

# Tencent (700 HK)

## Inline 2Q24 results; games business to drive revenue growth acceleration in 2H24E

Tencent reported 2Q24 results on 14 Aug: total revenue grew by 8% YoY to RMB161.1bn, in line with our/consensus estimate of RMB160.9/161.4bn; non-IFRS operating profit grew by 27% YoY to RMB58.4bn, largely in line with our estimate of RMB57.7bn; non-IFRS net income increased by 53% YoY to RMB57.3bn and was 17/18% ahead of our/consensus estimate, mainly due to the increase in share of profit of associates (+RMB6.6bn YoY). Underpinned by strong growth in game gross receipt, we are upbeat on the revenue growth acceleration and earnings growth in 2H24. E-commerce ecosystem development will support consumer internet revenue growth in mid-to-long term, while FBS revenue should bounce back as economic momentum recovers. We maintain our FY24-26E operating profit forecast largely unchanged but raise non-IFRS net income forecast by 5-8% to factor in the higher share of profit of associates. We maintain our SOTP-derived TP at HK\$480.0 and the BUY rating.

- **Game business recorded solid recovery in 2Q24.** Games revenue grew by 9% YoY to RMB48.5bn in 2Q24 (3% ahead of consensus). Domestic games revenue increased by 9% YoY to RMB34.6bn in 2Q24, with gross receipts growth outpacing revenue growth, driven by successful launch of *DnF Mobile* and recovery of flagship titles *Honor of Kings* & *Peacekeeper Elite*. International games revenue grew by 9% YoY to RMB13.9bn in 2Q24. And international games gross receipts recorded significantly faster YoY growth than its revenue, driven by the strong performance of *PUBG Mobile* and Supercell's games. Fuelled by strong growth in game gross receipts, we expect growth of games revenue to accelerate to +15% YoY in 2H24E.
- **Inline ad revenue growth despite macro uncertainty.** Online ad revenue grew by 19% YoY to RMB29.9bn in 2Q24 (in line with consensus), primarily driven by strong ad revenue growth from Video Accounts (VA) and long-form video, partially offset by decline in mobile ad network revenue. VA ad revenue grew by 80%+ YoY in 2Q24, due to growing user engagement and strong demand for live streaming promotions.
- **Fintech business under pressure amid soft consumption.** Fintech and Business Services (FBS) revenue was up by 4% YoY to RMB50.4bn in 2Q24 (1Q24/4Q23: +7/15% YoY). Fintech revenue recorded low single-digit YoY growth in 2Q24, with moderation in payment revenue growth and decline in consumer loan revenue due to stricter risk control. Business services segment remained resilient and registered a teens YoY growth rate in 2Q24, fuelled by solid growth of cloud and VA e-commerce revenue.
- **Earnings growth momentum continues.** Tencent's GPM rose by 5.8ppt YoY to 53.5% in 2Q24, within which VAS/ad/FBS GPM +3.0/6.7/9.2ppt YoY respectively, driven by high-margin revenue streams such as Domestic Games, Mini Games and VA. We forecast non-IFRS net income to record a FY24-26E CAGR of 18%, supported by the high-quality growth strategy. Current valuation of 15x FY24E non-IFRS PE offers attractive value. BUY.

### Earnings Summary

| (YE 31 Dec)                  | FY22A     | FY23A     | FY24E     | FY25E     | FY26E     |
|------------------------------|-----------|-----------|-----------|-----------|-----------|
| Revenue (RMB mn)             | 554,552   | 609,015   | 658,187   | 709,755   | 758,014   |
| Adjusted net profit (RMB mn) | 115,649.0 | 157,688.0 | 214,576.3 | 232,392.0 | 251,333.7 |
| EPS (Adjusted) (RMB)         | 12.13     | 16.66     | 22.16     | 24.00     | 25.95     |
| P/E (x)                      | 51.8      | 30.3      | 19.7      | 17.1      | 17.0      |

Source: Company data, Bloomberg, CMBIGM estimates

**BUY (Maintain)**

Target Price **HK\$480.00**  
 Up/Downside **28.4%**  
 Current Price **HK\$373.80**

### China Internet

**Saiyi HE, CFA**  
 (852) 3916 1739  
 hesaiyi@cmbi.com.hk

**Wentao LU, CFA**  
 luwentao@cmbi.com.hk

**Ye TAO**  
 franktao@cmbi.com.hk

### Stock Data

|                          |               |
|--------------------------|---------------|
| Mkt Cap (HK\$ mn)        | 3,486,526.1   |
| Avg 3 mths t/o (HK\$ mn) | 7,265.0       |
| 52w High/Low (HK\$)      | 397.00/262.20 |
| Total Issued Shares (mn) | 9327.3        |

Source: FactSet

### Shareholding Structure

|                               |       |
|-------------------------------|-------|
| MIH TC                        | 25.6% |
| Advance Data Services Limited | 8.4%  |

Source: HKEx

### Share Performance

|       | Absolute | Relative |
|-------|----------|----------|
| 1-mth | -5.8%    | 0.6%     |
| 3-mth | -2.1%    | 9.1%     |
| 6-mth | 28.9%    | 19.6%    |

Source: FactSet

### 12-mth Price Performance



Source: FactSet

## Business forecasts update and valuation

Figure 1: Tencent: forecast revision

| (RMB bn)            | Current |       |       | Previous |       |       | Change (%) |          |          |
|---------------------|---------|-------|-------|----------|-------|-------|------------|----------|----------|
|                     | FY24E   | FY25E | FY26E | FY24E    | FY25E | FY26E | FY24E      | FY25E    | FY26E    |
| Revenue             | 658.2   | 709.8 | 758.0 | 658.3    | 712.3 | 764.4 | 0.0%       | -0.4%    | -0.8%    |
| Gross profit        | 350.7   | 380.7 | 410.7 | 349.4    | 383.0 | 415.1 | 0.4%       | -0.6%    | -1.0%    |
| Operating profit    | 207.5   | 229.5 | 250.6 | 208.4    | 230.6 | 252.1 | -0.5%      | -0.5%    | -0.6%    |
| Adjusted net profit | 214.6   | 232.4 | 251.3 | 198.8    | 218.6 | 238.9 | 7.9%       | 6.3%     | 5.2%     |
| Adjusted EPS (RMB)  | 22.2    | 24.0  | 26.0  | 20.5     | 22.6  | 24.7  | 7.9%       | 6.3%     | 5.2%     |
| Gross margin        | 53.3%   | 53.6% | 54.2% | 53.1%    | 53.8% | 54.3% | 0.2 ppt    | -0.1 ppt | -0.1 ppt |
| Operating margin    | 31.5%   | 32.3% | 33.1% | 31.7%    | 32.4% | 33.0% | -0.1 ppt   | 0.0 ppt  | 0.1 ppt  |
| Adjusted net margin | 32.6%   | 32.7% | 33.2% | 30.2%    | 30.7% | 31.3% | 2.4 ppt    | 2.1 ppt  | 1.9 ppt  |

Source: CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

| (RMB bn)            | CMBIGM |       |       | Consensus |       |       | Diff (%) |          |          |
|---------------------|--------|-------|-------|-----------|-------|-------|----------|----------|----------|
|                     | FY24E  | FY25E | FY26E | FY24E     | FY25E | FY26E | FY24E    | FY25E    | FY26E    |
| Revenue             | 658.2  | 709.8 | 758.0 | 665.5     | 730.6 | 797.1 | -1.1%    | -2.8%    | -4.9%    |
| Gross profit        | 350.7  | 380.7 | 410.7 | 350.7     | 390.7 | 430.9 | 0.0%     | -2.6%    | -4.7%    |
| Operating profit    | 207.5  | 229.5 | 250.6 | 214.3     | 244.0 | 273.5 | -3.2%    | -5.9%    | -8.3%    |
| Adjusted net profit | 214.6  | 232.4 | 251.3 | 201.3     | 224.0 | 251.6 | 6.6%     | 3.7%     | -0.1%    |
| Adjusted EPS (RMB)  | 22.2   | 24.0  | 26.0  | 20.9      | 23.4  | 26.2  | 6.0%     | 2.4%     | -1.1%    |
| Gross margin        | 53.3%  | 53.6% | 54.2% | 52.7%     | 53.5% | 54.1% | 0.6 ppt  | 0.2 ppt  | 0.1 ppt  |
| Operating margin    | 31.5%  | 32.3% | 33.1% | 32.2%     | 33.4% | 34.3% | -0.7 ppt | -1.1 ppt | -1.2 ppt |
| Adjusted net margin | 32.6%  | 32.7% | 33.2% | 30.2%     | 30.7% | 31.6% | 2.4 ppt  | 2.1 ppt  | 1.6 ppt  |

Source: Bloomberg, CMBIGM estimates

Figure 3: Tencent: quarterly financials

| (RMB bn)                   | 3Q22  | 4Q22  | 1Q23   | 2Q23  | 3Q23  | 4Q23   | 1Q24   | 2Q24  | Cons. | Diff%   | CMBI  | Diff%    |
|----------------------------|-------|-------|--------|-------|-------|--------|--------|-------|-------|---------|-------|----------|
| SNS revenue                | 29.9  | 28.6  | 31.0   | 29.7  | 29.7  | 28.2   | 30.5   | 30.3  | 30.5  | -0.6%   | 30.2  | 0.5%     |
| YoY %                      | -1.4% | -1.7% | 6.3%   | 1.6%  | -0.4% | -1.5%  | -1.4%  | 2.2%  |       |         |       |          |
| QoQ %                      | 2.3%  | -4.2% | 8.2%   | -4.2% | 0.3%  | -5.3%  | 8.3%   | -0.7% |       |         |       |          |
| Games revenue              | 42.9  | 41.8  | 48.4   | 44.5  | 46.0  | 40.9   | 48.1   | 48.5  | 47.3  | 2.5%    | 47.7  | 1.8%     |
| YoY %                      | -4.6% | -2.3% | 10.9%  | 4.8%  | 7.4%  | -2.2%  | -0.5%  | 8.9%  |       |         |       |          |
| QoQ %                      | 0.8%  | -2.5% | 15.7%  | -7.9% | 3.3%  | -11.1% | 17.6%  | 0.8%  |       |         |       |          |
| Online ad revenue          | 21.4  | 24.7  | 21.0   | 25.0  | 25.7  | 29.8   | 26.5   | 29.9  | 29.4  | 1.7%    | 29.4  | 1.6%     |
| YoY %                      | -4.7% | 14.6% | 16.5%  | 34.2% | 20.0% | 20.8%  | 26.4%  | 19.5% |       |         |       |          |
| QoQ %                      | 15.0% | 15.0% | -15.0% | 19.3% | 2.9%  | 15.8%  | -11.0% | 12.7% |       |         |       |          |
| FBS revenue                | 44.8  | 47.2  | 48.7   | 48.6  | 52.0  | 54.4   | 52.3   | 50.4  | 52.4  | -3.8%   | 52.1  | -3.1%    |
| YoY %                      | 3.5%  | -1.5% | 13.9%  | 15.2% | 16.1% | 15.1%  | 7.4%   | 3.7%  |       |         |       |          |
| QoQ %                      | 6.2%  | 5.4%  | 3.1%   | -0.1% | 7.0%  | 4.5%   | -3.8%  | -3.6% |       |         |       |          |
| <b>Total revenue</b>       | 140.1 | 145.0 | 150.0  | 149.2 | 154.6 | 155.2  | 159.5  | 161.1 | 161.4 | -0.1%   | 160.9 | 0.1%     |
| YoY %                      | -1.6% | 0.5%  | 10.7%  | 11.3% | 10.4% | 7.1%   | 6.3%   | 8.0%  |       |         |       |          |
| QoQ %                      | 4.5%  | 3.5%  | 3.5%   | -0.5% | 3.6%  | 0.4%   | 2.8%   | 1.0%  |       |         |       |          |
| Overall GPM                | 44.2% | 42.6% | 45.5%  | 47.5% | 49.5% | 50.0%  | 52.6%  | 53.3% | 52.7% | 0.6 ppt | 53.4% | -0.1 ppt |
| G&A%                       | 18.9% | 18.8% | 16.4%  | 17.0% | 17.0% | 17.5%  | 15.6%  | 17.1% |       |         |       |          |
| S&M%                       | 5.1%  | 4.2%  | 4.7%   | 5.6%  | 5.1%  | 7.1%   | 4.7%   | 5.7%  |       |         |       |          |
| Non-IFRS net margin        | 24.7% | 20.5% | 21.7%  | 25.2% | 29.1% | 27.5%  | 31.5%  | 35.6% |       |         |       |          |
| <b>Non-IFRS net profit</b> | 34.6  | 29.7  | 32.5   | 37.5  | 44.9  | 42.7   | 50.3   | 57.3  | 48.7  | 17.8%   | 49.2  | 16.5%    |
| YoY %                      | 8.9%  | 19.4% | 44.9%  | 29.9% | 30.0% | 43.7%  | 54.5%  | 52.6% |       |         |       |          |

Source: Company data, CMBIGM estimates

Our SOTP-derived target price of HK\$480.0 comprises, per share:

- 1) HK\$190.6 for the online games business, based on an 18x 2024E PE, which is on par with the average PE for its global gaming peers.
- 2) HK\$30.0 for the SNS business, including the market cap of Tencent's stake in its subsidiaries, the valuation of Tencent Video (based on a 2.5x 2024E PS, at a premium to the 1.6x average PS of its peers given its content and user traffic leadership), and the valuation of other membership services (based on a 2.0x 2024E PS).
- 3) HK\$83.5 for the advertising business, based on an 18x 2024E PE, which is at a premium to the industry average (17x). This reflects Tencent's more resilient ad revenue growth outlook, supported by the solid performance of Weixin Video Account and Mini Program.
- 4) HK\$79.7 for the fintech business, based on a 4.0x 2024E PS, at a premium to the peer average (1.8x). This mainly reflects Tencent's strong leadership in China's digital payment market and its potential to capture other fintech business opportunities.
- 5) HK\$20.7 for the cloud business, based on a 4.0x 2024E PS, at a discount to the industry average (5.6x) as Tencent's current offerings mainly involve the lower-margin IaaS business.
- 6) HK\$67.3 for strategic investments, based on the current market value of Tencent's listed investments and the book value of its unlisted investments. We apply a 30% holding company discount to the fair value of Tencent's equity investments.
- 7) HK\$8.2 for net cash.

**Figure 4: Tencent: SOTP valuation**

|   | 2024E net<br>profit<br>(RMBmn) | 2024E<br>revenue<br>(RMBmn) | 2024E<br>PE (x) | 2024E<br>PS (x) | Market cap<br>(RMBmn) | Valuation<br>to Tencent<br>(RMBmn) | As % of<br>total<br>valuation | Per share<br>valuation<br>(HK\$) |
|---|--------------------------------|-----------------------------|-----------------|-----------------|-----------------------|------------------------------------|-------------------------------|----------------------------------|
| Online games                                | 90,850                         |                             | 18x             |                 |                       | 1,635,307                          | 39.7                          | 190.6                            |
| Social network services (SNS)               |                                | 119,761                     |                 |                 |                       | 257,086                            | 6.2                           | 30.0                             |
| Tencent Music (TME)                         |                                |                             |                 |                 | 136,402               | 75,157                             | 1.8                           | 8.8                              |
| China Literature                            |                                |                             |                 |                 | 23,233                | 13,749                             | 0.3                           | 1.6                              |
| Huya  |                                |                             |                 |                 | 8,284                 | 3,927                              | 0.1                           | 0.5                              |
| Online video – subscription                 |                                | 20,700                      |                 | 2.5x            |                       | 51,750                             | 1.3                           | 6.0                              |
| Others                                      |                                | 56,251                      |                 | 2.0x            |                       | 112,503                            | 2.7                           | 13.1                             |
| Online advertising                          | 39,817                         |                             | 18x             |                 |                       | 716,697                            | 17.4                          | 83.5                             |
| Fintech                                     |                                | 171,049                     |                 | 4.0x            |                       | 684,198                            | 16.6                          | 79.7                             |
| Cloud (business services)                   |                                | 44,400                      |                 | 4.0x            |                       | 177,602                            | 4.3                           | 20.7                             |
| Net cash                                    |                                |                             |                 |                 |                       | 70,486                             | 1.7                           | 8.2                              |
| <b>Valuation of core business</b>           |                                |                             |                 |                 |                       | <b>3,541,377</b>                   |                               |                                  |
| RMB/HK\$                                    |                                |                             |                 |                 |                       | 0.92                               |                               |                                  |
| <b>Valuation of core business (HK\$mn)</b>  |                                |                             |                 |                 |                       | <b>3,849,322</b>                   |                               |                                  |
| Valuation per share – core business (HK\$)  |                                |                             |                 |                 |                       | <b>412.7</b>                       |                               |                                  |
| Valuation per share – investments (HK\$)    |                                |                             |                 |                 |                       | 67.3                               | 14.0                          |                                  |
| <b>Valuation per share – Tencent (HK\$)</b> |                                |                             |                 |                 |                       | <b>480.0</b>                       |                               |                                  |

Source: Company data, CMBIGM estimates

**Figure 5: Peer comparison: online games and advertising sector**

|                      |           | Price   | EPS growth (YoY %) |       |       | PE (x) |       |       |
|----------------------|-----------|---------|--------------------|-------|-------|--------|-------|-------|
| Companies            | Ticker    | (LC)    | FY24E              | FY25E | FY26E | FY24E  | FY25E | FY26E |
| Online games         |           |         |                    |       |       |        |       |       |
| NetEase              | NTES US   | 89.5    | 6                  | 7     | 5     | 12     | 11    | 11    |
| Electronic Arts      | EA US     | 146.9   | 19                 | 5     | 14    | 21     | 20    | 17    |
| Take Two Interactive | TTWO US   | 144.9   | (37)               | 11    | 192   | NA     | NA    | 20    |
| Nexon                | 3659 JP   | 2,831.5 | 4                  | 10    | 6     | 19     | 17    | 16    |
| Nintendo             | 7974 JP   | 7,955.0 | 16                 | (25)  | 19    | 21     | 27    | 23    |
| Bandai Namco         | 7832 JP   | 2,861.0 | (14)               | 26    | 3     | 24     | 19    | 18    |
| Perfect World        | 002624 CH | 7.7     | (3)                | 27    | 16    | 17     | 14    | 12    |
| 37 Interactive       | 002555 CH | 13.2    | (9)                | 12    | 17    | 10     | 9     | 8     |
| Average PE           |           |         |                    |       |       | 18     | 17    | 16    |
| Online advertising   |           |         |                    |       |       |        |       |       |
| Focus Media          | 002027 CH | 5.9     | 9                  | 10    | 9     | 16     | 14    | 13    |
| Baidu                | BIDU US   | 86.2    | 3                  | 3     | 9     | 8      | 8     | 7     |
| Meta                 | Meta US   | 528.5   | 44                 | 14    | 15    | 25     | 21    | 19    |
| Google               | GOOG US   | 165.9   | 31                 | 12    | 12    | 21     | 19    | 17    |
| Average PE           |           |         |                    |       |       | 17     | 16    | 14    |

Source: Bloomberg, CMBIGM estimates

Note: Data as of market close on 13 Aug

**Figure 6: Peer comparison: online video, fintech, and cloud sectors**

|                       |           | Price | Revenue growth (YoY %) |       |       | PS (x) |       |       |
|-----------------------|-----------|-------|------------------------|-------|-------|--------|-------|-------|
| Companies             | Ticker    | (LC)  | FY24E                  | FY25E | FY26E | FY24E  | FY25E | FY26E |
| Online video          |           |       |                        |       |       |        |       |       |
| iQiyi                 | IQ US     | 3.3   | (0.4)                  | 5.5   | 4.9   | 0.7    | 0.7   | 0.6   |
| Mango Excellent Media | 300413 CH | 20.7  | 11.6                   | 9.3   | 7.9   | 2.4    | 2.2   | 2.1   |
| Average PS            |           |       |                        |       |       | 1.6    | 1.4   | 1.4   |
| Cloud                 |           |       |                        |       |       |        |       |       |
| Microsoft             | MSFT US   | 414.0 | 14.4                   | 14.5  | 14.1  | 11.0   | 9.6   | 8.4   |
| Google                | GOOG US   | 165.9 | 14.6                   | 19.2  | 10.4  | 6.9    | 5.8   | 5.3   |
| Salesforce            | CRM US    | 254.6 | 8.8                    | 9.2   | 0.0   | 6.5    | 6.0   | 6.0   |
| Kingsoft Cloud        | KC US     | 2.4   | 4.5                    | 8.4   | 10.1  | 0.6    | 0.5   | 0.5   |
| Amazon                | AMZN US   | 170.2 | 11.3                   | 10.9  | 10.9  | 2.8    | 2.5   | 2.3   |
| Average PS            |           |       |                        |       |       | 5.6    | 4.9   | 4.5   |
| Fintech               |           |       |                        |       |       |        |       |       |
| PayPal                | PYPL US   | 65.1  | 7.9                    | 7.9   | 8.1   | 2.1    | 1.9   | 1.8   |
| Square                | SQ US     | 63.4  | 13.5                   | 11.7  | 9.8   | 1.6    | 1.4   | 1.3   |
| Average PS            |           |       |                        |       |       | 1.8    | 1.7   | 1.5   |

Source: Bloomberg, CMBIGM estimates

Note: Data as of market close on 13 Aug

Our calculation of the valuation of Tencent's strategic investments is based on the current market value of Tencent's listed investments and the book value of its unlisted investments. We apply a 30% holding company discount to the fair value of Tencent's equity investments.

**Figure 7: Tencent: valuation of strategic investments**

| Name  | Ticker    | Tencent's stake % | Mkt cap (US\$m) | Value to Tencent (HK\$m) |
|---|-----------|-------------------|-----------------|--------------------------|
| PDD Holdings Inc                                    | PDD US    | 15.5              | 200,011         | 241,657                  |
| Sea Ltd   | SE US     | 18.2              | 42,840          | 60,815                   |
| Spotify Technology SA                               | SPOT US   | 8.4               | 67,219          | 43,989                   |
| Kuaishou Technology                                 | 1024 HK   | 15.7              | 25,070          | 30,622                   |
| NU Holdings Ltd/Cayman Islands                      | NU US     | 5.2               | 60,768          | 24,695                   |
| Snap Inc  | SNAP US   | 17.5              | 15,317          | 20,944                   |
| KE Holdings Inc                                     | BEKE US   | 11.3              | 18,047          | 15,907                   |
| Futu Holdings Ltd                                   | FUTU US   | 21.6              | 8,571           | 14,447                   |
| Krafton Inc   | 259960 KS | 13.5              | 11,556          | 12,159                   |
| Meituan   | 3690 HK   | 1.7               | 80,756          | 10,834                   |
| JD.com Inc  | 9618 HK   | 2.7               | 39,614          | 8,219                    |
| Vipshop Holdings Ltd                                | VIPS US   | 11.5              | 7,560           | 6,793                    |
| Tongcheng Travel Holdings Ltd                       | 780 HK    | 21.1              | 3,887           | 6,385                    |
| Bilibili Inc  | 9626 HK   | 13.4              | 5,848           | 6,116                    |
| Warner Music Group Corp                             | WMG US    | 4.9               | 14,455          | 5,547                    |
| Netmarble Corp                                      | 251270 KS | 17.5              | 3,946           | 5,392                    |
| Kanzhun Ltd   | BZ US     | 9.9               | 6,413           | 4,937                    |
| Yixin Group Ltd                                     | 2858 HK   | 53.9              | 612             | 2,570                    |
| Tuhu Car Inc  | 9690 HK   | 18.7              | 1,649           | 2,406                    |
| ZhongAn Online P&C Insurance C                      | 6060 HK   | 8.1               | 2,423           | 1,529                    |
| Kadokawa Corp                                       | 9468 JP   | 6.9               | 2,478           | 1,326                    |
| Maoyan Entertainment                                | 1896 HK   | 13.7              | 1,037           | 1,111                    |
| Lilium NV   | LILM US   | 29.3              | 482             | 1,102                    |
| Ubisoft Entertainment SA                            | UBI FP    | 5.5               | 2,418           | 1,030                    |
| Paradox Interactive AB                              | PDX SS    | 9.1               | 1,430           | 1,016                    |
| Other listed entities as a whole                    |           |                   | 44,517          | 21,197                   |
| <b>Listed investments (current value)</b>           |           |                   |                 | <b>552,747</b>           |
| <b>Unlisted investments (book value)</b>            |           |                   |                 | <b>356,964</b>           |
| <b>Total investment value</b>                       |           |                   |                 | <b>909,711</b>           |
| Holdco discount                                     |           |                   |                 | 30%                      |
| <b>Valuation of strategic investments</b>           |           |                   |                 | <b>636,798</b>           |
| <b>Valuation of strategic investments per share</b> |           |                   |                 | <b>67.3</b>              |

Source: Bloomberg, company data, CMBIGM estimates

Note: Data as of the market close on 13 Aug

**Risks**

Slower-than-expected GPM expansion; decline in revenue of legacy games; macro headwinds weigh on ads and FBS revenue growth.

## Financial Summary

| INCOME STATEMENT                           | 2021A            | 2022A            | 2023A            | 2024E            | 2025E            | 2026E            |
|--|------------------|------------------|------------------|------------------|------------------|------------------|
| YE 31 Dec (RMB mn)                         |                  |                  |                  |                  |                  |                  |
| Revenue                                    | 560,118          | 554,552          | 609,015          | 658,187          | 709,755          | 758,014          |
| Cost of goods sold                         | (314,174)        | (315,806)        | (315,906)        | (307,472)        | (329,062)        | (347,269)        |
| <b>Gross profit</b>                        | <b>245,944</b>   | <b>238,746</b>   | <b>293,109</b>   | <b>350,715</b>   | <b>380,692</b>   | <b>410,745</b>   |
| Operating expenses                         | 19,026           | (127,919)        | (133,035)        | (143,250)        | (151,159)        | (160,110)        |
| Selling expense                            | (40,594)         | (29,229)         | (34,211)         | (37,517)         | (39,037)         | (40,933)         |
| Admin expense                              | (89,847)         | (106,696)        | (103,525)        | (110,575)        | (117,110)        | (124,314)        |
| Others                                     | 149,467          | 8,006            | 4,701            | 4,842            | 4,987            | 5,137            |
| <b>Operating profit</b>                    | <b>264,970</b>   | <b>110,827</b>   | <b>160,074</b>   | <b>207,465</b>   | <b>229,534</b>   | <b>250,635</b>   |
| Share of (losses)/profits of associates/JV | (16,444)         | (16,129)         | 5,800            | 19,088           | 19,088           | 4,772            |
| Interest income                            | 6,650            | 8,592            | 13,808           | 14,550           | 13,379           | 4,227            |
| Interest expense                           | (7,114)          | (9,352)          | (12,268)         | (10,353)         | (2,846)          | (3,134)          |
| <b>Pre-tax profit</b>                      | <b>241,412</b>   | <b>85,346</b>    | <b>153,606</b>   | <b>216,201</b>   | <b>245,776</b>   | <b>252,273</b>   |
| Income tax                                 | (20,252)         | (21,516)         | (43,276)         | (50,478)         | (55,145)         | (60,056)         |
| <b>After tax profit</b>                    | <b>221,160</b>   | <b>63,830</b>    | <b>110,330</b>   | <b>165,723</b>   | <b>190,631</b>   | <b>192,217</b>   |
| Minority interest                          | (2,988)          | (466)            | (2,832)          | (3,221)          | (3,519)          | (3,833)          |
| <b>Net profit</b>                          | <b>218,172</b>   | <b>63,364</b>    | <b>107,498</b>   | <b>162,501</b>   | <b>187,111</b>   | <b>188,384</b>   |
| <b>Adjusted net profit</b>                 | <b>123,788</b>   | <b>115,649</b>   | <b>157,688</b>   | <b>214,576</b>   | <b>232,392</b>   | <b>251,334</b>   |
| Gross dividends                            | 12,704           | 20,256           | 28,485           | 40,421           | 44,159           | 48,092           |
| BALANCE SHEET                              | 2021A            | 2022A            | 2023A            | 2024E            | 2025E            | 2026E            |
| YE 31 Dec (RMB mn)                         |                  |                  |                  |                  |                  |                  |
| <b>Current assets</b>                      | <b>484,812</b>   | <b>565,989</b>   | <b>518,446</b>   | <b>517,171</b>   | <b>663,481</b>   | <b>846,559</b>   |
| Cash & equivalents                         | 167,966          | 156,739          | 172,320          | 152,351          | 251,410          | 398,968          |
| Account receivables                        | 49,331           | 45,467           | 46,606           | 50,573           | 52,900           | 54,802           |
| Inventories                                | 1,063            | 2,333            | 456              | 1,909            | 2,018            | 2,112            |
| Prepayment                                 | 65,390           | 76,685           | 88,411           | 81,815           | 85,578           | 91,732           |
| ST bank deposits                           | 83,813           | 104,776          | 185,983          | 213,880          | 245,321          | 280,662          |
| Financial assets at FVTPL                  | 10,573           | 27,963           | 14,903           | 15,648           | 16,431           | 17,252           |
| Other current assets                       | 106,676          | 152,026          | 9,767            | 994              | 9,825            | 1,032            |
| <b>Non-current assets</b>                  | <b>1,127,552</b> | <b>1,012,142</b> | <b>1,058,800</b> | <b>1,118,688</b> | <b>1,187,604</b> | <b>1,238,993</b> |
| PP&E                                       | 61,914           | 53,978           | 53,232           | 73,234           | 88,429           | 100,210          |
| Deferred income tax                        | 26,068           | 29,882           | 29,017           | 24,992           | 33,249           | 28,952           |
| Investment in JVs & assos                  | 323,188          | 252,715          | 261,665          | 273,109          | 284,919          | 297,084          |
| Intangibles                                | 171,376          | 161,802          | 177,727          | 206,169          | 232,098          | 255,565          |
| Financial assets at FVTPL                  | 192,184          | 206,085          | 211,145          | 211,145          | 211,145          | 211,145          |
| Other non-current assets                   | 352,822          | 307,680          | 326,014          | 330,039          | 337,765          | 346,037          |
| <b>Total assets</b>                        | <b>1,612,364</b> | <b>1,578,131</b> | <b>1,577,246</b> | <b>1,635,859</b> | <b>1,851,086</b> | <b>2,085,553</b> |
| <b>Current liabilities</b>                 | <b>403,098</b>   | <b>434,204</b>   | <b>352,157</b>   | <b>318,103</b>   | <b>341,632</b>   | <b>367,548</b>   |
| Short-term borrowings                      | 19,003           | 22,026           | 55,698           | 16,472           | 17,628           | 18,604           |
| Account payables                           | 109,470          | 92,381           | 100,948          | 94,076           | 99,675           | 108,495          |
| Tax payable                                | 12,506           | 13,488           | 17,664           | 13,208           | 13,853           | 14,327           |
| Other current liabilities                  | 256,673          | 299,955          | 171,693          | 188,193          | 204,322          | 219,967          |
| Lease liabilities                          | 5,446            | 6,354            | 6,154            | 6,154            | 6,154            | 6,154            |
| <b>Non-current liabilities</b>             | <b>332,573</b>   | <b>361,067</b>   | <b>351,408</b>   | <b>370,851</b>   | <b>382,517</b>   | <b>395,245</b>   |
| Long-term borrowings                       | 136,936          | 163,668          | 155,819          | 156,074          | 156,150          | 156,173          |
| Bond payables                              | 145,590          | 148,669          | 137,101          | 139,672          | 140,981          | 141,642          |
| Deferred income                            | 4,526            | 3,503            | 3,435            | 12,299           | 13,162           | 13,891           |
| Other non-current liabilities              | 45,521           | 45,227           | 55,053           | 62,807           | 72,223           | 83,539           |
| <b>Total liabilities</b>                   | <b>735,671</b>   | <b>795,271</b>   | <b>703,565</b>   | <b>688,955</b>   | <b>724,149</b>   | <b>762,793</b>   |
| Retained earnings                          | 669,911          | 705,981          | 813,911          | 975,913          | 1,152,426        | 1,344,416        |
| Other reserves                             | 136,388          | 15,410           | (5,320)          | (97,320)         | (97,320)         | (97,320)         |
| <b>Total shareholders equity</b>           | <b>806,299</b>   | <b>721,391</b>   | <b>808,591</b>   | <b>878,593</b>   | <b>1,055,106</b> | <b>1,247,096</b> |
| Minority interest                          | 70,394           | 61,469           | 65,090           | 68,311           | 71,831           | 75,663           |
| <b>Total equity and liabilities</b>        | <b>1,612,364</b> | <b>1,578,131</b> | <b>1,577,246</b> | <b>1,635,859</b> | <b>1,851,086</b> | <b>2,085,553</b> |

| <b>CASH FLOW</b>                                     | <b>2021A</b>     | <b>2022A</b>     | <b>2023A</b>     | <b>2024E</b>     | <b>2025E</b>     | <b>2026E</b>     |
|--|------------------|------------------|------------------|------------------|------------------|------------------|
| <b>YE 31 Dec (RMB mn)</b>                            |                  |                  |                  |                  |                  |                  |
| <b>Operating</b>                                     |                  |                  |                  |                  |                  |                  |
| Profit before taxation                               | 241,412          | 85,346           | 153,606          | 216,201          | 245,776          | 252,273          |
| Depreciation & amortization                          | 56,818           | 60,230           | 55,298           | 58,620           | 72,020           | 83,172           |
| Tax paid   | (20,252)         | (21,516)         | (43,276)         | (50,478)         | (55,145)         | (60,056)         |
| Change in working capital                            | (2,844)          | (28,405)         | 16,661           | 10,804           | 15,530           | 16,316           |
| Others   | (99,948)         | 50,437           | 39,673           | 14,550           | 5,799            | 21,441           |
| <b>Net cash from operations</b>                      | <b>175,186</b>   | <b>146,091</b>   | <b>221,962</b>   | <b>249,696</b>   | <b>283,979</b>   | <b>313,146</b>   |
| <b>Investing</b>                                     |                  |                  |                  |                  |                  |                  |
| Capital expenditure                                  | (34,931)         | (33,892)         | (36,477)         | (38,633)         | (40,827)         | (42,731)         |
| Acquisition of subsidiaries/ investments             | (117,642)        | 59,711           | (105,332)        | (31,313)         | (68,847)         | (43,511)         |
| Net proceeds from disposal of short-term investments | 0                | 0                | 0                | 0                | 0                | 0                |
| Others   | (25,976)         | (130,690)        | 16,648           | (68,431)         | (72,316)         | (75,689)         |
| <b>Net cash from investing</b>                       | <b>(178,549)</b> | <b>(104,871)</b> | <b>(125,161)</b> | <b>(138,378)</b> | <b>(181,990)</b> | <b>(161,931)</b> |
| <b>Financing</b>                                     |                  |                  |                  |                  |                  |                  |
| Net borrowings                                       | 45,239           | 31,982           | 30,834           | (33,102)         | 12,603           | 13,450           |
| Proceeds from share issues                           | 0                | 0                | 0                | 0                | 0                | 0                |
| Others   | (23,619)         | (91,935)         | (113,407)        | (98,186)         | (15,534)         | (17,107)         |
| <b>Net cash from financing</b>                       | <b>21,620</b>    | <b>(59,953)</b>  | <b>(82,573)</b>  | <b>(131,288)</b> | <b>(2,931)</b>   | <b>(3,657)</b>   |
| <b>Net change in cash</b>                            |                  |                  |                  |                  |                  |                  |
| Cash at the beginning of the year                    | 152,798          | 167,966          | 156,739          | 172,320          | 152,351          | 251,410          |
| Exchange difference                                  | (3,089)          | 7,506            | 1,353            | 0                | 0                | 0                |
| <b>Cash at the end of the year</b>                   | <b>167,966</b>   | <b>156,739</b>   | <b>172,320</b>   | <b>152,351</b>   | <b>251,410</b>   | <b>398,968</b>   |
| <b>GROWTH</b>  | <b>2021A</b>     | <b>2022A</b>     | <b>2023A</b>     | <b>2024E</b>     | <b>2025E</b>     | <b>2026E</b>     |
| <b>YE 31 Dec</b>                                     |                  |                  |                  |                  |                  |                  |
| Revenue  | 16.2%            | (1.0%)           | 9.8%             | 8.1%             | 7.8%             | 6.8%             |
| Gross profit   | 11.0%            | (2.9%)           | 22.8%            | 19.7%            | 8.5%             | 7.9%             |
| Operating profit                                     | 49.5%            | (58.2%)          | 44.4%            | 29.6%            | 10.6%            | 9.2%             |
| Net profit   | 42.7%            | (71.0%)          | 69.7%            | 51.2%            | 15.1%            | 0.7%             |
| Adj. net profit                                      | 0.9%             | (6.6%)           | 36.4%            | 36.1%            | 8.3%             | 8.2%             |
| <b>PROFITABILITY</b>                                 | <b>2021A</b>     | <b>2022A</b>     | <b>2023A</b>     | <b>2024E</b>     | <b>2025E</b>     | <b>2026E</b>     |
| <b>YE 31 Dec</b>                                     |                  |                  |                  |                  |                  |                  |
| Gross profit margin                                  | 43.9%            | 43.1%            | 48.1%            | 53.3%            | 53.6%            | 54.2%            |
| Operating margin                                     | 47.3%            | 20.0%            | 26.3%            | 31.5%            | 32.3%            | 33.1%            |
| Adj. net profit margin                               | 22.1%            | 20.9%            | 25.9%            | 32.6%            | 32.7%            | 33.2%            |
| Return on equity (ROE)                               | 28.9%            | 8.3%             | 14.1%            | 19.3%            | 19.4%            | 16.4%            |
| <b>GEARING/LIQUIDITY/ACTIVITIES</b>                  | <b>2021A</b>     | <b>2022A</b>     | <b>2023A</b>     | <b>2024E</b>     | <b>2025E</b>     | <b>2026E</b>     |
| <b>YE 31 Dec</b>                                     |                  |                  |                  |                  |                  |                  |
| Net debt to equity (x)                               | 0.2              | 0.2              | 0.2              | 0.2              | 0.1              | (0.1)            |
| Current ratio (x)                                    | 1.2              | 1.3              | 1.5              | 1.6              | 1.9              | 2.3              |
| Receivable turnover days                             | 32.1             | 29.9             | 27.9             | 28.0             | 27.2             | 26.4             |
| <b>VALUATION</b>                                     | <b>2021A</b>     | <b>2022A</b>     | <b>2023A</b>     | <b>2024E</b>     | <b>2025E</b>     | <b>2026E</b>     |
| <b>YE 31 Dec</b>                                     |                  |                  |                  |                  |                  |                  |
| P/E  | 15.0             | 51.8             | 30.3             | 19.7             | 17.1             | 17.0             |
| P/E (diluted)  | 15.3             | 52.6             | 30.8             | 20.0             | 17.4             | 17.3             |
| P/B  | 4.1              | 4.5              | 4.0              | 3.7              | 3.0              | 2.6              |

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



# Disclosures & Disclaimers

## Analyst Certification

The research analyst who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that analyst in this report. Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

## CMBIGM Ratings

**BUY** : Stock with potential return of over 15% over next 12 months  
**HOLD** : Stock with potential return of +15% to -10% over next 12 months  
**SELL** : Stock with potential loss of over 10% over next 12 months  
**NOT RATED** : Stock is not rated by CMBIGM

**OUTPERFORM** : Industry expected to outperform the relevant broad market benchmark over next 12 months  
**MARKET-PERFORM** : Industry expected to perform in-line with the relevant broad market benchmark over next 12 months  
**UNDERPERFORM** : Industry expected to underperform the relevant broad market benchmark over next 12 months

## CMB International Global Markets Limited

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

**CMB International Global Markets Limited ("CMBIGM") is a wholly owned subsidiary of CMB International Capital Corporation Limited (a wholly owned subsidiary of China Merchants Bank)**

## Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIGM does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIGM recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIGM, solely for the purpose of supplying information to the clients of CMBIGM or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIGM nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIGM has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIGM provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIGM may issue other publications having information and/ or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIGM may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIGM may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIGM does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIGM may have a conflict of interest that could affect the objectivity of this report and CMBIGM will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIGM. Additional information on recommended securities is available upon request.

For recipients of this document in the United Kingdom

This report has been provided only to persons (I) falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time) ("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.") of the Order, and may not be provided to any other person without the prior written consent of CMBIGM.

For recipients of this document in the United States

CMBIGM is not a registered broker-dealer in the United States. As a result, CMBIGM is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. The research analyst who is primary responsible for the content of this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA"). The analyst is not subject to applicable restrictions under FINRA Rules intended to ensure that the analyst is not affected by potential conflicts of interest that could bear upon the reliability of the research report. This report is intended for distribution in the United States solely to "major US institutional investors", as defined in Rule 15a-6 under the US, Securities Exchange Act of 1934, as amended, and may not be furnished to any other person in the United States. Each major US institutional investor that receives a copy of this report by its acceptance hereof represents and agrees that it shall not distribute or provide this report to any other person. Any U.S. recipient of this report wishing to effect any transaction to buy or sell securities based on the information provided in this report should do so only through a U.S.-registered broker-dealer.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBISG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBISG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBISG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBISG at +65 6350 4400 for matters arising from, or in connection with the report.