

NetEase (NTES US)

Strong 1Q25 results on solid games business and disciplined opex control

NetEase announced 1Q25 results: total revenue grew by 7% YoY to RMB28.8bn, largely in line with consensus estimate. Operating profit increased by 37% YoY to RMB10.4bn, 25% ahead of consensus estimate, mainly due to the disciplined opex control (-14% YoY). Games business regains momentum, with reaccelerating and better-than-expected revenue growth in 1Q25 (+12% YoY), and the strong growth of contract liabilities in 1Q25 (+19%/16% YoY/QoQ) should support the growth of games revenue in the coming quarters, in our view. In view of the solid business performance of games, we raise FY25-27E revenue forecast by 2-6%. We lift our SOTP-derived target price to US\$136.5 (previous: US\$125.5). Maintain BUY.

- **Games revenue growth reaccelerates.** Games & related VAS revenue was up by 12% YoY to RMB24.0bn in 1Q25 (4Q24: +2% YoY) and 4% ahead of consensus estimate, primarily driven by: 1) incremental contribution from new titles like *Where Winds Meet* and *Marvel Rivals*; 2) growth in revenue from legacy games like *Identity V*. *Where Winds Meet* surpassed 30mn registered players as of Mar 2025; *Marvel Rivals* topped Steam's global top seller chart after its Season 2 update in Apr 2025; *Once Human* mobile topped iOS download charts in over 160 regions after its launch in Apr 2025. Contract liabilities delivered strong growth of 19%/16% YoY/QoQ as of Mar 2025, which should support the revenue growth of games in the coming quarters, in our view. Looking ahead, several highly-anticipated titles are lined up for global launch, including *MARVEL Mystic Mayhem*, *Destiny: Rising* and *Ananta*.
- **Non-gaming businesses improve efficiency.** NetEase's Cloud music revenue declined by 8% YoY to RMB1.86bn in 1Q25, mainly due to the decline in social entertainment revenue; but music GPM rose by 4.8ppts QoQ to 36.7% in 1Q25 thanks to the effective cost control. Youdao's revenue was down by 7% YoY to RMB1.30bn in 1Q25, as the more disciplined customer acquisition approach led to decreased revenue from learning services. Innovative businesses and others revenue decreased by 18% YoY to RMB1.62bn in 1Q25, mainly attributable to decreased revenue from Yanxuan and advertising businesses.
- **Effective opex control boosts profitability.** Overall OPM rose by 7.8ppts YoY and 7.0ppts QoQ to 36.2% in 1Q25, mainly on disciplined opex control and GPM expansion. S&M/G&A expenses were down by 33%/20% YoY in 1Q25, equivalent to 9.4%/3.3% of total revenue (1Q24: 15.0%/4.5%). We expect NetEase will continue to maintain disciplined opex in addition to GPM expansion in FY25E, which should support OPM to improve by c.5.5ppts YoY in FY25E, based on our estimate. The enhanced profitability will offer room for investment in future opportunities such as new game genres and overseas market, in our view. NetEase currently trades at 14x FY25E non-GAAP PE, which is on par with 2-year historical average.

Earnings Summary

(YE 31 Dec)	FY23A	FY24A	FY25E	FY26E	FY27E
Revenue (RMB mn)	103,468	105,295	113,117	121,072	128,895
Adjusted net profit (RMB mn)	32,608.3	33,510.6	40,109.6	43,726.4	46,847.5
EPS (Adjusted) (RMB)	50.69	52.35	62.55	68.19	73.05
Consensus EPS (RMB)	50.69	52.35	55.24	58.01	63.64
P/S (x)	4.7	4.7	4.3	4.1	3.8
P/E (x)	16.9	16.7	13.6	12.3	11.5

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price US\$136.50
(Previous TP US\$125.50)
Up/Downside 27.4%
Current Price US\$107.11

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Stock Data

Mkt Cap (US\$ mn)	67,991.3
Avg 3 mths t/o (US\$ mn)	82.8
52w High/Low (US\$)	109.80/76.28
Total Issued Shares (mn)	634.8

Source: FactSet

Shareholding Structure

William Lei Ding	44.2%
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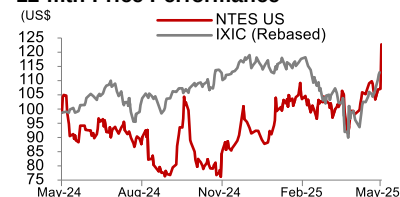
Source: Company data

Share Performance

	Absolute	Relative
1-mth	9.3%	-4.0%
3-mth	3.5%	8.2%
6-mth	25.3%	22.2%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: NetEase: earnings revision

RMB bn	Current			Previous			Change (%)		
	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
Revenue	113.1	121.1	128.9	110.7	117.1	121.9	2.2%	3.4%	5.7%
Gross profit	72.3	77.9	83.2	70.2	74.4	77.6	3.0%	4.6%	7.2%
Operating profit	38.0	42.1	46.2	33.7	36.8	39.5	12.9%	14.5%	16.9%
Adjusted net profit	40.1	43.7	46.8	36.0	38.6	40.5	11.3%	13.3%	15.6%
Adjusted EPS (RMB)	62.5	68.2	73.1	55.8	59.7	62.7	12.1%	14.2%	16.5%
Gross margin	63.9%	64.3%	64.6%	63.4%	63.5%	63.6%	0.5 ppt	0.8 ppt	0.9 ppt
Operating margin	33.6%	34.8%	35.9%	30.4%	31.4%	32.4%	3.2 ppt	3.4 ppt	3.4 ppt
Adjusted net margin	35.5%	36.1%	36.3%	32.6%	32.9%	33.2%	2.9 ppt	3.2 ppt	3.1 ppt

Source: CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

RMB bn	CMBIGM			Consensus			Diff (%)		
	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
Revenue	113.1	121.1	128.9	113.6	121.5	129.5	-0.4%	-0.4%	-0.5%
Gross profit	72.3	77.9	83.2	70.4	75.9	81.4	2.6%	2.6%	2.2%
Operating profit	38.0	42.1	46.2	32.5	36.6	40.1	17.2%	15.2%	15.2%
Adjusted net profit	40.1	43.7	46.8	35.4	38.4	40.3	13.2%	13.9%	16.1%
Adjusted EPS (RMB)	62.5	68.2	73.1	55.2	58.0	63.6	13.2%	17.5%	14.8%
Gross margin	63.9%	64.3%	64.6%	62.0%	62.5%	62.8%	1.9 ppt	1.8 ppt	1.7 ppt
Operating margin	33.6%	34.8%	35.9%	28.6%	30.1%	31.0%	5.0 ppt	4.7 ppt	4.9 ppt
Adjusted net margin	35.5%	36.1%	36.3%	31.2%	31.6%	31.2%	4.3 ppt	4.5 ppt	5.2 ppt

Source: Bloomberg, CMBIGM estimates

Figure 3: NetEase: key financial data forecasts

(RMB mn)	2Q23	3Q23	4Q23	1Q24	2Q24	3Q24	4Q24	1Q25	Cons.	Diff%
Online games revenue	18,799	21,780	20,921	21,460	20,056	20,864	21,242	24,048		
YoY%	3.6%	16.5%	9.6%	7.0%	6.7%	-4.2%	1.5%	12.1%		
As % of total revenue	78.3%	79.9%	77.1%	79.9%	78.7%	79.6%	79.4%	83.4%		
Youdao revenue	1,207	1,539	1,481	1,392	1,322	1,573	1,340	1,298		
YoY%	26.2%	9.7%	1.8%	19.7%	9.5%	2.2%	-9.5%	-6.7%		
As % of total revenue	5.0%	5.6%	5.5%	5.2%	5.2%	6.0%	5.0%	4.5%		
Cloud Music revenue	1,949	1,973	1,986	2,030	2,041	1,999	1,880	1,858		
YoY%	-11.1%	-16.3%	-16.4%	3.6%	4.7%	1.3%	-5.3%	-8.4%		
As % of total revenue	8.1%	7.2%	7.3%	7.6%	8.0%	7.6%	7.0%	6.4%		
Innovative businesses	2,057	1,979	2,753	1,970	2,067	1,774	2,285	1,624		
YoY%	9.9%	0.5%	12.9%	6.1%	0.5%	-10.3%	-17.0%	-17.6%		
As % of total revenue	8.6%	7.3%	10.1%	7.3%	8.1%	6.8%	8.5%	5.6%		
Total revenue	24,011	27,270	27,140	26,852	25,486	26,210	26,748	28,829	28,495	1.2%
YoY%	3.7%	11.6%	7.0%	7.2%	6.1%	-3.9%	-1.4%	7.4%		
Gross profit margin (%)	59.9%	62.2%	62.0%	63.4%	62.9%	62.9%	60.8%	64.1%		
S&M expenses ratio (%)	13.6%	13.1%	15.6%	15.0%	13.7%	14.5%	10.5%	9.4%		
R&D expenses ratio (%)	16.3%	15.9%	16.5%	15.5%	17.5%	16.9%	16.7%	15.2%		
Non-GAAP NPM (%)	37.6%	31.7%	27.2%	31.7%	30.7%	28.6%	36.2%	39.0%		
Non-GAAP net profit	9,017	8,645	7,379	8,511	7,819	7,499	9,682	11,237	8,979	25.1%
YoY%	66.7%	15.7%	53.4%	12.5%	-13.3%	-13.3%	31.2%	32.0%		

Source: Company data, CMBIGM estimates

We use sum-of-the-parts (SOTP) valuation methodology to value NetEase's four main business segments. Our SOTP-derived target price is US\$136.5, comprising:

- 1) US\$121.8 for the online game business (89.2% of total valuation), based on 16x 2025E EV/EBIT which is on par with the industry average.
- 2) US\$0.7 for Youdao (0.5% of total valuation), based on 1.0x 2025E EV/revenue, on par with the industry average;
- 3) US\$3.8 (2.8% of total valuation) for the NetEase Cloud Music business, based on 3.6x 2025E EV/revenue, on par with the industry average;
- 4) US\$1.6 (1.2% of total valuation) for the innovative businesses and others, based on 1.0x 2025E EV/revenue, on par with the industry average;
- 5) US\$8.7 for net cash.

Figure 4: NetEase: SOTP Valuation

(RMBmn)	Valuation basis	Multiple (x)	2025E sales	2025E EBIT	Valuation	Shareholding (%)	Valuation to NetEase	Valuation per ADS (US\$)
Online games	EV/EBIT	16.0	92,350	34,816	557,054	100.0%	557,054	121.8
Youdao	EV/revenue	1.0	5,288		5,288	59.2%	3,131	0.7
Cloud Music	EV/revenue	3.6	8,030		28,907	59.5%	17,211	3.8
Innovative businesses	EV/revenue	1.0	7,449		7,449	100.0%	7,449	1.6
Enterprise value							584,844	
Net cash							39,578	8.7
Equity value							624,423	
RMB/US\$							7.2	
Valuation (US\$mn)							86,665	
No. of ADSs (mn)							635	
Value per ADS (US\$)							136.5	

Source: Company data, CMBIGM estimates

Figure 5: Peer comparison: online games

Company	Ticker	Price (LC)	EBIT growth (YoY %)		EV/EBIT (x)	
			FY25E	FY26E	FY25E	FY26E
Tencent	700 HK	521.0	14	13	19	17
Electronic Arts	EA US	147.2	(11)	10	18	16
Nexon	3659 JP	2,618.5	(11)	10	14	13
Bandai Namco	7832 JP	4,593.0	124	(6)	14	15
Perfect World	002624 CH	13.5	NA	72	25	14
37 Interactive	002555 CH	15.1	12	14	9	8
Average EV/EBIT					16	14

Source: Bloomberg consensus estimates, CMBIGM

Note: data as of market close on 14 May

Figure 6: Peer comparison: education, online music, and e-commerce

Company	Ticker	Price (LC)	Revenue growth (YoY %)		EV/revenue (x)	
			FY25E	FY26E	FY25E	FY26E
Education						
New Oriental	EDU US	50.1	13	14	1.0	0.9
TAL Education	TAL US	10.2	57	32	1.3	1.0
Gaotu	GOTU US	3.8	33	23	0.7	0.6
Average					1.0	0.8
Community						
TME	TME US	17.0	11	10	5.8	5.2
Spotify	SPOT US	633.2	24	15	6.0	5.2
BiliBili	BILI US	18.2	14	9	1.4	1.3
Kuaishou	1024 HK	53.1	12	9	1.3	1.2
Average					3.6	3.3
E-commerce						
Alibaba	BABA US	134.1	8	9	1.7	1.6
JD	JD US	35.7	13	6	0.2	0.2
Pinduoduo	PDD US	118.9	19	18	1.9	1.6
Vipshop	VIPS US	14.9	1	2	0.3	0.3
Average					1.0	0.9

Source: Bloomberg consensus estimates, CMBIGM

Note: data as of market close on 14 May

Risks

Decline in revenue of legacy games; intensifying competition; tightening of regulations in the gaming sector.

Financial Summary

INCOME STATEMENT	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec (RMB mn)						
Revenue	96,496	103,468	105,295	113,117	121,072	128,895
Cost of goods sold	(43,730)	(40,405)	(39,488)	(40,824)	(43,212)	(45,692)
Gross profit	52,766	63,063	65,807	72,293	77,860	83,203
Operating expenses	(33,138)	(35,354)	(36,223)	(34,274)	(35,716)	(36,993)
Selling expense	(13,403)	(13,969)	(14,148)	(11,877)	(12,349)	(12,889)
Admin expense	(4,696)	(4,900)	(4,551)	(4,072)	(4,601)	(4,769)
R&D expense	(15,039)	(16,485)	(17,525)	(18,325)	(18,766)	(19,334)
Operating profit	19,629	27,709	29,584	38,019	42,144	46,210
Investment gain/loss	54	1,307	355	1,316	658	526
Other gains/(losses)	847	1,054	602	255	0	0
Interest income	2,150	4,120	4,921	4,157	4,034	3,478
Foreign exchange gain/loss	1,571	(133)	255	2	0	0
Pre-tax profit	24,250	34,057	35,718	43,749	46,836	50,214
Income tax	(5,032)	(4,700)	(5,461)	(7,000)	(7,494)	(8,034)
After tax profit	19,218	29,357	30,256	36,749	39,342	42,180
Minority interest	494	59	(559)	(736)	393	422
Net profit	19,713	29,417	29,698	36,013	39,735	42,602
Adjusted net profit	22,808	32,608	33,511	40,110	43,726	46,847
BALANCE SHEET	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec (RMB mn)						
Current assets	131,603	142,693	153,325	185,950	219,040	254,155
Cash & equivalents	24,889	21,429	51,383	75,115	98,523	123,132
Restricted cash	2,699	2,777	3,086	3,241	3,403	3,573
Account receivables	5,003	6,422	5,669	5,968	6,260	6,531
Inventories	994	695	572	591	625	661
Prepayment	5,448	6,077	6,417	6,756	7,086	7,393
ST bank deposits	84,948	100,856	75,441	82,985	91,284	100,412
Other current assets	7,623	4,436	10,756	11,294	11,859	12,452
Non-current assets	41,158	43,232	42,667	41,008	39,610	38,444
PP&E	6,342	8,075	8,520	8,990	9,485	10,008
Other non-current assets	34,815	35,157	34,147	32,019	30,125	28,436
Total assets	172,761	185,925	195,992	226,958	258,650	292,599
Current liabilities	56,829	53,842	49,668	54,692	58,580	62,738
Short-term borrowings	23,876	19,240	11,805	14,818	16,144	17,717
Account payables	1,507	881	721	745	788	834
Tax payable	2,813	2,572	2,759	2,964	3,173	3,378
Other current liabilities	17,252	18,219	19,982	21,277	22,716	24,147
Accrued expenses	11,381	12,930	14,401	14,888	15,759	16,663
Non-current liabilities	7,059	3,998	3,830	4,047	4,312	4,577
Other non-current liabilities	7,059	3,998	3,830	4,047	4,312	4,577
Total liabilities	63,888	57,841	53,497	58,739	62,892	67,315
Total shareholders equity	104,731	124,286	138,686	163,674	191,607	221,555
Minority interest	4,142	3,798	3,809	4,545	4,151	3,729
Total equity and liabilities	172,761	185,925	195,992	226,958	258,650	292,599

CASH FLOW	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	24,250	34,057	35,718	43,749	46,836	50,214
Depreciation & amortization	2,858	3,055	2,418	4,260	4,495	4,743
Tax paid	(5,032)	(4,700)	(5,461)	(7,000)	(7,494)	(8,034)
Change in working capital	3,497	376	3,652	1,354	1,905	1,971
Others	2,135	2,543	3,351	0	0	0
Net cash from operations	27,709	35,331	39,677	42,363	45,742	48,894
Investing						
Capital expenditure	(2,602)	(4,266)	(2,192)	(4,829)	(5,092)	(5,370)
Net cash from investing	(7,370)	(17,043)	17,916	(10,471)	(11,695)	(13,033)
Financing						
Dividend paid	(6,724)	(8,014)	(11,165)	(11,025)	(11,803)	(12,654)
Net borrowings	5,119	(8,305)	(7,476)	3,013	1,326	1,572
Proceeds from share issues	(274)	0	0	0	0	0
Others	(8,359)	(5,148)	(8,694)	0	0	0
Net cash from financing	(10,238)	(21,467)	(27,336)	(8,011)	(10,477)	(11,082)
Net change in cash						
Cash at the beginning of the year	17,376	27,588	24,207	54,475	78,355	101,925
Exchange difference	110	(202)	11	0	0	0
Others	0	0	0	0	0	0
Cash at the end of the year	27,588	24,207	54,475	78,355	101,925	126,705
GROWTH	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec						
Revenue	10.1%	7.2%	1.8%	7.4%	7.0%	6.5%
Gross profit	12.3%	19.5%	4.4%	9.9%	7.7%	6.9%
Operating profit	19.6%	41.2%	6.8%	28.5%	10.9%	9.6%
Net profit	16.9%	49.2%	1.0%	21.3%	10.3%	7.2%
Adj. net profit	15.4%	43.0%	2.8%	19.7%	9.0%	7.1%
PROFITABILITY	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec						
Gross profit margin	54.7%	60.9%	62.5%	63.9%	64.3%	64.6%
Operating margin	20.3%	26.8%	28.1%	33.6%	34.8%	35.9%
Adj. net profit margin	23.6%	31.5%	31.8%	35.5%	36.1%	36.3%
Return on equity (ROE)	19.7%	25.7%	22.6%	23.8%	22.4%	20.6%
GEARING/LIQUIDITY/ACTIVITIES	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec						
Net debt to equity (x)	(0.8)	(0.8)	(0.8)	(0.9)	(0.9)	(0.9)
Current ratio (x)	2.3	2.7	3.1	3.4	3.7	4.1
Receivable turnover days	18.9	22.7	19.7	19.3	18.9	18.5
Payable turnover days	12.6	8.0	6.7	6.7	6.7	6.7
VALUATION	2022A	2023A	2024A	2025E	2026E	2027E
YE 31 Dec						
P/E	25.6	16.9	16.7	13.6	12.3	11.5
P/E (diluted)	25.8	17.1	16.8	13.8	12.5	11.6
P/B	4.8	4.0	3.6	3.0	2.6	2.2

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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