NetEase (NTES US)

3Q26 review: games revenue missed on high base; margin expansion continues

BUY (Maintain)

Target Price	**US$155.00**
(Previous TP	US$159.50)
Up/Downside	**47.7%**
Current Price	**US$104.94**

NetEase announced 3Q26 financial results: total revenue declined by 2% YoY to RMB27.9bn, 8% below Visible Alpha (VA) consensus estimate mainly due to the soft games business; operating income increased by 18% YoY to RMB9.4bn driven by GPM expansion and opex control, but still 13% below consensus estimate as a result of top-line underperformance. Due to a lack of new games and high-base effect, we expect total revenue may continue to face pressure in 4Q26E. We trim FY26-28E total revenue forecasts by 4%-6%. We roll over our valuation window to FY27 and lower our SOTP-derived target price to US$155.0 (previous: US$159.5). That said, we expect games revenue growth to reaccelerate from 1Q27E onwards, supported by the launch of highly-anticipated new game *ANANTA.* The company's current valuation also offers attractive risk-reward at 11x FY27E non-GAAP PE. Maintain BUY.

- **Games revenue declined on high base.** Games & related VAS revenue decreased by 2% YoY to RMB22.9bn in 3Q26, 9% below consensus estimate mainly due to high-base effect and a lack of new games. Management also notes the short drama may compete for user attention and time spend in the short term. Contract liabilities growth slowed down to +4% YoY in 3Q26 (vs. +14% YoY in 2Q26). By products: 1) *Where Winds Meet* surpassed 100mn players globally in Aug 2026, further strengthening the company's global presence; 2) *Onmyoji* MAUs reached their highest level since 2022 during its tenth anniversary in September; 3) *Infinite Borders* also achieved a historical high DAUs since its launch in 2015. Looking ahead, we expect the high-base effect to persist in 4Q26E. All eyes are now on the global launch of ANANTA (无限大) in Jan 2027, which will be the key driver of the games revenue rebound in 1Q27E and FY27, in our view. Other key games in the pipeline include Beneath the Mist (雾海之下), Tamas: Shadowveil (诡影藏锋) and Blood Message (归唐).
- **Music and Youdao businesses under pressure.** NetEase Cloud Music revenue declined by 1% YoY to RMB1.9bn in 3Q26 due to intensive competition and adjustment of social entertainment business. Youdao revenue was down by 12% YoY to RMB1.4bn in 3Q26, primarily attributable to the decline in revenue from online marketing services and smart devices. Innovative businesses and others revenue was up by 7% YoY to RMB1.5bn in 3Q26, thanks to the low base in 3Q25.
- **Improving margin despite revenue decline.** Overall GPM expanded by 4.3ppts YoY to 68.4% in 3Q26, driven by channel cost optimization. Overall OPM also increased by 5.6ppts YoY to 33.8% in 3Q26, thanks to the GPM expansion and opex control. Total opex declined by 5% YoY to RMB9.6bn in 3Q26, equivalent to 35% of total revenue (3Q25: 36%). We remain upbeat on YoY OP growth and margin expansion in 4Q26E, although it takes more time for revenue growth to reaccelerate.

Earnings Summary

(YE 31 Dec)	FY24A	FY25A	FY26E	FY27E	FY28E
Revenue (RMB mn)	105,295	112,626	115,669	123,472	131,840
Gross margin (%)	62.5	64.3	69.1	69.4	69.7
Adjusted net profit (RMB mn)	33,510.6	37,343.7	37,336.3	43,044.5	47,247.4
EPS (Adjusted) (RMB)	52.35	58.83	57.90	66.75	73.27
Consensus EPS (RMB)	52.35	58.83	60.61	70.61	76.41
P/E (x)	15.1	13.2	13.0	11.2	10.2

Source: Company data, Bloomberg, CMBIGM estimates

China Internet

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

Wentao LU, CFA
luwentao@cmbi.com.hk

Ye TAO, CFA
(852) 3850 5226
franktao@cmbi.com.hk

Shuyin GUO
(852) 3916 3716
guoshuyin@cmbi.com.hk

Stock Data

Mkt Cap (US$ mn)	67,182.3
Avg 3 mths t/o (US$ mn)	50.5
52w High/Low (US$)	147.56/104.94
Total Issued Shares (mn)	640.2

Source: FactSet

Shareholding Structure

William Lei Ding	45.5%

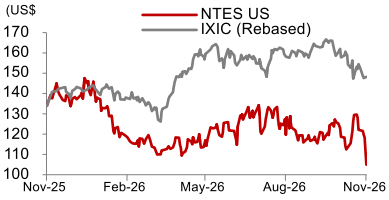
Source: Company data

Share Performance

	Absolute	Relative
1-mth	-16.1%	-9.3%
3-mth	-12.4%	-6.5%
6-mth	-10.2%	-3.4%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: NetEase: earnings revision

	Current			Previous			Change (%)		
RMB bn	FY26E	FY27E	FY28E	FY26E	FY27E	FY28E	FY26E	FY27E	FY28E
Revenue	115.7	123.5	131.8	120.8	130.1	138.8	-4.2%	-5.1%	-5.0%
Gross profit	80.0	85.7	91.9	83.5	90.1	96.6	-4.2%	-4.9%	-4.9%
Operating profit	43.5	47.6	51.8	45.9	49.5	53.5	-5.2%	-3.9%	-3.0%
Adjusted net profit	37.3	43.0	47.2	39.3	45.5	49.3	-5.0%	-5.4%	-4.2%
Adjusted EPS (RMB)	57.9	66.7	73.3	60.6	70.6	76.4	-4.5%	-5.5%	-4.1%
Gross margin	69.1%	69.4%	69.7%	69.1%	69.3%	69.5%	0.0 ppt	0.1 ppt	0.1 ppt
Operating margin	37.6%	38.5%	39.3%	38.0%	38.1%	38.5%	-0.4 ppt	0.5 ppt	0.8 ppt
Adjusted net margin	32.3%	34.9%	35.8%	32.5%	35.0%	35.5%	-0.3 ppt	-0.1 ppt	0.3 ppt

Source: CMBIGM estimates
Note: we lower FY26E adjusted net profit forecast mainly to reflect investment loss of RMB2.95bn in 2Q26.

Figure 2: CMBIGM estimates vs consensus

	CMBIGM			Consensus			Diff (%)		
RMB bn	FY26E	FY27E	FY28E	FY26E	FY27E	FY28E	FY26E	FY27E	FY28E
Revenue	115.7	123.5	131.8	120.8	130.1	138.8	-4.2%	-5.1%	-5.0%
Gross profit	80.0	85.7	91.9	83.5	90.1	96.6	-4.2%	-4.9%	-4.9%
Operating profit	43.5	47.6	51.8	45.9	49.5	53.5	-5.2%	-3.9%	-3.0%
Adjusted net profit	37.3	43.0	47.2	39.3	45.5	49.3	-5.0%	-5.4%	-4.2%
Adjusted EPS (RMB)	57.9	66.7	73.3	60.6	70.6	76.4	-4.5%	-5.5%	-4.1%
Gross margin	69.1%	69.4%	69.7%	69.1%	69.3%	69.5%	0.0 ppt	0.1 ppt	0.1 ppt
Operating margin	37.6%	38.5%	39.3%	38.0%	38.1%	38.5%	-0.4 ppt	0.5 ppt	0.8 ppt
Adjusted net margin	32.3%	34.9%	35.8%	32.5%	35.0%	35.5%	-0.3 ppt	-0.1 ppt	0.3 ppt

Source: Bloomberg, CMBIGM estimates

Figure 3: NetEase: key financial data forecasts

(RMB mn)	1Q25	2Q25	3Q25	4Q25	1Q26	2Q26	3Q26	Cons.	Diff%
Online games revenue	24,048	22,806	23,328	21,967	25,713	25,023	22,937	25,147	-8.8%
YoY%	12.1%	13.7%	11.8%	3.4%	6.9%	9.7%	-1.7%		
As % of total revenue	83.4%	81.8%	82.3%	79.7%	84.1%	83.1%	82.4%		
Youdao revenue	1,298	1,418	1,629	1,565	1,348	1,467	1,429	1,699	-15.9%
YoY%	-6.7%	7.2%	3.6%	16.8%	3.8%	3.5%	-12.3%		
As % of total revenue	4.5%	5.1%	5.7%	5.7%	4.4%	4.9%	5.1%		
Cloud Music revenue	1,858	1,969	1,964	1,968	1,981	1,977	1,946	2,013	-3.3%
YoY%	-8.4%	-3.5%	-1.8%	4.7%	6.6%	0.4%	-0.9%		
As % of total revenue	6.4%	7.1%	6.9%	7.1%	6.5%	6.6%	7.0%		
Innovative businesses	1,624	1,699	1,439	2,047	1,549	1,639	1,540	1,414	8.9%
YoY%	-17.6%	-17.8%	-18.9%	-10.4%	-4.6%	-3.5%	7.1%		
As % of total revenue	5.6%	6.1%	5.1%	7.4%	5.1%	5.4%	5.5%		
Total revenue	**28,829**	**27,892**	**28,359**	**27,547**	**30,591**	**30,107**	**27,852**	**30,344**	**-8.2%**
YoY%	7.4%	9.4%	8.2%	3.0%	6.1%	7.9%	-1.8%		
Gross profit margin (%)	**64.1%**	**64.7%**	**64.1%**	**64.2%**	**69.4%**	**70.5%**	**68.4%**	**68.9%**	**-0.5ppt**
Operating profit	**10,441**	**9,061**	**8,013**	**8,319**	**12,657**	**12,089**	**9,428**	**10,789**	**-12.6%**
YoY%	37.0%	29.6%	12.1%	6.4%	21.2%	33.4%	17.7%		
OPM (%)	36.2%	32.5%	28.3%	30.2%	41.4%	40.2%	33.8%		

Source: Company data, CMBIGM

We use sum-of-the-parts (SOTP) valuation methodology to value NetEase's four main business segments. Our SOTP-derived target price is US$155.0, comprising:

1) US$134.4 for the online game business (86.7% of total valuation), based on 14x 2027E EV/EBIT, on par with the industry average;

2) US$0.3 for Youdao (0.2% of total valuation), based on 0.4x 2027E EV/revenue, on par with the industry average;

3) US$2.7 (1.8% of total valuation) for the NetEase Cloud Music business, based on 2.4x 2027E EV/revenue, on par with the industry average;

4) US$0.6 (0.4% of total valuation) for the innovative businesses and others, based on 0.4x 2027E EV/revenue, on par with the industry average;

5) US$17.0 for net cash.

Figure 4: NetEase: SOTP Valuation

(RMBmn)	Valuation basis	Multiple (x)	2027E sales	2027E EBIT	Valuation	Shareholding (%)	Valuation to NetEase	Valuation per ADS (US$)
Online games	EV/EBIT	14.0	102,934	41,173	576,429	100.0%	576,429	134.4
Youdao	EV/revenue	0.4	5,361		2,144	57.1%	1,224	0.3
Cloud Music	EV/revenue	2.4	8,270		19,847	59.4%	11,789	2.7
Innovative businesses	EV/revenue	0.4	6,908		2,763	100.0%	2,763	0.6
Enterprise value							**592,205**	
Net cash							72,851	17.0
Equity value							**665,057**	
RMB/US$							6.7	
Valuation (US$mn)							**99,262**	
No. of ADSs (mn)							640	
Value per ADS (US$)							**155.0**	

Source: Company data, CMBIGM estimates

Figure 5: Peer comparison: online games

		Price	EBIT growth (YoY %)		EV/EBIT (x)	
Company	Ticker	(Local)	FY27E	FY28E	FY27E	FY28E
Tencent	700 HK	372.8	-4%	12%	12.4	11.1
Nintendo	7974 JP	9,002.0	13%	20%	20.9	17.5
Bandai Namco	7832 JP	7,149.0	9%	7%	16.0	15.0
Perfect World	002624 CH	9.8	96%	28%	8.9	7.0
37 Interactive	002555 CH	14.8	62%	11%	9.2	8.2
Average EV/EBIT					**13.5**	**11.7**

Source: Visible Alpha, CMBIGM
Note: data as of market close on 18 Nov

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

		Price	Revenue growth (YoY %)		EV/revenue (x)	
Company	Ticker	(Local)	FY27E	FY28E	FY27E	FY28E
Education						
New Oriental	EDU US	53.0	12%	10%	0.5	0.5
TAL Education	TAL US	10.2	14%	12%	0.6	0.5
Gaotu	GOTU US	2.4	13%	10%	0.1	0.1
Average					**0.4**	**0.4**
Community						
TME	TME US	9.4	7%	6%	1.9	1.8
Spotify	SPOT US	605.8	15%	13%	4.7	4.2
BiliBili	BILI US	11.4	10%	8%	0.4	0.4
Kuaishou	1024 HK	24.0	4%	6%	0.6	0.6

		Price	Revenue growth (YoY %)		EV/revenue (x)	
Average					**2.4**	**2.1**
E-commerce						
Alibaba	BABA US	84.4	13%	14%	1.0	0.9
JD	JD US	24.9	13%	5%	0.1	0.1
Pinduoduo	PDD US	77.5	10%	9%	0.4	0.4
Vipshop	VIPS US	12.8	1%	1%	0.1	0.1
Average					**0.4**	**0.4**

Source: Visible Alpha, CMBIGM
Note: data as of market close on 18 Nov

Risks

Decline in revenue of legacy titles; delay in new game launch; tightening regulations.

Financial Summary

INCOME STATEMENT	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec (RMB mn)						
Revenue	**103,468**	**105,295**	**112,626**	**115,669**	**123,472**	**131,840**
Cost of goods sold	(40,405)	(39,488)	(40,224)	(35,693)	(37,734)	(39,990)
Gross profit	**63,063**	**65,807**	**72,402**	**79,976**	**85,738**	**91,850**
Operating expenses	**(35,354)**	**(36,223)**	**(36,567)**	**(36,436)**	**(38,153)**	**(40,013)**
Selling expense	(13,969)	(14,148)	(14,620)	(14,806)	(16,051)	(17,139)
Admin expense	(4,900)	(4,551)	(4,228)	(3,123)	(3,087)	(3,098)
R&D expense	(16,485)	(17,525)	(17,719)	(18,507)	(19,015)	(19,776)
Operating profit	**27,709**	**29,584**	**35,835**	**43,541**	**47,585**	**51,837**
Investment gain/loss	1,307	355	732	(2,628)	(2,103)	(631)
Other gains/(losses)	1,054	602	1,087	513	0	0
Interest income	4,120	4,921	3,953	3,603	3,096	2,232
Foreign exchange gain/loss	(133)	255	(776)	(1,340)	0	0
Pre-tax profit	**34,057**	**35,718**	**40,830**	**43,689**	**48,578**	**53,439**
Income tax	(4,700)	(5,461)	(6,033)	(8,738)	(8,744)	(9,619)
After tax profit	**29,357**	**30,256**	**34,798**	**34,951**	**39,834**	**43,820**
Minority interest	59	(559)	(1,038)	(622)	0	0
Net profit	**29,417**	**29,698**	**33,760**	**34,329**	**39,834**	**43,820**
Adjusted net profit	**32,608**	**33,511**	**37,344**	**37,336**	**43,045**	**47,247**

BALANCE SHEET	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec (RMB mn)						
Current assets	**142,693**	**153,325**	**180,615**	**209,636**	**242,424**	**276,897**
Cash & equivalents	21,429	51,383	47,168	65,778	84,502	103,348
Restricted cash	2,777	3,086	4,319	4,319	4,319	4,319
Account receivables	6,422	5,669	5,338	5,372	5,620	5,881
Inventories	695	572	689	612	647	685
Prepayment	6,077	6,417	7,658	7,708	8,063	8,438
ST bank deposits	100,856	75,441	92,639	101,903	114,132	127,828
Other current assets	4,436	10,756	22,804	23,944	25,141	26,398
Non-current assets	**43,232**	**42,667**	**40,800**	**37,843**	**35,393**	**33,290**
PP&E	8,075	8,520	8,425	8,332	8,239	8,147
Other non-current assets	35,157	34,147	32,374	29,512	27,154	25,143
Total assets	**185,925**	**195,992**	**221,415**	**247,479**	**277,817**	**310,187**
Current liabilities	**53,842**	**49,668**	**52,369**	**55,243**	**58,648**	**61,275**
Short-term borrowings	19,240	11,805	6,384	11,032	11,651	11,255
Account payables	881	721	643	571	603	639
Tax payable	2,572	2,759	3,874	3,979	4,247	4,535
Other current liabilities	18,219	19,982	25,404	25,408	27,077	28,876
Accrued expenses	12,930	14,401	16,063	14,253	15,069	15,969
Non-current liabilities	**3,998**	**3,830**	**3,942**	**3,866**	**4,115**	**4,384**
Other non-current liabilities	3,998	3,830	3,942	3,866	4,115	4,384
Total liabilities	**57,841**	**53,497**	**56,311**	**59,110**	**62,763**	**65,659**
Total shareholders equity	**124,286**	**138,686**	**160,296**	**182,940**	**209,624**	**239,097**
Minority interest	3,798	3,809	4,808	5,430	5,430	5,430
Total equity and liabilities	**185,925**	**195,992**	**221,415**	**247,479**	**277,817**	**310,187**

CASH FLOW	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	**34,057**	**35,718**	**40,830**	**43,689**	**48,578**	**53,439**
Depreciation & amortization	3,055	2,418	2,247	4,213	4,166	4,119
Tax paid	(4,700)	(5,461)	(6,033)	(8,738)	(8,744)	(9,619)
Change in working capital	376	3,652	8,721	(1,780)	2,148	2,349
Others	2,543	3,351	4,973	0	0	0
Net cash from operations	**35,331**	**39,677**	**50,740**	**37,384**	**46,148**	**50,288**
Investing						
Capital expenditure	(4,266)	(2,192)	(2,007)	(3,998)	(3,955)	(3,914)
Net cash from investing	**(17,043)**	**17,916**	**(33,181)**	**(11,740)**	**(14,892)**	**(16,701)**
Financing						
Dividend paid	(8,014)	(11,165)	(13,826)	(10,485)	(11,950)	(13,146)
Net borrowings	(8,305)	(7,476)	(5,799)	4,648	619	(396)
Proceeds from share issues	0	0	0	0	0	0
Others	(5,148)	(8,694)	(536)	(1,200)	(1,200)	(1,200)
Net cash from financing	**(21,467)**	**(27,336)**	**(20,160)**	**(7,037)**	**(12,532)**	**(14,742)**
Net change in cash						
Cash at the beginning of the year	24,889	21,429	51,383	47,168	65,778	84,502
Exchange difference	(202)	11	(382)	0	0	0
Others	(78)	(314)	(1,232)	4	0	0
Cash at the end of the year	**21,429**	**51,383**	**47,168**	**65,778**	**84,502**	**103,348**

GROWTH	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
Revenue	7.2%	1.8%	7.0%	2.7%	6.7%	6.8%
Gross profit	19.5%	4.4%	10.0%	10.5%	7.2%	7.1%
Operating profit	41.2%	6.8%	21.1%	21.5%	9.3%	8.9%
Net profit	49.2%	1.0%	13.7%	1.7%	16.0%	10.0%
Adj. net profit	43.0%	2.8%	11.4%	(0.0%)	15.3%	9.8%

PROFITABILITY	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
Gross profit margin	60.9%	62.5%	64.3%	69.1%	69.4%	69.7%
Operating margin	26.8%	28.1%	31.8%	37.6%	38.5%	39.3%
Adj. net profit margin	31.5%	31.8%	33.2%	32.3%	34.9%	35.8%
Return on equity (ROE)	25.7%	22.6%	22.6%	20.0%	20.3%	19.5%

GEARING/LIQUIDITY/ACTIVITIES	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
Net debt to equity (x)	(0.8)	(0.8)	(0.8)	(0.9)	(0.9)	(0.9)
Current ratio (x)	2.7	3.1	3.4	3.8	4.1	4.5
Receivable turnover days	22.7	19.7	17.3	17.0	16.6	16.3
Payable turnover days	8.0	6.7	5.8	5.8	5.8	5.8

VALUATION	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
P/E	15.3	15.1	13.2	13.0	11.2	10.2
P/E (diluted)	15.5	15.2	13.3	13.1	11.3	10.3
P/B	3.6	3.2	2.8	2.4	2.1	1.9

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

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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

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