

CMGE Technology (302 HK)

Moving into strong 2H21E pipeline

CMGE reported largely-in-line 1H21 results, with topline/ bottom line +27%/+18% YoY, -9%/0% against our estimates. Apart from robust performance of *The Voyage* <航海王:热血航线> and *Soul Land* <斗罗大陆:斗神再临> in China, CMGE achieved eye-catching growth in game development, IP licensing, and overseas biz. There are 15+ new titles to be launched in 2H21E, and we expect *Dynasty Warriors* and *New Sword and Fairy* to boost 2H21E momentum. We keep our forecast unchanged, with TP at HK\$6.2. Maintain BUY.

- 1H21 largely-in-line.** CMGE's 1H21 rev/ adj. net profit +27%/+18% YoY, -9%/0% against our estimates. By segment, game publishing/ development/ IP licensing revenue +2.4%/156.8%/2012.6% YoY, backed by successful new games (*The Voyage* with ByteDance and *Soul Land*) and existing portfolio (*Thunder Empire* and *Condor Heroes*). Overseas rev +6x YoY to RMB219.7mn with low base, primarily due to strong *Condor Heroes* in Asia.
- Moving into strong 2H21 pipeline.** There are 15+ new titles to be launched in 2H21E, and we expect *Dynasty Warriors* (真·三国无双 霸, launched on 5 Aug with Tencent) and *New Sword and Fairy* (仙剑奇侠传:挥剑问情, with ByteDance) to boost 2H21E momentum. *Dynasty Warriors* performed well, ranking Top 9 in iOS grossing rank in first week after launch. Other anticipated titles in 2H21E include *Sword and Fairy 7* (仙剑七, 15 Oct), *Thunder Empire 3*, *My Sword Diary* <我的御剑日记>, and *Rakshasa Street* <镇魂街>. Coupled with overseas rollout of *Condor Heroes*, *Hitman Reborn*, and *Sword and Fairy 7*, we believe CMGE rev/adj. net income will +10%/+16% in 2H21E. As minors in China only contributed 0.026% of CMGE's 1H21 rev, we believe risks of tightening game regulations are manageable.
- Focusing on game + IP development and collaboration.** CMGE acquired the remaining interest of Softstar and *Sword and Fairy* right in mainland China at HK\$642mn, doubling down on its IP-centric strategy. Apart from collaboration with Huawei and Bilibili (third-largest shareholder since Apr 2021), CMGE invested in four game developers in 2021, including its strategically self-developed game with *Sword and Fairy* IP (*Project: World*).
- Maintain BUY.** We keep our forecast unchanged, with TP at HK\$6.2 (implying 12x FY21E P/E). Maintain BUY. Further catalysts: 1) upcoming titles in 2H21E; 2) further cooperation with Bilibili.

Earnings Summary

| (YE 31 Dec) | FY19A | FY20A | FY21E | FY22E | FY23E |
|--------------------------|----------|----------|----------|----------|----------|
| Revenue (RMB mn) | 3,036 | 3,820 | 5,233 | 6,103 | 6,970 |
| YoY change (%) | 90% | 26% | 37% | 17% | 14% |
| Adj. net income (RMB mn) | 611 | 807 | 1,012 | 1,173 | 1,319 |
| Adj. EPS (RMB) | 0.32 | 0.35 | 0.43 | 0.50 | 0.57 |
| YoY growth (%) | NA | 7% | 25% | 16% | 12% |
| Consensus EPS (RMB) | NA | NA | 0.39 | 0.45 | 0.53 |
| P/E (x) | 9.3 | 8.7 | 6.9 | 6.0 | 5.3 |
| P/S (x) | 2.3 | 1.8 | 1.3 | 1.1 | 1.0 |
| Yield (%) | 1% | 3% | 3% | 3% | 3% |
| ROE (%) | 21.9 | 16.2 | 21.1 | 21.8 | 19.8 |
| Net gearing (%) | Net cash | Net cash | Net cash | Net cash | Net cash |

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

| | |
|---------------|----------|
| Target Price | HK\$6.2 |
| (Previous TP) | HK\$6.2) |
| Up/Downside | +72.2% |
| Current Price | HK\$3.61 |

China Internet Sector

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Stock Data

| | |
|--------------------------|------------|
| Mkt Cap (HK\$ mn) | 9,993 |
| Avg 3 mths t/o (HK\$ mn) | 125.00 |
| 52w High/Low (HK\$) | 5.09/ 2.59 |
| Total Issued Shares (mn) | 2,768 |
| Source: Bloomberg | |

Shareholding Structure

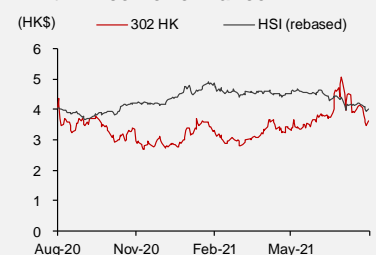
| | |
|---------------------------|-------|
| Fairview Ridge Investment | 25.0% |
| Pegasus Network | 10.6% |
| Hotel Zhike | 7.2% |
| Source: Bloomberg | |

Share Performance

| | Absolute | Relative |
|-------|----------|----------|
| 1-mth | -31.7% | -23.8% |
| 3-mth | 2.1% | 16.9% |
| 6-mth | 5.8% | 29.1% |

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Ernst & Young

Related Reports

- Strong pipeline & solid 1H21E ahead – 26 Jul 2021
- Eyes on three key titles in pipeline – 26 Mar 2021
- Looking into 2H20E strong pipeline – 14 Sep 2020

Figure 1: CMGE's 1H21 review

| RMB ('000), Dec-YE | 1H20 | 1H21 | YoY | CMBI estimate | Diff |
|-------------------------------------|--------------|--------------|------------|---------------|------------|
| Revenue | 1,714 | 2,180 | 27% | 2,400 | -9% |
| Cost of sales | (1,183) | (1,341) | NA | | |
| Gross profit | 531 | 840 | 58% | | |
| Sales and marketing expenses | (23) | (101) | NA | | |
| Research and development expenses | (80) | (124) | NA | | |
| General and administrative expenses | (167) | (184) | NA | | |
| Other income | 55 | 6 | -90% | | |
| Operating (loss)/profit | 317 | 436 | 38% | | |
| Finance costs | (21) | (11) | NA | | |
| Share of loss of an associate | 5 | (2) | NA | | |
| Profit before taxation | 301 | 423 | 40% | | |
| Income tax expense | (25) | (44) | NA | | |
| Profit for the year | 276 | 378 | 37% | | |
| Adjusted net profit | 342 | 402 | 18% | 403 | 0% |
| Margin Analysis | | | | | |
| Gross margin | 31% | 39% | | | |
| Operating margin | 18% | 20% | | | |
| Adj. net margin | 20% | 18% | | 17% | |

Growth Analysis

| | | | |
|------------------|--|-----|-----|
| Revenue | | 27% | 40% |
| Gross profit | | 58% | |
| Operating profit | | 38% | |
| Net profit | | 18% | 18% |

Source: Company data, CMBIS estimates

Figure 2: CMBIS estimates vs consensus

| RMB mn, Dec-YE | CMBIS | | | Consensus | | | Diff (%) | | |
|------------------|-------|-------|-------|-----------|-------|-------|----------|----------|----------|
| | FY21E | FY22E | FY23E | FY21E | FY22E | FY23E | FY21E | FY22E | FY23E |
| Revenue | 5,233 | 6,103 | 6,970 | 5,337 | 6,279 | 7,422 | -2.0% | -2.8% | -6.1% |
| Gross Profit | 1,798 | 2,093 | 2,388 | 1,790 | 2,109 | 2,538 | 0.4% | -0.7% | -5.9% |
| Operating Profit | 1,068 | 1,256 | 1,425 | 818 | 952 | 1,259 | 30.5% | 31.9% | 13.2% |
| Adj. net profit | 1,012 | 1,173 | 1,319 | 1,010 | 1,177 | 1,403 | 0.1% | -0.3% | -6.0% |
| Adj. EPS (RMB) | 0.43 | 0.50 | 0.57 | 0.39 | 0.45 | 0.53 | 12.4% | 12.5% | 6.5% |
| Gross Margin | 34.4% | 34.3% | 34.3% | 33.5% | 33.6% | 34.2% | +0.8ppts | +0.7ppts | +0.1ppts |
| Operating Margin | 20.4% | 20.6% | 20.4% | 15.3% | 15.2% | 17.0% | +5.1ppts | +5.4ppts | +3.5ppts |
| Adj. net margin | 19.3% | 19.2% | 18.9% | 18.9% | 18.7% | 18.9% | +0.4ppts | +0.5ppts | +0.0ppts |

Source: CMBIS estimates, Bloomberg

Financial Summary

Income statement

| YE 31 Dec (RMB mn) | FY19A | FY20A | FY21E | FY22E | FY23E |
|-------------------------|---------|---------|---------|---------|---------|
| Revenue | 3,036 | 3,820 | 5,233 | 6,103 | 6,970 |
| Game publishing | 2,553 | 2,978 | 4,382 | 5,094 | 5,786 |
| Game development | 421 | 730 | 773 | 924 | 1,090 |
| IP licensing | 62 | 112 | 78 | 86 | 95 |
| | - | - | - | - | - |
| COGS | (1,953) | (2,597) | (3,435) | (4,010) | (4,582) |
| Gross profit | 1,083 | 1,223 | 1,798 | 2,093 | 2,388 |
| S&M | (230) | (341) | (392) | (458) | (523) |
| R&D | (577) | (404) | (338) | (380) | (440) |
| Other expenses | (21) | (103) | - | - | 2 |
| Operating profit | 255 | 375 | 1,068 | 1,256 | 1,425 |
| Other income | 95 | 389 | 123 | 124 | 126 |
| Finance costs | (15) | (35) | - | - | - |
| Associates | 8 | (13) | - | - | - |
| Pre-tax Income | 344 | 717 | 1,190 | 1,380 | 1,552 |
| Income Tax | (100) | (27) | (179) | (207) | (233) |
| MI | (5) | (11) | - | - | - |
| Net profit | 248 | 701 | 1,012 | 1,173 | 1,319 |
| Adj. net profit | 611 | 807 | 1,012 | 1,173 | 1,319 |

Cash flow summary

| YE 31 Dec (RMB mn) | FY19A | FY20A | FY21E | FY22E | FY23E |
|---------------------------|---------|-------|-------|-------|-------|
| Pre-tax Income | 344 | 717 | 1,190 | 1,380 | 1,552 |
| D&A | 56 | 82 | 8 | 9 | - |
| Change in WC | (372) | (80) | 506 | (25) | (29) |
| Others | 284 | (96) | (197) | (227) | (255) |
| Operating CF | 310 | 624 | 1,507 | 1,137 | 1,268 |
| Capex | (35) | (30) | (30) | (30) | (30) |
| Others | (1,284) | (855) | 0 | 0 | 30 |
| Investing CF | (1,319) | (885) | (30) | (30) | - |
| Equity raised | 1,351 | 459 | - | - | - |
| Others | (724) | (391) | 1,026 | 1,107 | 1,268 |
| Financing CF | 626 | 69 | 1,026 | 1,107 | 1,268 |
| Net change in cash | 626 | 69 | 1,026 | 1,107 | 1,268 |
| Cash (beg of yr) | 144 | 771 | 795 | 1,821 | 2,928 |
| FX | 1 | (45) | - | - | - |
| Cash (end of yr) | 771 | 795 | 1,821 | 2,928 | 4,195 |

Balance sheet

| YE 31 Dec (RMB mn) | FY19A | FY20A | FY21E | FY22E | FY23E |
|--------------------------------|-------|-------|-------|-------|-------|
| Non-current assets | 2,627 | 3,321 | 3,100 | 3,159 | 3,216 |
| Fixed asset | 5 | 6 | (0) | (2) | (5) |
| Goodwill | 1,119 | 1,108 | 1,023 | 1,023 | 1,023 |
| Intangible assets | 155 | 155 | 159 | 182 | 204 |
| Others | 1,604 | 2,234 | 2,256 | 2,345 | 2,431 |
| Current assets | 2,581 | 3,010 | 2,522 | 3,746 | 5,132 |
| Cash | 771 | 795 | 1,821 | 2,928 | 4,195 |
| Trade receivables | 790 | 883 | 501 | 586 | 673 |
| Other current assets | 1,020 | 1,332 | 201 | 232 | 263 |
| Current liabilities | 1,284 | 1,464 | 789 | 881 | 970 |
| Bank loans | 442 | 451 | - | - | - |
| Trade and other payables | 687 | 841 | 632 | 724 | 813 |
| Tax payable | 117 | 138 | 138 | 138 | 138 |
| Other current liabilities | 37 | 34 | 19 | 19 | 19 |
| Non-current liabilities | 213 | 66 | 53 | 53 | 53 |
| Deferred tax liabilities | 32 | 53 | 53 | 53 | 53 |
| Contingent consideration | 163 | - | - | - | - |
| Others | 17 | 13 | - | - | - |
| Total Equity | 3,712 | 4,801 | 4,780 | 5,971 | 7,326 |

Key ratios

| YE 31 Dec | FY19A | FY20A | FY21E | FY22E | FY23E |
|---------------------------|--------|-------|--------|--------|--------|
| Sales mix (%) | | | | | |
| Game publishing | 84.1 | 77.9 | 83.7 | 83.5 | 83.0 |
| Game development | 13.9 | 19.1 | 14.8 | 15.1 | 15.6 |
| IP licensing | 2.0 | 2.9 | 1.5 | 1.4 | 1.4 |
| Total | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |
| Growth rate (%) | | | | | |
| Revenue | 90.2 | 25.8 | 37.0 | 16.6 | 14.2 |
| Gross profit | 103.4 | 12.9 | 47.0 | 16.4 | 14.1 |
| EBIT | 11.9 | 47.3 | 184.3 | 17.6 | 13.5 |
| Net profit | 82.1 | 32.1 | 25.4 | 16.0 | 12.4 |
| P&L ratios (%) | | | | | |
| Gross Margin | 35.7 | 32.0 | 34.4 | 34.3 | 34.3 |
| Pre-tax margin | 11.3 | 18.8 | 22.7 | 22.6 | 22.3 |
| Adj. net margin | 20.1 | 21.1 | 19.3 | 19.2 | 18.9 |
| Effective tax rate | (29.2) | (3.7) | (15.0) | (15.0) | (15.0) |
| Returns (%) | | | | | |
| ROE | 21.9 | 16.2 | 21.1 | 21.8 | 19.8 |
| ROA | 14.9 | 12.0 | 16.9 | 18.7 | 17.3 |

Source: Company data, CMBIS estimates

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