

FriendTimes Inc. (6820 HK)

Eyes on strong <Tale of Empress>

We expect FriendTimes ("FT") to see a strong quarter in 1Q20E, benefiting from: 1) more MAU and time spent shift to online leisure for the epidemic outbreak; and 2) eye-catching performance of newly-launched *Tale of Empress* (<浮生为卿歌>). Given recent sector valuation rebound and FT's strong grossing of new titles, we lifted FT's TP from HK\$1.4 to HK\$2.0 (implying **10x/7x** FY19/20E P/E), with earnings forecast unchanged. Valuation is still attractive. Maintain BUY.

- **Mobile games to benefit from epidemic.** We expect game comps to benefit from the epidemic outbreak, with more time spent shift to online leisure & MAU in the CNY. Mobile games could directly benefit, while PC games not (less operation of internet café). Game sector saw price rebound in recent weeks, with valuation up to over 20x FY20E P/E.
- **Strong <Tale of Empress> to bring upside.** After launch on 31 Dec 2019, *Tale of Empress* (<浮生为卿歌>) delivered eye-catching performance. According to App Annie, *Tale of Empress* ranked Top20-50 in iOS grossing rank, and climbed to Top 15 on 9 Feb 2020 (Apple store rank). We estimate its monthly grossing at RMB40mn in Jan, and daily grossing up to over RMB2mn in Feb. We see high visibility for its daily grossing to continuously increase, if version update is executed well. The coronavirus epidemic might affect its R&D productivity in the short term for holiday extension, but S&M effort is not impacted. We believe FT will strategically invest in its key title in terms of user acquisition and content update in 1H20E. Coupled with healthy operation metrics of existing games (such as *Legend of Empress* (<熹妃传>), *Royal Chaos* (<熹妃 Q 传>), we expect FT to see a strong quarter in 1Q20E.
- **Potential new titles rollout ahead.** Apart from <Tale of Empress>, there are several new titles in 2020 pipeline (e.g. *Fate: The Loved Journey* (<此生无白>), most of which are female-oriented. For conservative estimates, we forecast insignificant revenue contribution from new titles except for *Tale of Empress* and *Yokai Kitchen* (<精灵食肆>). But we keep positive on its solid game pipeline and further grossing upside.
- **Maintain BUY.** Given recent game sector valuation rebound and eye-catching performance of key titles, we lifted our TP from HK\$1.4 to **HK\$2.0** (implying **10x/7x** FY19/20E P/E), still largely lower than industry average. More catalysts to come: 1) solid FY19E results; 2) rising *Tale of Empress* and launch of new titles; and 3) potential dividends.

Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue (RMB mn)	700	1,464	1,717	2,276	2,703
YoY change (%)	23%	109%	17%	33%	19%
Adj. net income (RMB mn)	118	337	404	558	670
Adj. EPS (RMB)	0.05	0.15	0.18	0.25	0.30
YoY growth (%)	45%	185%	20%	38%	20%
P/E (x)	18.6	8.0	6.6	4.8	4.0
P/S (x)	3.1	1.5	1.3	1.0	0.8
Yield (%)	0.0	0.0	0.0	0.0	0.0
ROE (%)	33%	59%	28%	28%	25%
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, CMBIS estimates

BUY (Maintain)

Target Price	HK\$2.0
(Previous TP)	HK\$1.4
Up/Downside	+44.0%
Current Price	HK\$1.39

China Internet Sector

Sophie Huang

(852) 3900 0889

sophiehuang@cmbi.com.hk

Stock Data

Mkt Cap (HK\$ mn)	3,088
Avg 3 mths t/o (HK\$ mn)	4.68
52w High/Low (HK\$)	1.55/0.75
Total Issued Shares (mn)	2,190

Source: Bloomberg

Shareholding Structure

Eternal Heart Holding	42.8%
Warm Sunshine	8.6%
Ling Long Holding	8.5%

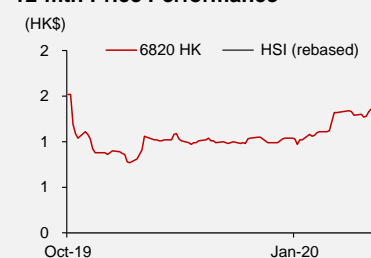
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	33.3%	39.0%
3-mth	29.5%	30.7%
6-mth	NA	NA

Source: Bloomberg

12-mth Price Performance

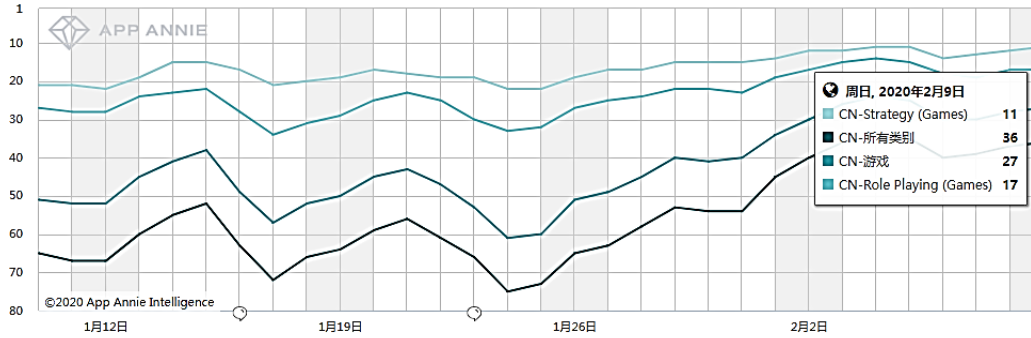


Source: Bloomberg

Auditor: KPMG

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Initiation: Surfing on the female-oriented games tailwind – 12 Dec 2019

Figure 1: Grossing rank of <Tale of Empress>

Source: App Annie

Figure 2: Valuation Table

Company	Ticker	Mkt.Cap (USD mn)	Rating	TP	Currency	Price	P/E			P/S			EV/EBITDA			FY19-21 EPS CAGR	FY19-21 PEG
							FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E		
Leaders																	
Tencent	700 HK	491,563	BUY	Under review	HKD	392	36.4	29.8	24.5	9.1	7.3	6.1	25.9	21.2	17.6	21%	1.43
Alibaba	BABA US	592,614	BUY	Under review	USD	220	30.2	24.6	19.6	8.0	6.2	5.0	24.7	19.6	15.5	21%	1.17
Baidu	BIDU US	46,140	BUY	157	USD	131	23.6	18.9	14.4	3.0	2.7	2.4	19.7	12.7	9.5	28%	0.68
JD	JD US	58,961	NR	NA	USD	40	39.4	29.0	21.3	0.7	0.6	0.5	26.9	19.2	14.7	35%	0.83
Meituan	3690 HK	76,060	NR	NA	HKD	102	317.1	77.1	35.6	5.6	4.2	3.3	101.7	47.5	25.4	203%	NA
Pinduoduo	PDD US	42,287	BUY	Under review	USD	36	NA	3384.4	42.8	9.6	5.8	4.3	NA	NA	161.5	NA	NA
NetEase	NTES US	44,387	NR	NA	USD	347	21.5	21.1	18.7	4.9	4.6	4.1	16.5	14.6	12.8	8%	2.63
Average							30.2	24.7	19.7	5.8	4.5	3.7	35.9	22.4	36.7	53%	1.35
Ecommerce																	
Alibaba	BABA US	592,614	BUY	Under review	USD	220	30.2	24.6	19.6	8.0	6.2	5.0	24.7	19.6	15.5	21%	1.17
JD	JD US	58,961	NR	NA	USD	40	39.4	29.0	21.3	0.7	0.6	0.5	26.9	19.2	14.7	35%	0.83
Pinduoduo	PDD US	42,287	BUY	Under review	USD	36	NA	3384.4	42.8	9.6	5.8	4.3	NA	NA	161.5	NA	NA
Vipshop	VIPS US	9,272	NR	NA	USD	14	14.7	11.7	10.8	0.7	0.7	0.6	10.7	8.3	7.7	16%	0.75
Babypree	1761 HK	348	NR	NA	HKD	2	NA	NA	208.0	4.9	4.1	3.2	NA	NA	NA	NA	NA
Average							28.1	21.8	23.6	4.8	3.5	2.7	20.8	15.7	49.8	24%	0.92
OTA																	
Ctrip	TCOM US	20,047	NR	NA	USD	34	25.5	22.1	17.6	3.9	3.5	3.0	25.5	21.5	16.2	22%	1.01
Tongcheng-elong	780 HK	3,072	BUY	17	HKD	11	13.8	12.2	9.5	2.9	2.4	2.0	8.8	6.7	5.2	24%	0.50
Tuniu	TOUR US	257	NR	NA	USD	2	NA	19.7	10.6	0.8	0.8	0.7	NA	NA	NA	NA	NA
Average							19.7	18.0	12.6	2.5	2.2	1.9	17.1	14.1	10.7	3%	0.75
Game																	
Tencent	700 HK	491,563	BUY	Under review	HKD	392	36.4	29.8	24.5	9.1	7.3	6.1	25.9	21.2	17.6	21%	1.43
NetEase	NTES US	44,387	NR	NA	USD	347	21.5	21.1	18.7	4.9	4.6	4.1	16.5	14.6	12.8	7%	3.16
Kingsoft	3888 HK	5,076	NR	NA	HKD	29	NA	95.2	55.8	4.5	3.4	2.6	201.8	44.1	26.1	NA	NA
Perfect World	002624 CH	10,248	BUY	Under review	CNY	50	37.3	29.8	26.1	8.5	7.1	6.3	29.5	24.4	21.5	15%	1.96
Sanqi Interactive	002555 CH	11,625	BUY	Under review	CNY	34	38.7	33.4	29.7	6.5	5.6	5.0	31.4	26.8	23.2	14%	2.33
Giant Interactive	002558 CH	5,455	NR	NA	CNY	19	33.9	28.7	26.9	9.1	8.1	7.3	NA	NA	NA	12%	2.33
Average							33.6	28.6	25.2	7.1	6.0	5.2	25.8	21.7	18.8	17%	2.24
Live streaming																	
MOMO	MOMO US	6,770	BUY	45	USD	32	11.6	9.8	8.5	2.8	2.4	2.1	9.7	6.9	5.7	19%	0.50
YY	YY US	5,180	BUY	82	USD	64	16.0	11.9	8.4	1.4	1.1	1.0	12.3	8.4	4.9	38%	0.32
Inke	3700 HK	321	NR	NA	HKD	1	5.3	2.8	2.8	NA	NA	NA	NA	NA	NA	38%	0.07
Huya	HUYA US	4,173	NR	NA	USD	19	42.1	24.9	16.8	3.5	2.6	2.1	45.2	18.7	12.0	65%	0.38
Average							18.7	12.3	9.1	2.6	2.0	1.7	22.4	11.3	7.5	39%	0.32
Entertainment																	
Tencent Music	TME US	22,631	NR	NA	USD	13.8	33.8	29.3	22.1	6.2	4.9	3.9	30.8	23.3	16.9	28%	1.06
iQiyi	IQ US	18,031	NR	NA	USD	24.8	NA	NA	NA	4.4	3.7	3.2	NA	NA	NA	-48%	NA
China Literature	772 HK	4,565	NR	NA	HKD	35.0	31.2	25.1	21.4	4.5	4.0	3.5	18.5	14.0	12.8	21%	1.22
Bilibili	BILI US	8,590	NR	NA	USD	26.3	NA	NA	315.8	8.9	6.0	4.5	NA	11402.8	59.5	NA	NA
Average							32.5	27.2	119.7	6.0	4.6	3.7	24.6	3813.4	29.7	0%	1.14
Ads																	
Baidu	BIDU US	46,140	BUY	157	USD	130.8	23.6	18.9	14.4	3.0	2.7	2.4	19.7	12.7	9.5	30%	0.63
Weibo	WB US	10,190	NR	NA	USD	45.3	16.6	16.2	14.0	5.7	5.4	4.8	14.2	13.4	11.6	10%	1.61
Sina	SINA US	2,815	NR	NA	USD	40.6	14.3	14.5	11.2	1.3	1.2	1.2	5.6	5.4	4.3	14%	1.07
Mobvista	1860 HK	745	BUY	5	HKD	3.6	17.3	10.6	7.4	1.3	1.1	0.9	17.0	8.9	6.1	46%	0.23
Duiba	1753 HK	536	BUY	6	HKD	3.6	15.4	7.3	5.1	2.0	1.4	1.0	12.8	4.0	2.7	232%	0.03
58.com	WUBA US	8,984	NR	NA	USD	60.1	15.2	17.8	16.0	4.0	3.5	3.1	16.2	14.0	11.6	0%	NA
Average							17.1	14.2	11.3	2.9	2.6	2.2	14.3	9.7	7.6	33%	0.71
Total Average							20.8	17.3	16.7	4.0	3.3	2.8	23.2	23.3	41.0	29.6%	1.08

Source: Bloomberg

Note: Data updated by 7 Feb 2020

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue	700	1,464	1,717	2,276	2,703
Games	699	1,464	1,717	2,276	2,703
Others	1	0	0	0	0
COGS	(268)	(546)	(623)	(799)	(943)
Gross profit	432	918	1,094	1,477	1,760
S&M	(190)	(422)	(486)	(660)	(784)
R&D	(89)	(136)	(168)	(205)	(243)
G&A	(17)	(32)	(34)	(46)	(49)
Other income	12	36	32	39	45
Operating profit	147	363	437	606	729
Finance costs	(0)	(1)	(4)	(7)	(10)
Other gains, net	(4)	(1)	(0)	(0)	(0)
Pre-tax Income	143	361	434	598	719
Income Tax	(25)	(25)	(30)	(41)	(49)
MI	(0)	0	-	-	-
Net profit	118	337	404	558	670
Adj. net profit	118	337	404	558	670

Cash flow summary

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Pre-tax Income	143	361	434	598	719
D&A	7	9	7	7	11
Change in WC	(18)	23	(118)	36	(15)
Others	(13)	(49)	(35)	(49)	(61)
Operating CF	120	344	288	592	654
Capex	(7)	(61)	(80)	(70)	(60)
Others	(9)	6	9	15	22
Investing CF	(16)	(55)	(71)	(55)	(38)
Equity raised	-	-	500	-	-
Change of debts	(12)	-	60	60	48
Others	(10)	(124)	(14)	(7)	(10)
Financing CF	(22)	(124)	546	53	38
Net change in cash	82	165	763	590	653
Cash (beg of yr)	226	305	473	1,236	1,826
FX	(2)	2	-	-	-
Cash (end of yr)	305	473	1,236	1,826	2,480

Balance sheet

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Non-current assets	42	113	186	249	298
Fixed asset	11	78	160	224	274
Right-of-use assets	14	13	4	3	3
Intangible assets	2	1	1	1	1
Others	16	20	20	20	20
Current assets	433	623	1,479	2,056	2,752
Cash	305	473	1,236	1,826	2,480
Trade receivables	115	132	223	205	243
Other current assets	12	18	20	25	29
Current liabilities	112	149	179	257	328
Bank loans	-	-	60	120	168
Trade and other payables	52	82	37	32	38
Lease liabilities	3	5	5	5	5
Other current liabilities	58	62	77	100	118
Non-current liabilities	7	14	18	23	27
Contract liabilities	2	11	15	20	24
Lease liabilities	5	2	2	2	2
Others	-	-	-	-	-
Total Equity	356	573	1,468	2,025	2,695

Key ratios

YE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Sales mix (%)					
Games	99.9	100.0	100.0	100.0	100.0
Others	0.1	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	100.0
Growth rate (%)					
Revenue	23.1	109.1	17.3	32.5	18.8
Gross profit	20.7	112.4	19.1	35.0	19.1
EBIT	53.8	146.6	20.3	38.5	20.4
Net profit	45.0	185.4	20.0	38.0	20.1
P&L ratios (%)					
Gross Margin	61.7	62.7	63.7	64.9	65.1
Pre-tax margin	20.5	24.7	25.3	26.3	26.6
Adj. net margin	16.8	23.0	23.5	24.5	24.8
Effective tax rate	17.7	6.8	6.8	6.8	6.8
Returns (%)					
ROE	33.2	58.7	27.5	27.5	24.9
ROA	24.8	45.7	24.3	24.2	22.0

Source: Company data, CMBIS estimates

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CMB International Securities Limited

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

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