

YY (YY US)

Margin pressure with global expansion

SUMMARY. YY delivered mixed 2Q19 results, with topline beat but margin miss. Overseas expansion performed well, but market concern remains on competitive landscape and TAM. We trimmed its adj. net profit by 10%/22% in FY19/20E, and adjusted TP to **US\$74**. Valuation at 11x FY19E P/E is attractive.

- **Mixed 2Q19 result with margin miss.** 2Q19 revenue grew 67% YoY, 3% above consensus. However, Adj. net profit declined 36% YoY, 3% below consensus. Mgmt guided 3Q19 revenue at RMB 6.6-6.8bn (midpoint +62.5% YoY), 3% above consensus. Excluding Huya, YY Live & Bigo's 3Q19E revenue guidance accelerated to 58%-62% YoY (vs. 57% YoY in 2Q19). Mgmt announced a share repurchase plan up to US\$300mn over the next 12 months.
- **International expansion with rich app portfolio.** We are impressed by its overseas app performance, with 433.5mn global MAU (in which 78% from overseas). **Bigo Live** served as its largest revenue contributor, while **Likee** and **IMO** put user growth as priority. Mgmt are confident in its overseas monetization potential, mainly on: 1) paying ratio far below industry average, despite already-high ARPU; and 2) IMO and Likee to explore diversified monetization. Market concern might lie on its difficulty to cross check overseas data and global competition (e.g. Tiktok). We estimate Bigo to generate revenue of US\$667mn/US1.2bn in FY19/20E and net loss of US\$126mn/US\$110mn. Mgmt guided Bigo to achieve single-month breakeven in FY20E, and overall breakeven in FY21E.
- **Near-term margin pressure.** 2Q19 adj. net margin dropped 5.4ppts QoQ, mainly on: 1) heavier promotion for Likee; 2) increasing bandwidth for Bigo; and 3) higher revenue mix from Huya. We expect 3Q19E adj. net margin to continuously decline 1ppts QoQ to 7.1%, for higher S&M/Rev ratio and decreasing gross margin. We cut FY19/20E adj. net margin by 1.1ppts/2.6ppts, to reflect more aggressive overseas promotion, and correspondingly trimmed adj.net profit by 10%/22% in FY19/20E.
- **Maintain BUY.** We adjusted SOTP-based TP to **US\$74** from US\$91, under our new estimates. Our new TP is equivalent to 15x FY19E P/E, based on: 1) YY Live (7x FY19E P/E); 2) Huya (based on mkt cap) and 3) Bigo (2x FY19E P/S).

Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue (RMB mn)	11,595	15,764	24,088	30,975	36,075
YoY growth (%)	41.3	36.0	52.8	28.6	16.5
Net income (RMB mn)	2,751	3,196	2,283	2,645	4,084
Adj. EPS (RMB)	45.23	49.94	32.78	37.98	58.64
YoY growth (%)	63.6	10.4	(34.4)	15.9	54.4
P/E (x)	7.8	7.1	10.8	9.3	6.0
P/B (x)	3.4	1.7	1.9	1.8	1.6
Yield (%)	0.0	0.0	0.0	0.0	0.0
ROE (%)	30.6	9.9	6.4	6.8	11.6
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, CMBIS estimates

BUY (Maintain)

Target Price	US\$73.9
(Previous TP	US\$91.0)
Up/Downside	+39.0%
Current Price	US\$53.2

China Internet Sector

Sophie Huang
 (852) 3900 0889
 sophiehuang@cmbi.com.hk

Stock Data

Mkt Cap (US\$ mn)	4,197
Avg 3 mths t/o (US\$ mn)	79.0
52w High/Low (US\$)	89/51
Total Issued Shares (mn)	63.5
Source: Bloomberg	

Shareholding Structure

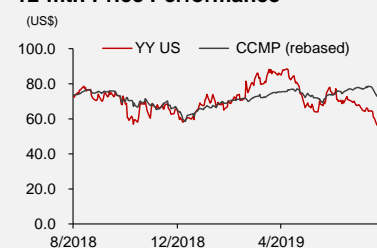
Lei Jun	16.0%
Capital Group	5.5%
Morgan Stanley	4.9%
Source: HKEx	

Share Performance

	Absolute	Relative
1-mth	-21.2%	-16.4%
6-mth	-20.9%	-21.4%
12-mth	-22.7%	-26.2%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: PwC

Related Reports

1. Guidance beat; Stepping up globalization – 31 May 2019
2. 4Q18 beat, with Bigo's acquisition settled – 6 Mar 2019

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Figure 1: 2Q19 financial review

RMB mn	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	QoQ	YoY	Consensus	Diff %
Revenue	3,249	3,773	4,100	4,641	4,781	6,295	31.7%	66.8%	6,115	3%
Operating profit	596	714	611	719	474	72	-84.8%	-89.9%	1,148	-94%
Net profit	444	-137	651	684	3,104	107	-96.5%	-178.5%	118	-9%
Adj. net profit	700	810	787	836	654	520	-20.5%	-35.9%	533	-3%
Adj. EPS (RMB)	10.96	12.69	12.07	12.86	9.32	5.14	-44.8%	-59.5%	7.33	-30%
Margin (%)										
Gross margin	38.0%	38.0%	38.0%	35.1%	33.9%	33.7%			33.9%	
Operating margin	18.4%	18.9%	14.9%	15.5%	9.9%	1.1%			1.9%	
Adj. net margin	21.5%	21.5%	19.2%	18.0%	13.7%	8.3%			8.7%	
Growth (%)										
Revenue (YoY)	30.8%	44.6%	32.6%	28.0%	47.1%	66.8%			62.1%	
Revenue (QoQ)	5.1%	16.1%	8.7%	13.2%	3.0%	31.7%			27.9%	
Operating profit	-4.0%	19.1%	-7.6%	-12.5%	-20.6%	-89.9%			60.9%	
Adj. net profit	16.9%	35.7%	23.1%	-11.9%	-6.6%	-35.9%			-34.2%	

Source: Company data, Bloomberg

Figure 2: 2Q19 revenue breakdown

RMB mn	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	QoQ	YoY
Total revenue	2,267	2,609	3,092	3,627	3,249	3,773	4,100	4,641	4,781	6,295	31.7%	66.8%
by segment												
Live broadcasting	2,057	2,373	2,872	3,369	2,032	3,560	3,895	4,391	4,485	5,923	32.1%	66.4%
Online games	140	154	122	128								
Membership	45	52	49	50	258	32	206	249	296	372		
Others	24	29	49	79								
by platform												
YY Live	1,893	2,145	1,868	2,148	2,407	2,735	2,824	3,136	2,753	3,054	10.9%	11.7%
Huya	197	339	399	461	844	1,038	1,277	1,505	1,631	2,010	23.2%	93.6%
Bigo									396	1,231	211.0%	

Source: Company data

Figure 3: CMBI earnings revision

Rmb mn, Mar-YE	New			Old			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	24,088	30,975	36,075	24,043	30,308	35,627	0.2%	2.2%	1.3%
Gross Profit	8,250	10,546	12,355	8,234	10,380	12,451	0.2%	1.6%	-0.8%
Operating Profit	1,396	1,569	3,498	1,754	2,660	4,418	-20.4%	-41.0%	-20.8%
Net profit	2,283	2,645	4,084	2,542	3,370	4,685	-10.2%	-21.5%	-12.8%
Adj. EPS (RMB)	32.78	37.98	58.64	36.51	48.39	67.28	-10.2%	-21.5%	-12.8%
Gross Margin	34.2%	34.0%	34.2%	34.2%	34.2%	34.9%	+0.0ppts	-0.2ppts	-0.7ppts
Operating Margin	5.8%	5.1%	9.7%	7.3%	8.8%	12.4%	-1.5ppts	-3.7ppts	-2.7ppts
Net Margin	9.5%	8.5%	11.3%	10.6%	11.1%	13.2%	-1.1ppts	-2.6ppts	-1.8ppts

Source: Company data, CMBIS estimates

Figure 4: CMBI estimates vs consensus

Rmb mn, Mar-YE	CMBI			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	24,088	30,975	36,075	24,459	30,829	35,777	-1.5%	0.5%	0.8%
Gross Profit	8,250	10,546	12,355	8,343	10,491	12,307	-1.1%	0.5%	0.4%
Operating Profit	1,396	1,569	3,498	1,534	2,170	3,392	-9.0%	-27.7%	3.1%
Net profit	2,283	2,645	4,084	2,489	3,473	4,824	-8.3%	-23.8%	-15.3%
Adj. EPS (RMB)	32.78	37.98	58.64	33.14	42.58	57.70	-1.1%	-10.8%	1.6%
Gross Margin	34.2%	34.0%	34.2%	34.1%	34.0%	34.4%	+0.1ppt	+0.0ppts	-0.2ppts
Operating Margin	5.8%	5.1%	9.7%	6.3%	7.0%	9.5%	-0.5ppts	-2.0ppts	+0.2ppts
Net Margin	9.5%	8.5%	11.3%	10.2%	11.3%	13.5%	-0.7ppts	-2.7ppts	-2.2ppts

Source: Company data, Bloomberg

Figure 5: SOTP valuation

SOTP		Metrics		Multiple		Valuation
(Rmb mn)	Rev	Net profit		Shareholding		Valuation
YY Live	FY19	12,022	2,585	7x PE	100%	18,093
Huya	Based on Mkt cap: US\$4.65bn				41%	12,793
BIGO	FY19	4,605	NA	2x PS	100%	9,210
Total		12,022	2,585			40,096
Holding discount						20%
Equity Value (Rmb mn)						32,077
Target Price (US\$)						73.9

Source: Company data, CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue	11,595	15,764	24,088	30,975	36,075
Live broadcasting	10,671	14,878	23,158	30,008	35,088
Others	924	886	930	968	987
COGS	(7,026)	(10,017)	(15,838)	(20,429)	(23,720)
Gross profit	4,568	5,746	8,250	10,546	12,355
S&M	(691)	(1,149)	(3,258)	(4,344)	(3,615)
Admin.Exp.	(545)	(883)	(1,373)	(1,704)	(1,804)
R&D	(782)	(1,192)	(2,391)	(3,075)	(3,581)
Others	149	118	169	145	144
Operating profit	2,699	2,640	1,396	1,569	3,498
Financial income	180	486	440	509	474
Other income	12	(590)	-	-	-
Pre-tax Income	2,891	2,535	1,836	2,078	3,972
Income Tax	(416)	(478)	(349)	(395)	(755)
MI	18	(465)	(149)	(253)	(547)
Net profit	2,494	1,642	1,338	1,431	2,670
Adj. net profit	2,751	3,196	2,283	2,645	4,084

Cash flow summary

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Net income	2,494	1,642	1,338	1,431	2,670
D&A	214	241	273	300	345
Change in WC	705	(108)	-	-	-
Income tax paid	(416)	(478)	(349)	(395)	(755)
Others	673	1,126	1,293	1,609	2,168
Operating CF	3,670	2,423	2,556	2,945	4,428
Capex	(328)	(447)	(682)	(878)	(1,022)
Associates	-	-	-	-	-
Others	(2,304)	(4,293)	-	-	-
Investing CF	(2,632)	(4,739)	(682)	(878)	(1,022)
Equity raised	-	5,846	-	-	-
Change of Debts	-	-	-	-	-
Others	-	-	-	-	-
Financing CF	-	5,846	-	-	-
Net change in cash	1,038	3,530	1,874	2,067	3,406
Cash (beg of yr)	1,580	2,618	6,147	8,021	10,088
FX	-	-	-	-	-
Cash (end of yr)	2,618	6,147	8,021	10,088	13,495

Balance sheet

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Non-current assets	4,329	8,278	6,269	6,269	6,269
Fixed asset	1,017	1,296	1,296	1,296	1,296
Long-term investments	1,153	4,592	4,592	4,592	4,592
Intangible assets	37	75	75	75	75
Others	2,122	2,316	306	306	306
Current assets	10,129	17,483	17,920	19,391	22,091
Cash	2,617	6,004	8,021	10,088	13,495
Deposit over 3 months	6,000	7,327	8,488	7,892	7,185
Account receivable	376	1,217	1,217	1,217	1,217
Others	1,136	2,934	194	194	194
Current liabilities	3,146	3,846	3,846	3,846	3,846
Borrowings	588	-	-	-	-
Account payable	76	115	115	115	115
Tax payable	146	236	236	236	236
Accrued expenses	1,466	2,414	2,414	2,414	2,414
Other	869	1,082	1,082	1,082	1,082
Non-current liabilities	75	119	168	208	237
Convertible debt	7	-	-	-	-
Other long-term liabilities	69	119	168	208	237
MI	6	6	6	6	6
Total net assets	11,238	21,796	20,175	21,606	24,276
Shareholders' equity	11,232	21,790	20,169	21,600	24,270

Key ratios

YE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Sales mix (%)					
Live broadcasting	92.0	94.4	96.1	96.9	97.3
Others	8.0	5.6	3.9	3.1	2.7
Total	100.0	100.0	100.0	100.0	100.0
Growth rate (%)					
Revenue	41.3	36.0	52.8	28.6	16.5
Gross profit	47.3	25.8	43.6	27.8	17.1
EBIT	50.4	(2.2)	(47.1)	12.4	122.9
Net profit	63.6	(34.1)	(18.5)	6.9	86.6
P&L ratios (%)					
Operating margin	23.3	16.7	5.8	5.1	9.7
Pre-tax margin	24.9	16.1	7.6	6.7	11.0
Adj. net margin	23.7	20.3	9.5	8.5	11.3
Effective tax rate	(14.4)	(18.8)	(19.0)	(19.0)	(19.0)
Returns (%)					
ROE	30.6	9.9	6.4	6.8	11.6
ROA	20.6	8.2	5.4	5.7	9.9
Per share					
EPS (RMB)	45.2	49.9	32.8	38.0	58.6
DPS (RMB)	0.0	0.0	0.0	0.0	0.0
BVPS (RMB)	184.8	358.4	331.8	355.3	399.2

Source: Company data, CMBIS estimates

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CMB International Securities Limited

Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

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