

Perfect World (002624 CH)

Game leader with valuable IPs

We expect Perfect World ("PW") to keep its solid game momentum and see potential entertainment recovery, backed by valuable IPs, strong development team and high-quality productions. We forecast PW to deliver 11%/17% revenue/earnings CAGR during FY18-21E. Initiate with BUY with DCF-based TP RMB49.

- **A leading game & entertainment player with valuable IPs.** As a PC game pioneer, PW successfully transferred its strategic focus on mobile games, and developed notable IP-based titles, such as New Jade Dynasty Mobile (新诛仙) and Perfect World Mobile (完美世界手游). We forecast PW to deliver 11%/17% revenue/earnings CAGR during FY18-21E, thanks to its solid game and entertainment pipeline.
- **Game: rich game portfolio to maintain strong momentum.** Backed by valuable IPs and strong development team, PW had rich game pipeline in 2H19E, including New Swordsman Mobile (新笑傲江湖), Nightmare, New Forsaken World (新神魔大陆), etc. We expect its rich game pipeline will continuously boost ongoing growth in 2020E, supported by stepping-up new games introduction and launch. We forecast its game sector to grow 23%/14% YoY in FY19/20E, in which PC/ mobile games to deliver 5%/39% YoY growth in FY19E.
- **Entertainment: more high-quality productions to come.** Film industry in China faces multiple challenges in 2019, including flat industrial growth and tightening regulations on celebrity, content and pipeline. Given recent film headwinds, we expect PW's entertainment segment to bear pressure in FY19E, but keep positive on its recovery in FY20E, supported by its strong pipeline with high-quality TV dramas and movies.
- **Initiate with BUY.** We initiate BUY with DCF-based TP of RMB49, implying 26.7x P/E in FY20E. We think the majority of PW's solid FY19E financials have been partly priced in, and PW's positive price drivers and catalysts originate from: 1) further performance of new games; and 2) stepping-up contribution from entertainment after regulation headwinds.

Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue (RMB mn)	7,930	8,034	8,651	9,945	11,056
YoY growth (%)	28.8	1.3	7.7	15.0	11.2
Net income (RMB mn)	1,505	1,706	2,086	2,410	2,719
EPS (RMB)	1.14	1.30	1.59	1.83	2.07
YoY growth (%)	29.0	13.4	22.3	15.5	12.8
P/E (x)	35.8	31.6	25.8	22.4	19.8
P/S (x)	6.8	6.7	6.2	5.4	4.9
Yield (%)	0.4	0.4	0.5	0.6	0.7
ROE (%)	17.5	20.2	18.7	18.5	17.6
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, CMBIS estimates

BUY (Initiation)

Target Price	RMB48.9
Up/Downside	+19.3%
Current Price	RMB41.0

China Internet Sector

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Stock Data

Mkt Cap (RMB mn)	51,514
Avg 3 mths t/o (RMB mn)	421.2
52w High/Low (RMB)	41/22.6
Total Issued Shares (mn)	1,293

Source: Bloomberg

Shareholding Structure

Perfect World	35.1%
DQ JunYang Ent	11.9%
Chi Yufeng	10.2%

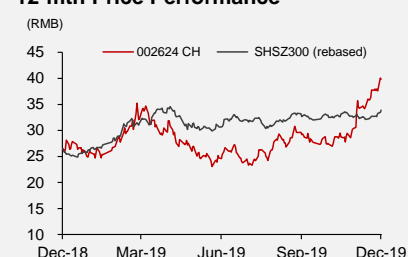
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	32.1%	28.4%
3-mth	35.3%	34.3%
6-mth	62.3%	48.8%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

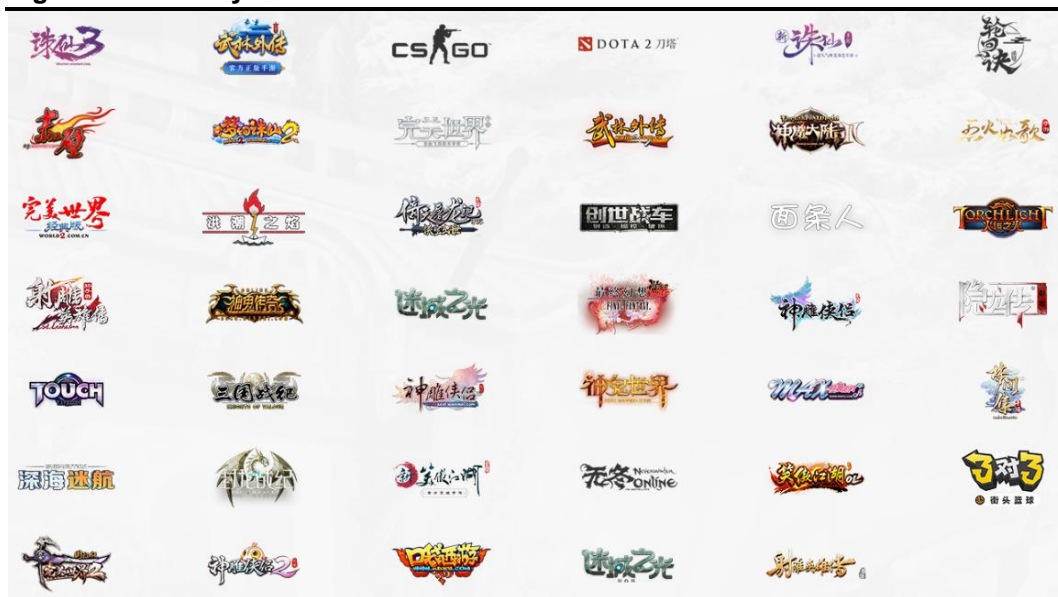
Investment Summary

Widely-anticipated IP reserve to deliver ongoing pipeline

Leveraging valuable PC IPs to boost mobile momentum

We see high visibility for PW to continue develop high quality and selective hot titles, backed by its valuable PC IP reserve. Since 2013, PW has begun to transfer its strategic focus on mobile games from PC games, and successfully developed notable PC IP-based titles, such as New Jade Dynasty Mobile <新诛仙>, Perfect World Mobile <完美世界手游>, and Return of the Condor Heroes 2 <神雕侠侣 2>. Moreover, most of its hot titles have long lifecycle.

Figure 1: PW's key titles



Source: Company, CMBIS

Figure 2: PW's PC game in operation

No	Title	Chinese Title	Type	Launch Date
1	Jade Dynasty 3	诛仙3	MMORPG	2007
2	PW International	完美国际	MMORPG	2006
3	Swordsman	笑傲江湖 OL	MMORPG	2013
4	My Own Swordsman	武林外传	MMORPG	2006
5	Forsaken World 2	神魔大陆 2	MMORPG	2013
6	Fantasy Jade Dynasty 2	梦幻诛仙 2	MMORPG	2009
7	Redcliffe	赤壁	MMORPG	2008
8	Creation chariots	创世战车	FTG	2019
9	The Mummy	神鬼传奇	MMORPG	2009
10	War of the Immortals	神鬼世界	MMORPG	2010
11	Perfect World	完美世界	MMORPG	2005
12	Condor Heroes	神雕侠侣	MMORPG	2012
13	Dance party MAX	热舞派对 MAX	Social Casual	2008
14	Pocketpet Journey West	口袋西游	MMORPG	2008
15	CS:GO	CS:GO	RTS	2012
16	DOTA 2	DOTA 2	MOBA	2013

Source: Company data, CMBIS

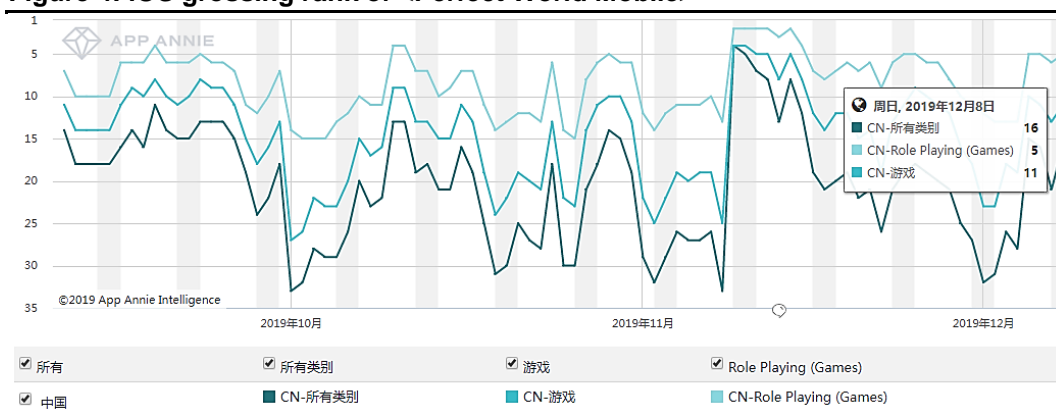
Figure 3: PW's mobile game in operation

No	Title	Chinese Title	Type	Grossing Rank	Launch Date
1	Jade Dynasty Mobile	诛仙手游	MMORPG	4	2016.09
2	Perfect World Mobile	完美世界手游	MMORPG	1	2019.03
3	My Own Swordsman Mobile	武林外传官方手游	MMORPG	3	2018.05
4	Condor Heroes 2	神雕侠侣2 手游	MMORPG	6	2019.07
5	Reincarnation	轮回诀	RPG	30	2018.04
6	Feng Long Zhan Ji	封龙战纪	MMORPG	63	2019.01
7	The Legend of The Condor Heroes Mobile	射雕英雄传手游	MMORPG	5	2017.06
8	The Legend of The Condor Heroes 3D	射雕英雄传 3D	MMORPG	9	2016.03
9	Dream book	梦间集	Simulation	61	2017.07
10	Torchlight	火炬之光	MMORPG	66	2016.12
11	Final Fantasy Awakening	最终幻想 • 觉醒	MMORPG	5	2016.12
12	Heavenly Sword Dragon Slaying Saber	倚天屠龙记	MMORPG	8	2016.05
13	Legend of Condor Hero Mobile	神雕侠侣手游	MMORPG	11	2015.01
14	The Flame's Daughter	烈火如歌	MMORPG	26	2018.04
15	My Origin	我的起源	Sandbox	48	2019.11
16	Yun Meng Si Shi Ge	云梦四时歌	RPG	6	2019.05

Source: Company data, App Annie, CMBIS

Flagship of <Perfect World Mobile> to contribute meaningful revenue in FY19E

<Perfect World Mobile> gained tractions and ranked Top 10 grossing game since it was launched in Mar 2019. We believe the eye-catching performance of < Perfect World Mobile > could be a notable case to show its self-development ability and monetization potential of reputable IPs. PW will further develop and release its new generation of PC/console version, and we are bullish on its continuous contribution from this IP. We expect <Perfect World Mobile> to contribute 26% of total mobile game revenue in FY19E.

Figure 4: iOS grossing rank of <Perfect World Mobile>

Source: App Annie, CMBIS

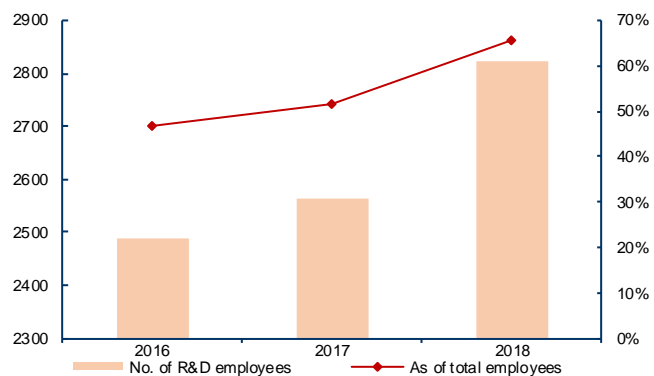
Not only MMORPG, but more...

We expect PW's game category expansion to enrich its game portfolio and deliver ongoing contribution. PW had rich experience in MMORPG games development. Apart from MMORPG, PW continuously explores diversified game types, such as SLG, CCG, female-oriented games. For instance, <Dream Book>, as PW's self-developed female-oriented game performed well quickly, and PW plans to leverage this IP to incubate more versions.

Stepping up game development to maximize IP monetization

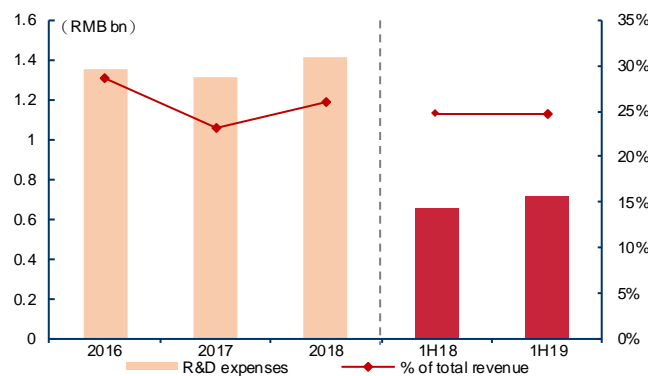
We believe PW's solid R&D team and stepping-up investment play key role in well-known game development. In 2018, PW had a R&D team with 2,823 developers, accounting for 66% of total employees. Moreover, its R&D/rev ratio were around 25% in the past three years, higher than industrial average (18%).

Figure 5: PW's R&D team



Source: Company data, CMBIS

Figure 6: R&D expenses



Source: Company data, CMBIS

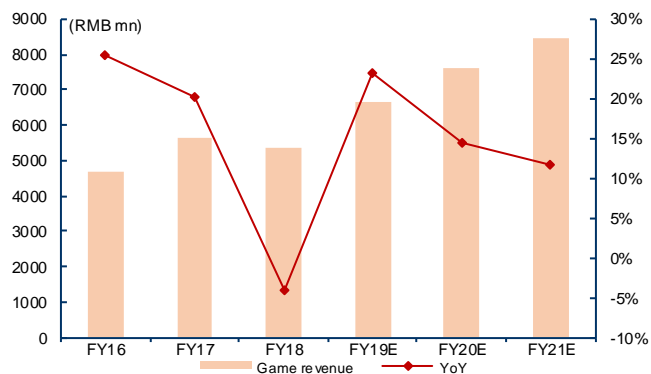
Rich game portfolio with great monetization potential

Backed by valuable IPs and strong development team, PW had rich game pipeline in 2H19E, including New Swordsman Mobile (新笑傲江湖), Nightmare, etc. PC games also see strong titles in pipeline, including New Fantasy Zhuxian (新诛仙世界), Perfect World (完美世界主机版). etc. We expect its rich game pipeline will continue boost ongoing growth in 2020E, supported by stepping-up new games introduction and launch (e.g. New Forsaken World (新神魔大陆), Meng Jian Ji Tian'e Zuo(梦间集天鹅座), New Fantasy Zhuxian(梦幻新诛仙)).

Mobile games to maintain strong momentum

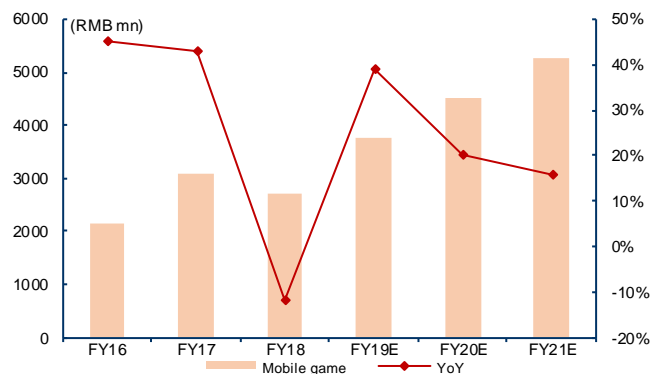
We are bullish on PW's mobile game revenue growth in FY19E. We forecast its mobile games to grow 39% YoY in FY19E, given its strong pipeline and newly-launched hot titles. In particular, we expect Perfect World Mobile (完美世界手游) and Zhuxian(诛仙) to contribute revenue significantly (accounting for 48% of total mobile game revenue in FY19E), due to 1) their high quality graphic effects, 2) innovative features based on its profound understanding of players, and 3) reputable IP and cooperation with Tencent.

Figure 7: PW's game revenue estimate



Source: Company data, CMBIS estimates

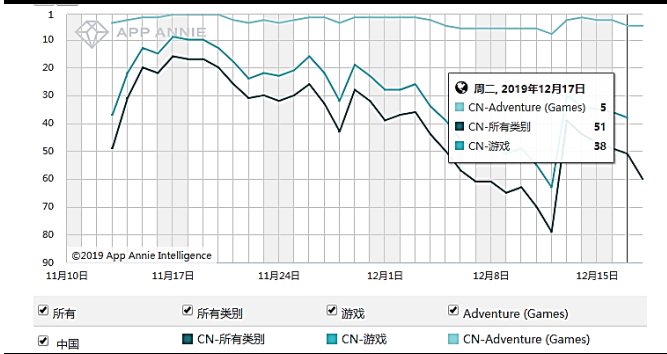
Figure 8: PW's mobile game revenue estimate



Source: Company data, CMBIS estimates

In 4Q19, ReEvo (我的起源), a sandbox game distributed by Tencent, performed well after launch, with iOS grossing rank at ~30 in game category. New Swordsman Mobile (新笑傲江湖) will also be launched in Dec 2019. We expect these new games to contribute 6%/17% of total revenue in FY19/20E.

Figure 9: ReEvo (我的起源) grossing rank



Source: App Annie, CMBIS

Figure 10: ReEvo (我的起源)

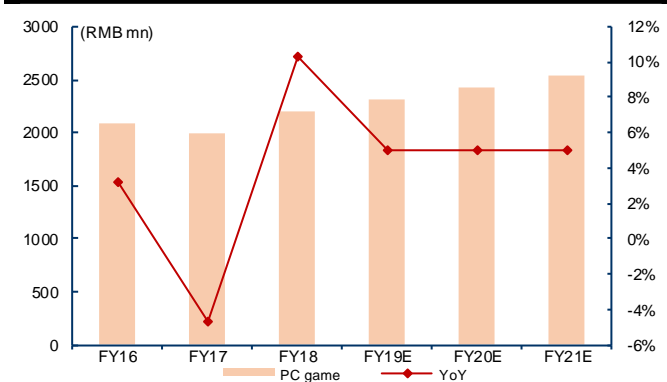


Source: Company, CMBIS

PC games outperformed despite industrial decline

Although PC games step into declining stage, PW's PC games still deliver solid growth in FY19E. We forecast its PC games to grow 5% YoY in FY19E, largely higher than industrial average. Among the new PC games to be launched, we are optimistic on the performance of New Fantasy Zhuxian (新诛仙世界), Perfect World (完美世界主机版).

Figure 11: PC game revenue forecast



Source: Company data, CMBIS estimate

Figure 12: Perfect World PC version



Source: Company, CMBIS

Expecting games to grow at 23% YoY in FY19E.

In total, we forecast its game sector to grow 23%/15% YoY in FY19/20E. We think FY19E performance has well acknowledged by the market, and further catalysts will derive from FY20E pipeline.

Entertainment: solid pipeline with high quality products

Film industry in China faces multiple challenges in 2019, including flat industrial growth and tightening regulations on celebrity, content, pipeline. Given recent film headwinds, we expect PW's entertainment to bear pressure in FY19E, but keep positive on its recovery in FY20E, supported by its strong pipeline with high quality TV dramas and movies.

Notable track record backed by solid team and high quality content

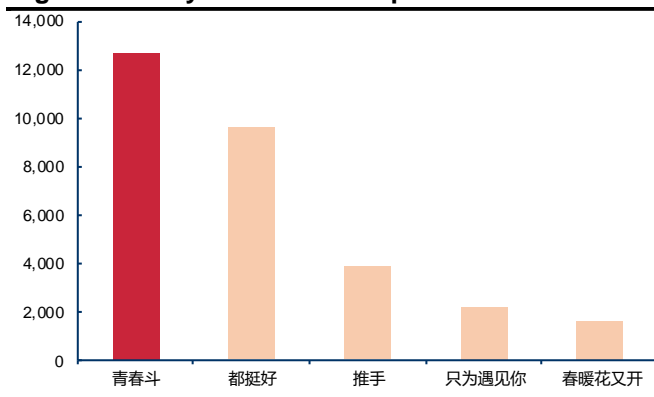
By investing in excellent production team and enterprises, PW has built over 10 selective production teams with diversified production style. It will introduce enriched productions catering to all kinds of audience demand. In the past years, PW produced multiple proven successful dramas, like *Ashes of Live* (香蜜沉沉烬如霜), *The Flame's Daughter* (烈火如歌) and recent *Youth Strive* (青春斗). We believe PW could leverage its M&A resources, solid team and content production, to continue deliver well-performed drama series.

Figure 13: The Flame's Daughter (烈火如歌)



Source: Company, CMBIS

Figure 14: Playback Rank in Apr 1 2019



Source: VLinkage, CMBIS

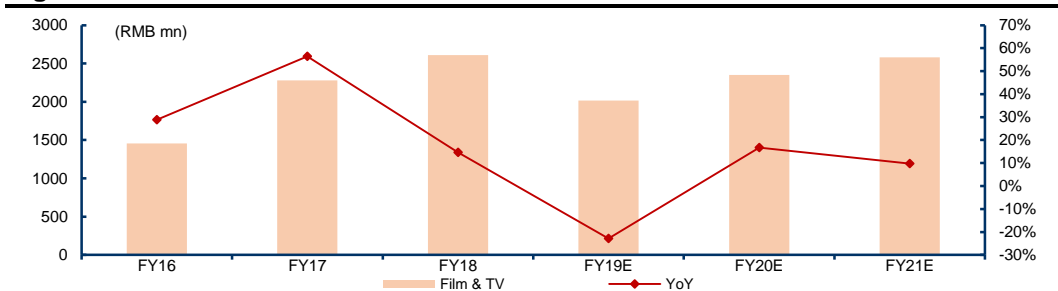
More high quality productions to come

With regulations on film and TV relaxed in 4Q19, we see high visibility for PW to see stepping-up production release and revenue recognized. Looking ahead, there are about 20 TV dramas in pipeline. We believe the upcoming productions will be further catalysts, including *New Horizon* (壮志高飞), *Bu Hun Nv Wang* (不婚女王), etc.

Expecting entertainment to recover in FY20E

We expect entertainment segment to decline 23% YoY in FY19E, in which solid TV drama to partly offset movies decline. However, we expect its entertainment revenue to rebound in FY20E (forecasting 17% YoY growth), with strong pipeline and upcoming productions release. Meanwhile, we see high visibility for its entertainment segment GPM to recover, for decreasing cost of TV production and celebrity salaries.

Figure 15: Entertainment revenue forecast



Source: Company data, CMBIS estimate

Figure 16: Solid entertainment pipeline

No.	Title	English Name
1	不婚女王	Bu Hun Nv Wang
2	壮志高飞	Zhuang Zhi Gao Fei
3	半生缘	Eighteen Springs
4	最美的乡村	The most beautiful countryside
5	暴风眼	Storm Eye
6	怪你过分美丽	You're too beautiful
7	冰糖炖雪梨	Bing Tang Dun Xue Li
8	月上重火	Heavy fire
9	全世界最好的你	Best of you
10	江山故人	Jiang Shan Gu Ren
11	新一年又一年	Year After Year
12	大海港	Seaport
19	我在天堂等你	Waiting for you in heaven
14	蓝盔特战队	Blue helmet
15	燃烧	Burning
16	高大霞的火红年代	Gao Daxia's Flaming Age
17	霍元甲	Huo Yuanjia

Source: Company, CMBIS

Figure 17: Zhuang Zhi Gao Fei (壮志高飞)

Source: Company, CMBIS

Figure 18: Bu Hun Nv Wang (不婚女王)

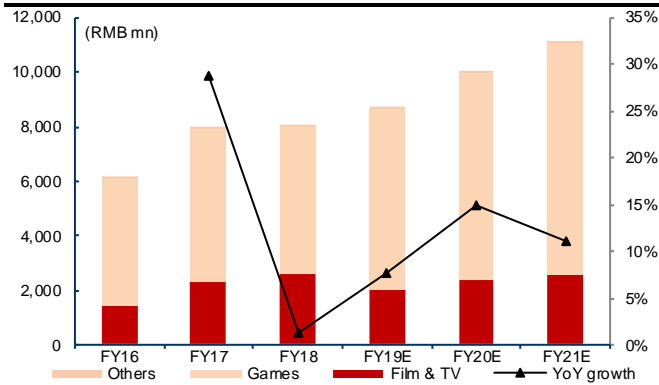
Source: Company, CMBIS

Financial Analysis

Revenue Breakdown

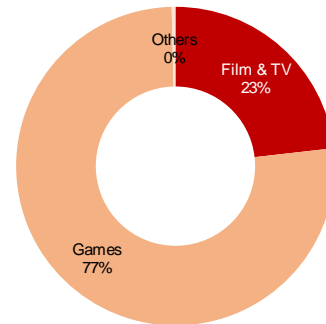
We forecast PW's revenue will grow at 8%/15%/11% YoY in FY19/20/21E, in which game business still devotes most of total revenue. We expect game revenue up to RMB6,636mn in FY19E with a CAGR of 16% in FY18-21E, accounting for 77% of total revenue. The robust growth is mainly driven by solid pipeline of both games and entertainment.

Figure 19: Revenue growth estimates



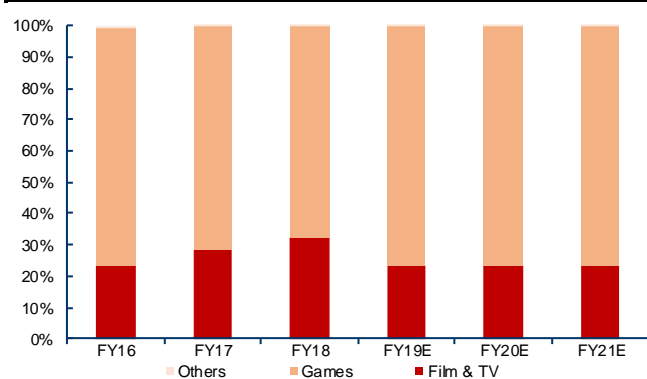
Source: Company data, CMBIS estimates

Figure 20: FY19E revenue breakdown



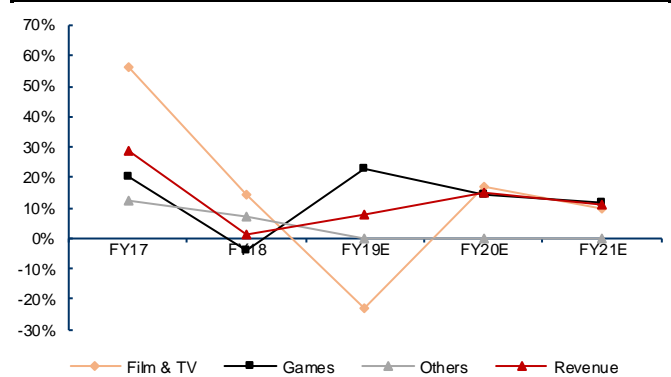
Source: CMBIS estimates

Figure 21: Revenue breakdown estimates



Source: Company data, CMBIS estimates

Figure 22: Revenue growth estimates



Source: Company data, CMBIS estimates

Income Statement

We expect better margin outlook, and forecast its adj. net profit to grow at 17% CAGR in FY18-21E, mainly driven by 11% revenue CAGR and improving operating margin (28% in FY20E, vs. 24% in FY18).

We expect gross margin to pick up in FY19E, for lower revenue mix from entertainment (with lower GPM). In terms of operating margin, we expect opex ratio to rise in FY19E, but decline from FY20E, for operating leverage. Overall, we expect its adj. net margin up to 24%/24%/25% in FY19/20/21E.

As a result, we forecast its net profit to reach RMB2,086mn in FY19E, with net margin up to 24% in FY19E.

Figure 23: Income statement

RMB mn, Dec-YE	FY16	FY17	FY18	FY19E	FY20E	FY21E
Revenue	6,159	7,930	8,034	8,651	9,945	11,056
Cost of sales	(2,404)	(3,381)	(3,550)	(3,114)	(3,852)	(4,326)
Gross profit	3,755	4,549	4,484	5,537	6,094	6,731
Sales and marketing expenses	(755)	(744)	(880)	(887)	(970)	(1,078)
Research and development expenses	-	-	(1,413)	(1,665)	(1,780)	(1,924)
General and administrative expenses	(1,836)	(2,073)	(704)	(737)	(788)	(903)
Other income	37	(143)	406	182	229	307
Operating (loss)/profit	1,201	1,589	1,892	2,431	2,785	3,132
Non-operating income	157	72	31	30	50	50
Non-operating expenses	(2)	(13)	(7)	(7)	(7)	(7)
Profit before taxation	1,356	1,649	1,916	2,453	2,828	3,175
Income tax expense	(223)	(189)	(156)	(307)	(353)	(397)
Profit for the year	1,133	1,460	1,759	2,147	2,474	2,778
Non-controlling interests	33	45	(53)	(61)	(65)	(59)
Net profit attributable to equity shareholders	1,166	1,505	1,706	2,086	2,410	2,719
Margin Analysis						
Gross margin	61%	57%	56%	64%	61%	61%
Operating margin	20%	20%	24%	28%	28%	28%
Net margin	19%	19%	21%	24%	24%	25%
Growth Analysis						
Revenue		29%	1%	8%	15%	11%
Gross profit		21%	-1%	23%	10%	10%
Operating profit		32%	19%	28%	15%	12%
Net profit		29%	13%	22%	16%	13%

Source: Company data, CMBIS estimates

Balance Sheet

Healthy balance sheet with net cash position in FY19/20/21E

According to our estimates of profit before taxation and change in working capital, PW has strong operating cash inflow in supporting CAPEX in the next three years. Therefore, we believe PW can stay in net cash position in FY19/20/21E. We expect PW to hold RMB7.2bn/RMB9.4bn cash and cash equivalent as of 31 Dec of 2019E and 2020E.

Figure 24: Balance Sheet

RMB mn, Dec-YE	FY17	FY18	FY19E	FY20E	FY21E
Non-current assets	6,339	5,195	4,233	3,380	2,562
Fixed asset	491	362	300	238	184
LT investment	3,237	3,452	3,622	3,712	3,802
Intangible assets	114	87	94	98	100
Others	2,496	1,294	217	-668	-1,524
Current assets	10,246	10,783	13,519	16,690	19,978
Cash	3,236	4,229	7,165	9,390	11,998
Prepayment	852	790	693	857	962
Account receivable	1,662	1,964	2,115	2,432	2,703
Others	4,497	3,800	3,547	4,011	4,314
Current liabilities	5,215	3,921	3,992	4,330	4,562
Short-term debt	618	1,270	1,270	1,270	1,270
Customer advances	529	409	441	507	563
Accounts Payable	1,803	1,372	1,204	1,489	1,672
1-year loan	1,106	0	200	200	200
Others	1,160	870	877	864	856
Non-current liabilities	2,552	2,725	2,525	2,325	2,125
Borrowings	500	794	594	394	194
Others	2,052	1,932	1,932	1,932	1,932
MI	823	870	925	983	1,036
Total Equity	8,787	9,309	11,213	13,392	15,829
Shareholders' equity	7,964	8,439	10,288	12,409	14,793

Source: Company data, CMBIS estimates

Cash Flow and Working Capital

Solid pipeline to ensure strong operating cash flow

Leveraging its strong pipeline and margin improvement, we expect PW to maintain its strong operating cash inflow trend and record RMB2,244mn / RMB1,803mn of operating cash inflow in FY19/20E, respectively.

Figure 25: Cash flow and working capital analysis

RMB mn, Dec-YE	FY17	FY18	FY19E	FY20E	FY21E
Net income	1,505	1,706	2,086	2,410	2,719
D&A	280	166	117	103	105
Change in WC	(1,074)	(1,261)	59	(630)	(468)
Others	93	(742)	(18)	(80)	(171)
Operating CF	804	(130)	2,244	1,803	2,185
Capex	(194)	(141)	67	(69)	(69)
Associates	-	-	-	-	-
Others	1,909	3,117	960	922	886
Investing CF	1,715	2,976	1,027	853	817
Equity raised	2	0	-	-	-
Change of Debts	(359)	(160)	-	(200)	(200)
Others	(1,095)	(1,793)	(336)	(231)	(194)
Financing CF	(1,451)	(1,952)	(336)	(431)	(394)
Net change in cash	1,032	920	2,936	2,226	2,608
Cash (beg of yr)	1,900	2,931	3,852	6,788	9,013
FX	(37)	27	-	-	-
Cash (end of yr)	2,931	3,852	6,788	9,013	11,621

Source: Company data, CMBIS estimates

Valuation

Investment Thesis

We initiate BUY with DCF-based TP of RMB49, implying 26.7x FY20E P/E. We think the majority of PW's solid FY19E financials have been partly priced in, and PW's positive price drivers and catalysts originate from: 1) further performance of new games, and 2) stepping-up contribution from entertainment after regulation headwinds.

Initiate with BUY

We use DCF valuation as our primary method since it is suitable to apply DCF valuation to game companies with healthy cash flows in the long run. Assuming a WACC of 13.9% and a terminal growth rate of 3%, our estimated TP is RMB49, representing 26.7x FY20E P/E, slightly higher than industry average of 23.5x FY20E P/E.

Figure 26: DCF valuation

DCF Valuation (RMB mn)										
	2020E	2021E	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E
EBIT	2,785	3,132	3,915	4,845	5,938	7,211	8,679	10,358	12,261	14,402
Tax	(353)	(397)	(496)	(614)	(752)	(914)	(1,100)	(1,312)	(1,554)	(1,825)
D&A	103	105	110	113	117	120	124	128	131	135
Change in working capital	(630)	(468)	(374)	(300)	(240)	(192)	(153)	(123)	(98)	(79)
CAPEX	(69)	(69)	(71)	(72)	(74)	(75)	(77)	(78)	(80)	(81)
FCF	1,836	2,302	3,084	3,973	4,989	6,150	7,473	8,972	10,661	12,553
Terminal Value										118,928

Assumptions	
WACC	13.9%
Tax rate	-12.0%
Risk free rate	3.53%
Cost of debt	6.0%
Beta	1.20
Market risk return	11.4%
Cost of equity	14.1%
Debt/Assets	2.6%
Long term growth	3.0%
Debt	0

Equity Value	
PV	58,630
minus: Net debt (RMB mn)	(5,695)
minus: Minority interest (RMB mn)	0
Equity Value (RMB mn)	64,325
Shares(mn)	1,315
TP (RMB)	49

		WACC					
		~	12%	13%	14%	15%	16%
Terminal growth rate	1.5%	56.1	50.0	45.6	40.8	37.3	
	2.0%	57.8	51.3	46.6	41.6	37.9	
	2.5%	59.6	52.7	47.7	42.4	38.6	
	3.0%	61.6	54.2	48.9	43.3	39.3	
	3.5%	63.8	55.9	50.2	44.3	40.0	
	4.0%	66.4	57.7	51.7	45.4	40.9	
	4.5%	69.2	59.8	53.3	46.6	41.8	

Source: Company data, Bloomberg, CMBIS estimates

Peers comparison

We selected six games comps ((Tencent, NetEase, Kingsoft, Perfect World, Sanqi, Giant)) and four entertainment comps (TME, BILI, IQ, China Literature) as peers, to reflect its business model. Average FY20E P/E of China games and entertainment are 23.5x and 24.0x, respectively. Our DCF-based TP implies multiple of 26.7x FY20E P/E, slightly higher than industry average, for its higher earnings growth and strong pipeline. We believe its solid games and entertainment rebound could be further catalysts.

Figure 27: Peers valuation

Company	Ticker	Mkt.Cap (USD mn)	Currency	Price	P/E			P/S			EV/EBITDA			FY19-21 EPS CAGR
					FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	
Leaders														
Tencent	700 HK	453,672	HKD	378	33.7	28.0	23.1	8.5	6.8	5.6	24.5	20.1	16.8	21%
Alibaba	BABA US	555,243	USD	207										
Baidu	BIDU US	42,685	USD	123	22.6	18.0	13.9	2.8	2.5	2.3	18.6	11.8	10.2	28%
JD	JD US	50,580	USD	35	35.0	25.4	19.2	0.6	0.5	0.5	22.6	15.7	12.2	35%
Meituan	3690 HK	78,109	HKD	103	338.7	79.2	36.8	5.7	4.3	3.4	119.8	51.4	26.7	203%
Pinduoduo	PDD US	44,960	USD	39	NA	544.7	52.1	10.3	6.2	4.5	NA	NA	774.0	NA
NetEase	NTES US	38,985	USD	305	19.3	18.8	17.1	4.2	4.0	3.6	14.2	12.8	11.7	8%
Average					27.8	22.8	18.5	5.7	4.3	3.5	37.1	21.7	123.7	53%
Ecommerce														
Alibaba	BABA US	555,243	USD	207										
JD	JD US	50,580	USD	35	35.0	25.4	19.2	0.6	0.5	0.5	22.6	15.7	12.2	35%
Pinduoduo	PDD US	44,960	USD	39	NA	544.7	52.1	10.3	6.2	4.5	NA	NA	774.0	NA
Vipshop	VIPS US	9,266	USD	14	14.8	11.9	10.9	0.7	0.7	0.6	10.5	8.3	7.6	16%
Babytree	1761 HK	388	HKD	2	NA	NA	232.3	5.5	4.5	3.5	NA	NA	22.9	NA
Average					26.1	20.4	25.4	4.9	3.6	2.8	18.8	14.1	166.3	24%
OTA														
Ctrip	TCOM US	20,059	USD	34	25.5	21.2	17.1	3.9	3.5	3.0	24.6	19.4	15.4	22%
Tongcheng-elong	780 HK	3,446	HKD	13	17.1	13.6	10.9	3.3	2.7	2.2	10.4	7.7	6.1	24%
Tuniu	TOUR US	287	USD	2	NA	22.1	11.9	0.9	0.9	0.8	NA	NA	NA	NA
Average					21.3	19.0	13.3	2.7	2.3	2.0	17.5	13.5	10.8	3%
Game														
Tencent	700 HK	453,672	HKD	378	33.7	28.0	23.1	8.5	6.8	5.6	24.5	20.1	16.8	21%
NetEase	NTES US	38,985	USD	305	19.3	18.8	17.1	4.2	4.0	3.6	14.2	12.8	11.7	7%
Kingsoft	3888 HK	3,447	HKD	19	NA	71.7	40.7	3.1	2.3	1.8	141.7	28.6	17.6	NA
Perfect World	002624 CH	7,406	CNY	41	24.9	21.4	18.7	6.1	5.2	4.6	20.2	17.8	16.0	15%
Sanqi Interactive	002555 CH	7,553	CNY	26	25.4	21.9	19.4	4.3	3.7	3.3	19.6	17.1	14.7	14%
Giant Interactive	002558 CH	5,177	CNY	18	32.3	27.3	25.6	8.6	7.7	6.9	NA	NA	NA	12%
Average					27.1	23.5	20.8	5.8	5.0	4.3	19.6	17.0	14.8	17%
Live streaming														
MOMO	MOMO US	7,554	USD	36	13.0	10.9	9.5	3.1	2.6	2.3	11.3	7.9	6.7	19%
YY	YY US	4,525	USD	56	14.0	10.4	7.5	1.2	1.0	0.8	9.7	6.6	3.8	38%
Inke	3700 HK	272	HKD	1	4.5	2.4	2.4	NA	NA	NA	NA	NA	NA	38%
Huya	HUYA US	3,803	USD	17	38.8	22.9	15.4	3.2	2.3	1.9	39.5	16.3	10.5	65%
Average					17.6	11.6	8.7	2.5	2.0	1.7	20.2	10.3	7.0	39%
Entertainment														
Tencent Music	TME US	18,788	USD	11.5	29.4	23.9	17.9	5.2	4.1	3.2	24.6	18.7	13.6	28%
iQiyi	IQ US	14,352	USD	19.7	NA	NA	NA	3.5	3.0	2.5	27.8	16.3	9.0	-48%
China Literature	772 HK	4,333	HKD	33.3	29.6	24.2	20.6	4.4	3.8	3.3	17.3	13.5	11.6	21%
Bilibili	BILI US	5,857	USD	18.0	NA	NA	102.6	6.1	4.2	3.2	NA	252.3	29.9	NA
Average					29.5	24.0	47.0	4.8	3.8	3.1	23.3	75.2	16.0	0%
Ads														
Baidu	BIDU US	42,685	USD	123.2	22.6	18.0	13.9	2.8	2.5	2.3	18.6	11.8	10.2	30%
Weibo	WB US	10,113	USD	44.9	16.5	15.8	13.8	5.7	5.3	4.7	14.0	12.9	11.3	10%
Sina	SINA US	2,590	USD	37.3	13.3	13.3	10.7	1.2	1.1	1.0	5.3	4.9	4.1	14%
Mobvista	1860 HK	662	HKD	3.4	15.4	9.8	6.4	1.2	1.0	0.8	15.3	8.0	5.5	46%
Duiba	1753 HK	646	HKD	4.6	20.2	8.4	5.9	2.3	1.6	1.2	16.8	5.3	3.6	232%
58.com	WUBA US	9,299	USD	62.2	16.3	18.8	17.2	4.2	3.7	3.3	17.2	14.8	12.4	0%
Average					17.4	14.0	11.3	2.9	2.5	2.2	14.5	9.6	7.8	33%
Total Average					20.8	17.3	16.7	4.0	3.3	2.8	23.2	23.3	41.0	29.6%

Source: Bloomberg

Note: Data updated by 18 Dec 2019

Key Investment Risks

Key investment risks might derive from: 1) Uncertainty in regulations; 2) slower-than-expected launch of new games; 3) grossing decline of hot titles; and 4) film headwinds.

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue	7,930	8,034	8,651	9,945	11,056
Film & TV	2,277	2,611	2,015	2,352	2,582
Games	5,622	5,389	6,636	7,594	8,475
Others	31	33	33	33	33
COGS	(3,381)	(3,550)	(3,114)	(3,852)	(4,326)
Gross profit	4,549	4,484	5,537	6,094	6,731
S&M	(744)	(880)	(887)	(970)	(1,078)
Admin. Exp.	(2,073)	(704)	(737)	(788)	(903)
R&D	-	(1,413)	(1,665)	(1,780)	(1,924)
Others	(328)	(144)	(70)	75	160
Operating profit	1,589	1,892	2,431	2,785	3,132
Non-operating Rev	72	31	30	50	50
Non-operating Exp	(13)	(7)	(7)	(7)	(7)
Pre-tax Income	1,649	1,916	2,453	2,828	3,175
Income Tax	(189)	(156)	(307)	(353)	(397)
Less: MI	45	(53)	(61)	(65)	(59)
Net profit	1,505	1,706	2,086	2,410	2,719

Cash flow summary

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Net income	1,505	1,706	2,086	2,410	2,719
D&A	280	166	117	103	105
Change in WC	(1,074)	(1,261)	59	(630)	(468)
Others	93	(742)	(18)	(80)	(171)
Operating CF	804	(130)	2,244	1,803	2,185
Capex	(194)	(141)	67	(69)	(69)
Associates	-	-	-	-	-
Others	1,909	3,117	960	922	886
Investing CF	1,715	2,976	1,027	853	817
Equity raised	2	0	-	-	-
Change of Debts	(359)	(160)	-	(200)	(200)
Others	(1,095)	(1,793)	(336)	(231)	(194)
Financing CF	(1,451)	(1,952)	(336)	(431)	(394)
Net change in cash	1,032	920	2,936	2,226	2,608
Cash (beg of yr)	1,900	2,931	3,852	6,788	9,013
FX	(37)	27	-	-	-
Cash (end of yr)	2,931	3,852	6,788	9,013	11,621

Balance sheet

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Non-current assets	6,339	5,195	4,233	3,380	2,562
Fixed asset	491	362	300	238	184
LT investment	3,237	3,452	3,622	3,712	3,802
Intangible assets	114	87	94	98	100
Others	2,496	1,294	217	(668)	(1,524)
Current assets	10,246	10,783	13,519	16,690	19,978
Cash	3,236	4,229	7,165	9,390	11,998
Restricted cash	852	790	693	857	962
Account receivable	1,662	1,964	2,115	2,432	2,703
Others	4,497	3,800	3,547	4,011	4,314
Current liabilities	5,215	3,921	3,992	4,330	4,562
Short-term debt	618	1,270	1,270	1,270	1,270
Customer advances	529	409	441	507	563
Accounts Payable	1,803	1,372	1,204	1,489	1,672
1-year loan	1,106	-	200	200	200
Others	1,160	870	877	864	856
Non-current liabilities	2,552	2,725	2,525	2,325	2,125
Borrowings	500	794	594	394	194
Others	2,052	1,932	1,932	1,932	1,932
MI	823	870	925	983	1,036
Total Equity	8,787	9,309	11,213	13,392	15,829
Shareholders' equity	7,964	8,439	10,288	12,409	14,793

Key ratios

YE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Sales mix (%)					
Film & TV	28.7	32.5	23.3	23.6	23.4
Games	70.9	67.1	76.7	76.4	76.6
Others	0.4	0.4	0.4	0.3	0.3
Total	100.0	100.0	100.4	100.3	100.3
Growth rate (%)					
Revenue	28.8	1.3	7.7	15.0	11.2
Gross profit	21.1	(1.4)	23.5	10.0	10.5
EBIT	32.3	19.1	28.5	14.6	12.4
Net profit	77.4	22.1	12.6	19.4	13.5
P&L ratios (%)					
OPM	20.0	23.6	28.1	28.0	28.3
Pre-tax margin	20.8	23.8	28.4	28.4	28.7
Net margin	17.6	21.2	22.2	23.1	23.5
tax rate	(2.4)	(1.9)	(3.5)	(3.6)	(3.6)
Returns (%)					
ROE	17.5	20.2	18.7	18.5	17.6
ROA	9.1	10.7	11.7	12.0	12.1
Per share					
EPS (RMB)	1.14	1.30	1.59	1.83	2.07
DPS (RMB)	0.17	0.18	0.22	0.25	0.29
BVPS (RMB)	2.23	2.93	5.16	6.86	8.84

Source: Company data, CMBIS estimates

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