybe Sandrine can add a little bit more on the investments of the BBM. First of all, in terms of April and May, we definitely see an improving trend year-over-year. As I mentioned, the luxury, the sports and apparel start to show the signs of recovery. And for us, our Gap brand has also shown a steady recovery and a positive trend in terms of April and May.

In terms of the 6/18, I would say, for the upcoming 6/18, it is probably one of the most prepared 6/18 from the platform and from the brand, because this is the first 6/18 promotion after 3 years COVID pandemic, and both the platform and brands put a lot of efforts into it.

From a platform point of view, Tmall, JD, Douyin, they all launched new initiatives to attract customers and to incentivize the brands to use their platform. And from a brand point of view, they will start to -- they will start very early to prepare the merchandising and also the new initiative, how can they attract the new customer. And Baozun is in the process to help them during the last 2, 3 weeks to launch those plans. And we have seen some good early signs in terms of our plan starts to make some impact in terms of the upcoming 6/18. So the attitude is positive, but there are still uncertainties in terms of how strong the customer confidence is because the overall macro environment has still not recovered to our expectation. So we would say, it's cautiously positive at this moment.

In terms of the near-term management priority, I think as Vincent has laid out, so in this year, we have put our Baozun Group into BEC, BBM and BZI, the 3 business units. And myself and Sandrine and Vincent himself will each take the role in terms of driving the strategy for each of the business unit with our own priority and our own plan. And now we are focused on execution to make sure we actually deliver our plan to achieve the overall Group plan for this year.

On the investment, maybe Sandrine, can you add a few sentences?

Sandrine Zerbib Baozun Inc. - President of Baozun Brand Management

Just a few words to say that, obviously, in the mid to long-term, we want to grow portfolio of mid-end and premium consumer lifestyle brands under BBM. And therefore, we have actually looked at many brands in order to be able to be extremely selective and to really narrow down to very few potential candidates for this portfolio, particularly for this year, we want to really limit ourselves to 1, max-max 2 new brands for the portfolio, because this year obviously our focus is on Gap and our top priority is a smooth post-acquisition transition of Gap China.

Arthur Yu Baozun Inc. - CFO

And on that one, we also have an internal process to evaluate each of the opportunities with a lot of care and a lot of the details. So we will only do the acquisition when the good opportunity appears.

Operator

We are now going to proceed with our next question. And the question is coming from the line of [Colin Chan] from CITIC. We're now going to proceed with our next question. The next question is coming from the line of Thomas Chong from Jefferies.

Thomas Chong Jefferies LLC, Research Division - Equity Analyst

My first question is a follow-up on the 6/18 campaign. So as we see more, -- the online shopping market is undergoing a more competition. So how should we think about the impact on us? And my second question is that, as you've seen the consumer sentiment is gradually recovering. So how should we think about the second half performance for the discretionary like apparel, cosmetics, durables, electronics and as well as the luxury category? Should we see a pick-up in the second half?

Arthur Yu Baozun Inc. - CFO

I think the competition of the platform is actually a good news for Baozun, because through the competition, the platform becomes a commodity in some way. So at this moment, a lot of features which is available to Tmall will become available to Douyin and something Douyin is good at, Tmall is trying to replicate. So in that way, the platform is becoming a marketplace and the brand is doing the business through those marketplace with the need to differentiate themselves by the brand themselves. So that they need Baozun who understands the different characters of the platform. And also, we can help the brand to define a strategy specific for them to be successful in an omni-channel environment. So that's the strategy Baozun has laid out a number of years ago to pursue the omni-channel strategy. So our back-end system can support us to manage the different channels and the knowledge we accumulated in terms of how to operate in each channel will play a big growth in helping brands going forward. So that's #1.

And #2, I think ways the platform becomes a commodity in some way, the value-added service offered from Baozun becomes very unique to support the brand. So for example, IT, digital marketing, logistics and warehouse, they all improve the brand capability to serve their customer better through the upgrading of the capability. So in recent quarters, we have seen the value-added service start to see a big pipeline and we are confident that will help us to drive the revenue growth into the future.

Your second question in terms of the customer sentiment, as I mentioned, it's definitely gradually recovered for the apparels and for the cosmetic to some extent. But durables like the electronics and the other categories, I think we probably need to wait and see. And I would say, 6/18 is a good place to test how much the consumer confidence will come back and what the spending kind of pattern will be looked like for the whole year.

Operator

We are now going to proceed with our next question. And the question is coming from the line of Colin Shan from CITIC.

Colin Shan CITIC Securities - Analyst

I'm Colin Shan, CITIC Securities. I have 2 questions. The first is that I noticed that in Q1 the non-Tmall GMV share rise to 49% with a significant increase year-over-year and quarter-over-quarter. So I'm curious about the driver of the change? And what's your expectation of the GMV distribution in different channels in the next few quarters? And a follow-up question to that, facing the structural changes of e-commerce channels, do you observe any changes about the standard and criteria when a brand choose to cooperate with their partners?

Arthur Yu Baozun Inc. - CFO

So Colin, the first one, I think is very simple that it's the omni-channel strategy we have been pursuing over the last 2 to 3 years and start to show the fruits in terms of, we now have a Tmall percentage become only half and non-Tmall become half. We think this is a healthy foundation for us to drive the omni-channel strategy going forward. This is also what the brand is trying to pursue at this moment in time.

But what I would say, the Tmall and non-Tmall is not something to say the non-Tmall growth is higher, the better. It's actually Tmall has its very unique advantage in terms of providing the certainties and providing very good quality customers from the Tmall kind of the consumer group. Our recommendation to the brand is to choose the best platform for the best product which are suitable for their own business model and for their own strategy. So that's the way we will help the brands to design a strategy to be successful in this new environment post-COVID in terms of e-commerce.

Your second question in terms of the overall environment and also on what they're looking at the e-commerce service provider, it's actually a lot of the brands we're talking to recently, they put a lot of emphasis on the value-added service we can provide to the brand. With the AI and also the competition, a lot of the very basic activities can be replicated very easily, either by machine or by Baozun competitors. But what we have, the unique strength from Baozun is our capability to provide the insight and our kind of help to help the brands to design a strategy to be successful. So those activities are what Baozun will add a great value.

And in terms of the IT solution, the digital marketing and also the logistics and the warehouse, they are also very thought after at this moment, as I mentioned earlier. So overall, I think for a service provider like Baozun, the current competition and the intensified kind of the competition from all the channels is actually a good news for us.

Operator

We are now going to proceed with our next question. And the question is coming from the line of Sophia Tan from Credit Suisse.

Sophia Tan Crédit Suisse AG, Research Division - Research Analyst

I have one question on behalf of Ashley in terms of our BBM business line. It actually has been several months post our acquisition, so can you please share with us the major surprise or the challenges that we have countered so far? And whether this brings some challenges to -- changes to our previous guidance for the operating results, financial outlook or any execution timeline?

Sandrine Zerbib Baozun Inc. - President of Baozun Brand Management

I think the biggest surprise is actually a positive surprise, which is the fact that we were able to improve our gross margin much faster than we had expected. And this is due to the fact that, in fact, the consumers have accepted a higher price points and less discounts much faster, particularly offline, much faster than we had anticipated. And this is actually a very important positive surprise for us, because obviously, it drives all the rest of the P&L. So a very positive surprise that we believe that all in all will enable us to over-achieve our year in terms of gross margin, even if, obviously, with upcoming 6/18 and 11/11, we will not necessarily keep exactly the same level of gross margin as we've experienced in this first quarter. So that's for the surprise.

And then for the challenges, I think I see 2 challenges. The first one is obviously the speed of recovery of overall market recovery and consumer sentiment recovery, because this will determine how fast we can indeed push ourselves and the recovery and the

transformation of Gap obviously. And the other challenge is to make sure that in terms of execution, we continue to work hard to really put all the bits and pieces together, because today, we had this first good surprise without having all the bits and pieces yet together. In fact, the new products are not yet here. The new marketing is not yet here. The new store concept that we are working on is not yet here. So you can see that we have a very ambitious plan to work on for the remainder of the year. And we need to continue to work hard to get all these bits and pieces together to really push the results to the maximum.

Operator

(Operator Instructions) We are now going to proceed with our next question. And the question is coming from the line of Sophie Huang from CMBI.

Qun Huang CMB International Securities Limited, Research Division - Research Analyst

Just a follow-up question regarding to BBM. We're just wondering, what customer feedback have you had with your discount reduction strategy? Do you mind share more color on this recent sales performance of online and offline stores? How do you think about the consolidation impact on different channels, I mean, online and offline sales?

Sandrine Zerbib Baozun Inc. - President of Baozun Brand Management

In fact, as I just said, we had a relatively good surprise in terms of acceptance of the reduction of discounts, which enabled us to improve our gross margin faster than we had anticipated, but this was actually faster offline than online. This acceptance of reduced discounts, we expect to take a little bit more time online than offline, which is also due to the fact that we need to wait for obviously certain activities in marketing, but also in product.

As we said, we now work from products that were ordered before we took over the company. And therefore, all what we plan to do in terms of differentiating products for different channels online has not been yet implemented because we don't have the products to differentiate yet. So we think that this will be very important to accelerate this acceptance online, which has already good signs and positive signs from the offline side of things.

In terms of omni-channel management, we're still underway of putting together the new systems. And the new systems will be -- that will enable really integrated online and offline inventory management will only be available in the end in the last quarter of this year.

Operator

We have no further questions at this time. I'll now hand the call back to Wendy Sun for closing remarks.

Wendy Sun Baozun Inc. - IR Director

Thank you, operator. In closing, on behalf of the Baozun management team, we would like to thank you for your participation in today's call. If you require any further information, feel free to reach out to us. Thank you for joining us today. This concludes the call.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect your lines. Thank you.

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