SCH Advisors - iQiyi Research Paper: iQiyi, the Chinese Netflix

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iQiyi - China's Netflix

MANHATTAN, NEW YORK, UNITED STATES, August 6, 2018 /EINPresswire.com/ -- Welcome to the first edition of SCH Advisors monthly research paper. Each edition will highlight a specific company within a progressive dynamic sector.

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Chinese streaming video platform iQiyi has had a strong run, since its late-March IPO. iQiyi stock actually fell on its first day of trading; it then nearly tripled before pulling back to a current price around $30.

All told, IQ still has gained around 80% from its IPO price of $18, and it has more than doubled from its first-day close.

One reason for the optimism is that IQ offers an attractive story. iQiyi, as many put it, is the Netflix of China. The comparisons aren't perfect. iQiyi does have some user-generated content, for instance. But there are enough similarities to whet investors' appetite.

And with NFLX stock one of the best performers in the market — it's risen 855% over the past five years, even with post-earnings fall last week — investors are hoping that IQ provides a second chance for those big gains.

It is then worth considering on a fundamental basis whether iQiyi stock really might be the next Netflix. And there is an argument that it's possible. But investors also have to mind the risks and remember that few stocks can repeat the performance of NFLX over the past few years.

What Netflix Looked Like as It Grew

One of the issues with comparing Netflix's growth to that of iQiyi is that the business models are different — and Netflix's has changed. Over the past four quarters, iQiyi has generated about $2.8 billion in revenue, with an operating loss over $600 million.

In 2011, Netflix cleared $3 billion for the first time and made $376 million in profit. Of course, it still heavily relied on its more profitable DVD business at that point. (That year saw the company's initial attempt to cleave off the DVD business from streaming, which was reversed amid customer complaints.)

Still, the growth potential is illuminated by looking at Netflix's user growth. That company closed

2011 with 20.1 million paid subscriptions in the U.S. iQiyi's paid base is roughly triple that at the moment. In the six years plus since, Netflix's U.S. subscribers have grown to 56 million, nearly tripling. The same pace for iQiyi would get the company to ~170 million subscribers by 2023.

Looking at Netflix's total users — including international offerings — its figure at the end of 2014 was 57 million. That's roughly equivalent to iQiyi's current base. And at the end of that year, Netflix had a market cap of about $21 billion, not far from IQ's enterprise value of $23 billion. How investors view that fact likely determines their view toward IQ stock.

Is iQiyi the Next Netflix?

The clearly bullish implication from that comparison is that IQ could have huge upside ahead. After all, the market in retrospect badly underpriced Netflix's users in 2014.

NFLX stock has risen about eight-fold since the end of that year. And at the moment, the market appears to be undervaluing iQiyi's users. Each Netflix user (worldwide) is worth about $1,280 based on the current market cap; the figure for IQ is just $390.

If an investor assumes that iQiyi can grow its streaming at a similar rate as did Netflix, and that the per-user value will grow to even half that of Netflix, there's big upside here. That model would value iQiyi at over $100 billion and IQ stock at roughly $130 per ADS, quadruple current levels. Discounted back at 10%, IQ right now should be worth about $66, double its share price.

That's a fundamental representation of the bull case here. If iQiyi truly is China's Netflix, then its stock should act accordingly.

The Risks to IQ Stock

But there are risks to consider, both short-term and long-term. First, iQiyi users likely are worth less than those of Netflix. Its subscription price is about US$3 per month.

Unlike Netflix, iQiyi does sell advertising as well. In 2017, advertising revenue actually was larger than subscription revenue. Still, total monetization looks to be a little more than half that of Netflix, which suggests iQiyi's users should be less valuable.

There also are some short-term trading concerns. IQ stock already has pulled back from its highs. As James Hadley, Senior Advisor at SCH pointed out this month, the lockup period for IQ ends on Sep. 25. Sellers will be able to exit the stock in full at this point.

Snap, Twitter, and Facebook, among many others, all saw heightened volatility ahead of those expirations. IQ likely won't be any different. Longer term, majority owner Baidu will be looking to sell shares, providing a potential overhang to the stock.

And there are concerns about Chinese stocks as a whole. Like Alibaba, iQiyi has a convoluted corporate structure. Alibaba mostly has shrugged those concerns off, but still-cheap multiples suggest the market is assigning some sort of discount to the business given the ownership risk.

Indeed, IQ feels like the quintessential Chinese stock. Bulls see a massive market opportunity in the country's population of nearly 1.4 billion. Bears see a company operating in a single-party, still nominally Communist country where shareholder protections are weak at best.

For China bulls, which SCH Advisors are, IQ is an attractive play. At this point, SCH leans toward the bullish side — there's a path here to huge upside — and everyone has seen the profits gained by the likes of Alibaba and Tencent when a US model is applied in Chinese market place.

To receive more information on iQiyi or subsequent editions of their research papers via mailing list, contact SCH Advisors at info@sch-advisors.com or visit www.sch-advisors.com to see how they can make a difference to your financial security.

Jonathan Harper
SCH Advisors
+1 6468095762
email us here
