

ZKH Earnings Call Transcript

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Quarter: 3

Operator: Ladies and gentlemen, good day, and welcome to ZKH Group Limited Third Quarter 2025 Earnings Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Jin Li, Head of Investor Relations. Please go ahead.

Jin Li: Good morning, and welcome to our third quarter earnings conference call. With me are Mr. Eric Chen, our Founder, Chairman and CEO; and Max Lai, our CFO. Today's discussion may include forward-looking statements. Related factors are described in our today's press release. And we will also discuss certain non-GAAP financial measures for comparison purpose only. Please refer to the earnings release for definitions of these measures and a reconciliation of GAAP to non-GAAP results. With that, I will turn the call over to Eric. Eric, please go ahead.

Long Chen: [Interpreted] Hello, everyone. Thank you for joining the Third Quarter 2025 Earnings Conference Call for ZKH Group. In the third quarter, thanks to our team's concerted efforts, we are pleased to see signs of stabilization and recovery in our business following nearly four quarters of proactive business optimization and adjustment. In the third quarter, the number of transacting customers exceeded 70,000, reaching a new quarterly high and strengthening the foundation for future growth. Both GMV and the number of transacting customers among industry key accounts and regional SME customers continue to grow year-over-year. The company's gross margin continued its upward trend. As a result, our third quarter GMV, revenue and gross profit largely recovered to their prior year levels. From an order flow perspective, average weekday order value rose from approximately RMB 37 million in July to approximately RMB 52 million November to date, representing an improvement of over 40%. Compared to the previous year, this level has also grown to about -- grown by about 20%. We expect this positive momentum in average weekday order value to continue through the remainder of the year. Taken together, these advancements underscore that we are firmly back on a growth trajectory. In the third quarter, our total operating expenses were down by 14% year-over-year to approximately RMB 420 million. Overall, our profitability meaningfully improved during the quarter. Operating loss, net loss and adjusted net loss all narrowed significantly. Our adjusted net loss was down by approximately 78% year-over-year to just RMB 14 million. Our adjusted net loss margin also improved to 0.6%. Moreover, we once again achieved monthly breakeven in September, and we are on track to deliver quarterly profitability in the fourth quarter. In terms of cash flow, we generated net cash of approximately RMB 100 million from operating activities for the third quarter, primarily driven by the substantial narrowing of losses and continued optimization of working capital management, including accounts receivable and accounts payable. Our business development is underpinned by the ongoing advancement, refinement, and application of our product capabilities in AI technologies. In the third quarter, we continued to make strides in both areas, propelling business growth, while enhancing operational efficiency. As a professional one-stop MRO procurement service platform, the breadth and depth of our product offerings are fundamental to our growth. We strategically operate 32 product lines, each with a tailored approach. Some product lines are highly specialized with an emphasis on curation, while others prioritize expanding product variety and supplier base. In the third quarter, we added over 2.3 million sellable SKUs across categories such as chemical reagents, machining and transmission, bringing our total sellable SKUs to more than 19 million. We also onboarded over 1,200 new suppliers, primarily OEMs, further enriching our product offerings and solidifying our core advantage as a

one-stop procurement platform. Our private label products are a key strategic initiative to provide our customers with high value-for-money offerings, enhancing our overall product competitiveness. In the third quarter, we launched over 600 new private label SKUs, spanning categories such as security-related products, personal protective equipment, tools, and material handling and storage products. The GMV of our private label products maintained double-digit growth, outpacing the company's overall growth rate. Looking ahead, we plan to steadily increase our private label products contribution to total GMV from around 8% today to approximately 30%. We will continue to focus on professional and industrial-grade MRO categories, that are -- that is spare parts, chemicals and manufacturing parts. These areas serve as key differentiators and value drivers that set us apart from our competitors. For product lines where we have distinct advantages, such as our chemical product line of industrial lubricants and adhesives, we have developed a robust and reliable supply chain comprised of 13 specialized chemical warehouses, three of which are dedicated to hazardous materials and an in-house fleet for distribution and delivery. We will continue to enhance our integrated capabilities from product selection to last-mile delivery and on-site service, further reinforcing our competitive moat. In the third quarter, our chemical product line achieved double-digit year-over-year GMV growth. In the AI realm, we are continuing to advance our AI infrastructure across both the data and application layers, focusing on intelligent business processes and data governance to systematically improve our sales and operational efficiency. We have already deeply integrated AI across various business scenarios including material cataloging and management, product recommendation, sales conversion, data standardization and workflow automation. AI has emerged as an increasingly important driver of cost reduction, efficiency improvement, business growth, R&D; productivity and data asset enhancement. At the opening of the 8th China International Import Expo in November, we officially launched Expert Linglong, our proprietary AI large model and intelligent agent suite, specifically designed and developed for the MRO industry vertical. Expert Linglong marked a significant milestone for ZKH in empowering the entire MRO supply chain with AI. Our AI Smart Workbench, one of Expert Linglong's core applications enables automation across 45 business process scenarios, such as creating orders or issuing invoices with a single prompt. It has significantly reduced cross-system, manual operations and enhanced process efficiency, platform-wide synergy and workforce productivity. Measured by order volume processed per employee, in the third quarter, our customer service productivity increased by 42% year-over-year, while procurement productivity increased by 52%. Moreover, AI has become the key engine for capturing customer needs and improving supply-demand matching efficiency. Our ProductRecom Agent continues to improve product recommendation accuracy generating over RMB 100 million in new incremental sales revenue since its launch in the fourth quarter of 2024 through the end of the third quarter this year. Our AI tools also excel in complex business scenarios. For example, processing a 300-line customer inquiry traditionally takes 3 hours. By combining AI with expert experience, this task can now be completed in 30 seconds with 98% accuracy. Since the start of the year, we have utilized AI to optimize our product classification models and system rules boosting the platform's automated product classification rate from 11% to 31%. This not only reduces manual intervention, but also increases product onboarding efficiency and improves the accuracy of matching customer needs. Moving forward, we will continue to develop our self-service AI-driven procurement agent to speed up responses and further elevate customer experience. Our Expert Linglong large model is also empowering upgrades across our R&D; system. Our R&D; teams have widely adopted AI coding tools with over 15% of our code now being generated by AI, significantly improving development efficiency. Looking ahead, the Expert Linglong large model will remain at the core of our AI development, driving deeper technological empowerment across our product, supply chain and last-mile delivery capabilities. We believe that AI is more than the tool. It is a key force reshaping the MRO supply chain ecosystem. In summary, the third quarter was highly productive. We drove steady progress in all of our business segments, in line with our strategic road map, building stronger growth momentum across the board. Looking ahead, we remain committed to advancing our development goals of product excellence, AI-driven growth and profitability improvement, delivering long-term value to our customers and shareholders. Now I will turn the call over to our CFO, Max Lai, to present our financial results. Thank you, everyone.

Chun Chiu Lai: Thank you, Eric, and thanks, everyone, for making time to join our earnings call today.

I'm pleased to walk you through our robust financial performance, driven by revenue recovery, enhanced profitability metrics and possible operating cash flow. Let me begin with the top line. Both GMV and revenues returned to approximately last year's levels, with GMV down 2.3% year-over-year to RMB 2.62 billion and total revenues up 2.1% to RMB 2.33 billion. This performance indicates that the headwinds from our business optimization initiatives has largely cycled through, providing greater visibility for renewed top line growth in the quarters ahead. Notably, the number of transacting customers exceed 70,000 reaching a new quarterly high and private label GMV grew 16.7% year-over-year, outpacing the overall business and reaching 8.2% of total GMV. Turning to business quality. Our gross margin remained healthy at 16.8% compared with 17% a year ago. On a GMV basis, our gross margin continued to improve, expanding by 41.5 basis points year-over-year to 14.9%. Specifically, gross margin for our product sales 1P model increased by 11.2 basis points to 16.2 percentage on ZKH Platform and 223.8 basis points to 7.7% on the GBP Platform. Additionally, we take our take rate of Marketplace model rose by 47.5 basis points to 13.1% year-over-year. These gains were mainly driven by our optimized procurement costs and a high contribution from our private label products, which typically deliver high margins. On operational efficiency, our disciplined focus on streamlining the costs and enhancing productivity continue to yield tangible results. Total operating expenses decreased 14.4% year-over-year to RMB 493.8 million, representing 18.1% of net revenues, a significant improvement from 21.6% in the prior year period. Breaking this down, fulfillment expenses were RMB 90.4 million down 9.8% year-over-year, reflecting lower employee benefits and warehouse rental costs. Sales and marketing expenses declined 13.2% to RMB 145.9 million primarily driven by lower employee benefits and travel expenses. R&D; expenses decreased 19% to RMB 40.3 million mainly attributable to lower employee benefits. And general and administration expenses were RMB 145.8 million, down 17% year-over-year, driven by lower employee benefits expenses and lower credit loss allowances. Efficiency gains underpinned margin improvements and a substantial reduction in losses. Operating loss narrowed 69.3% to RMB 32.3 million, with margin improving to negative 1.4% from negative 4.6%. Non-GAAP EBITDA improved to a loss of RMB 8.5 million from RMB 62.8 million, with margin improving to negative 0.4% from negative 2.8%. Adjusted net loss narrowed to RMB 14.1 million from RMB 66.2 million and margin improved to negative 0.6% from negative 2.9%. As of 30 September 2025, our cash position remained strong at RMB 1.9 billion. Net cash generated from operating activity was RMB 105.5 million compared with net cash used in operating activity of RMB 160.5 million in the same period of 2024. To conclude, our first quarter results demonstrate clear signs of stabilization and recovery, underpinned by a more balanced customer mix, a higher-margin product portfolio driven by private label growth and a structural efficiency gain from AI-enabled process optimization and strengthened supply chain capabilities. Looking ahead, we expect to capitalize on this momentum through disciplined investment in AI and data capabilities, continuous enhancement of our product and supply chain capabilities and focused execution while advancing our international expansion. We remain focused on top line growth, further margin expansion and loss reduction on our path towards sustainable profitability. Thank you. And I would like to now open the call for Q&A.; Operator, please go ahead.

Operator: [Operator Instructions] The first question comes from Xiaodan Zhang with CICC.

Xiaodan Zhang: [Foreign Language] So, according to publicly available information, JD Industrial is preparing for an IPO in Hong Kong. So could management share your views on the competitive landscape of MRO market in China?

Long Chen: [Interpreted] So I believe this JD MRO looking to get listed is a very good thing for ZKH and for the industry at large. Because it's very good in terms of spreading this idea of doing one stop purchasing on e-commerce platforms. And it's definitely an opportunity that our times have afforded us. China being the #1 manufacturer in the world is actually big enough for leading MRO companies to exist. And these MRO companies cannot only serve Chinese manufacturers, but also benefit global ones. And in the MRO space, we have seen different kinds of players, including those players traditionally engaged in supplying office supplies. As ZKH, we started out in serving and selling chemicals and industrial-grade MROs. So, we are really specialized -- we specialize in selling spare parts, chemicals and manufactured goods. And we have built an innovation center in Taichung. This goes to show how we are committed to be deeply involved and integrating our services. And so, in

terms of R&D; testing, product selection and comparison, and we would like to use the specialty of ours to help our customers better. We have also built our own warehouses and last-mile delivery capabilities. So, this supply chain capability can not only serve the whole of China, but also the rest of the world. And in terms of the competitive landscape, I would say, over the years, things have really stabilized and as leaders in the space, our advantages are becoming increasingly marked. And the fact that we are able to have acquired lots and lots of SMEs goes to show that there has been a great improvement to our supply chain capabilities. So basically, at the end of the day, we are committed and focused on beefing up and enhancing our supply chain capabilities in the MRO space. That was my answer to your question. Thank you.

Operator: Are you ready for your next question? The next question comes from Leo Chiang with Deutsche Bank.

Leo Chiang: [Foreign Language] Let me translate myself. Management just mentioned in the prepared remarks that the company will commit to advancing development goals of profitability improvement. What are the reasons the company has not been profitable so far? And how does the company consider and balance between profitability and the mid- to long-term development investment?

Long Chen: [Interpreted] So, we got lots of investment and funding along our journey. As a start-up -- start-ups have different phases, right? In early days, we were more focused on the health of our cash flow. So, more of the funds were used and spent on infrastructure build-out and the build-out of our core capabilities and the competencies. So, we were suffering losses primarily due to these investments that we made in order to beef up our core competencies. But I believe we are entering a new phase now. This is a phase marked by profitability, and we're going to use some of the profits and spend the profits to further build our core competencies. Now that we are profitable, one thing that is clear is we are having an increasingly strong operating leverage. Specifically, our expense ratio keeps dropping, while our fulfillment gross margin keeps rising. And our profitability is getting better. And this is very much in line with our original plan for our development. In terms of specific profit and losses, '21, we made a loss of RMB 910 million due to the loss and loss of investments that we made. 2022, we made a loss of RMB 630 million. '23 losses were RMB 290 million. '24, RMB 160 million. '25, we saw losses greatly narrowed and in Q4, we are very likely to turn a profit. So we are pretty certain that our GMV growth year-over-year could reach 15% to 20% per year going forward. In terms of how we're going to go about striking a balance between profitability and long-term growth, I think, it comes down a lot to control of expenses. So, we will continue to improve our efficiency and control our expenses as well as enhancing our capabilities of customer acquisition. We will also keep investing in our core competencies, while ensuring profitability. So these core competencies include R&D; when it comes to AI, R&D; when it comes to product capabilities and our overseas business expansion. So, we will not only make sure that our profitability is sustainable, but also we will enhance it while ensuring long-term growth.

Operator: The next question comes from Ruchen Tang with CITIC.

Ruchen Tang: [Foreign Language] So, let me quickly translate the question first. So, looking for -- looking out on your latest developments and the future plans for overseas expansion, could you talk us a little bit about how you think about developing your business in the States versus serving Chinese companies as they go abroad?

Long Chen: [Interpreted] Overall, when it comes to going abroad, there's two parts. One is serving Chinese companies as they go abroad as there's lots and lots of Chinese companies that are currently taking their business globally. Also, we're going to develop business in the U.S. Mainland and Europe, we're actually already actively doing that. But after a period of testing things out, we have made some adjustments as well. So firstly, we still highly value Chinese companies going abroad. And because investments there on our part are pretty limited, and the certainty of this business is very high. So in Q3, for example, we have already finished the MRO purchasing and delivery for some of our customers for quite a few Chinese customers rather in Thailand, Malaysia, Indonesia and Mexico, for their local factories. And we have finished things like product certification, customers' clearance, et cetera. As for our business in the U.S., we believe that's going to be a mid- to long-term play. So because it's going to take longer time in terms of product prep getting to market, so we decided to control -- we have decided to control our investment pace and cadence in the U.S. And overall, we believe our overseas business

will achieve breakeven in the whole of 2026. So that was actually all of my answer to this question.

Operator: And that concludes the question-and-answer session. I would like to turn the conference back over to management for any additional or closing comments.

Chun Chiu Lai: Thank you once again for joining us today. You can find the webcast of today's call on ir.zkh.com. If you have any further questions, please feel free to contact us. Our contact information can be found in today's press release. Thank you, and have a great day.

Operator: The conference has now concluded. Thank you for attending today's presentation. You may now disconnect. [Portions of this transcript that are marked [Interpreted] were spoken by an interpreter present on the live call.]