

TME (TME US)

Resilient subs to offset soft ads and social

TME's 1Q22 results were largely in line, with rev/adj net. profit -15%/-24% YoY (rev -1%/+3% vs. consensus/ our estimate, while bottom line 8%/4% above consensus/our estimate). Online music declined 5% YoY (vs. our estimate of -3% YoY), mainly on softer ads and sublicensing, while subscription was resilient (+18% YoY). Social entertainment continuously decreased 21% YoY (vs. our estimate of -25% YoY), amid the regulatory headwinds, soft macro, and increased competition. 2Q22E would be challenging (forecasting rev -20% YoY), given soft ads (lockdowns disruption) and livestreaming headwinds (tightening regulation in May). To reflect epidemic impact and softer social entertainment, we trimmed FY22-24E rev by 3.6-4.6% and cut earnings by 9%-11%. Maintain HOLD with lower TP of US\$4.6 (14.8x FY22E P/E).

- 1Q22 beat on margin.** 1Q22E topline -15% YoY, -1%/+3% vs. consensus, with weak ads and social offsetting by solid subs (+4mn net adds). Music/social -5%/-21% YoY in 1Q22E (vs. our estimates of -3%/-25%), with subs/non-subs +18%/-41% YoY. Adj. net profit came out at RMB939mn (-24% YoY), 8%/4% above our estimate, due to higher GPM (28%) and low-than-expected S&M expense offset by higher G&A.
- Challenging 2Q22E on epidemic and regulatory headwinds.** We remain positive on its subs momentum (rev +20% YoY in FY22E), in which ARPU to see sequential growth from 2Q22E while net adds turned moderate. However, 2Q22E would be a challenging quarter (forecasting rev -20% YoY), considering: 1) shrinking ads budget dragged by flash-screen ads and lockdown disruptions (especially for Eastern China), resulting in non-subs rev -40% YoY in 2Q22E (in our estimate); and 2) livestreaming to continuously decline (forecasting -30% YoY) with further tightening regulation in May. We expect ads to see gradual recovery with video ads initiatives in 2H22E, while livestreaming headwinds to linger in 2H22E.
- Efficient opex control to offset GPM downtrend.** We expect GPM of subs, LFA and livestreaming to improve in FY22E, given lower rev sharing and manageable incentives. But blended GPM would decline for revenue mix change (forecasting -2ppt YoY to 28% in FY22E). We expect adj. NPM at 13% (-1ppt YoY) in FY22E, with effective opex control.
- Maintain HOLD.** We trimmed FY22E-24E rev by 3.6-4.6%, and cut earnings by 9-11%, to reflect epidemic impact and livestreaming adjustment. Maintain HOLD with lower TP at US\$4.6 (14.8x FY22E P/E).

Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY 24E
Revenue (RMB mn)	29,153	31,244	26,933	27,915	29,201
YoY growth (%)	14.6	7.2	(14)	3.6	4.6
Adj. net income (RMB mn)	4,971	4,332	3,506	3,452	3,770
Adj. EPS (RMB)	3.0	2.6	2.1	2.1	2.2
YoY growth (%)	1.0	(13)	(19)	(2)	9.2
Consensus EPS (RMB)	NA	NA	2.2	2.4	2.7
P/E (x)	8.9	10.2	12.6	12.8	11.7
P/B (x)	1.5	1.4	1.6	1.6	1.5
Yield (%)	0.0	0.0	0.0	0.0	0.0
ROE (%)	9.4	7.4	5.7	5.3	5.5
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

HOLD (Maintain)

Target Price US\$4.6
(Previous TP) US\$5.0
Up/Downside +12.5%
Current Price US\$4.1

China Internet Sector

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Stock Data

Mkt Cap (US\$ mn)	6,950
Avg 3 mths t/o (US\$ mn)	89.37
52w High/Low (US\$)	16.53/ 2.95
Total Issued Shares (mn)	838
Source: Bloomberg	

Shareholding Structure

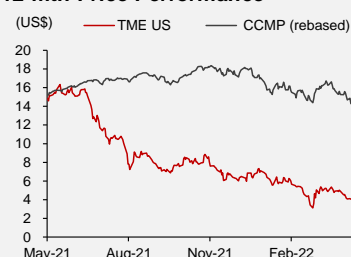
Baillie Gifford	5.98%
Canada Pension Plan	4.31%
Blackrock	3.56%
Source: Bloomberg	

Share Performance

	Absolute	Relative
1-mth	-16.5%	-5.6%
3-mth	-34.7%	-21.8%
6-mth	-51.2%	-34.5%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Ernst & Young

Related Reports

- Soft social entertainment on epidemic – 21 April 2022
- Challenges into 2022 – 23 Mar 2022
- Prudent on 4Q21E & FY22E topline growth – 10 Nov 2021

Figure 1: 1Q22 financial review

RMB mn, Dec-YE	4Q20	1Q21	2Q21	3Q21	4Q21	1Q22	QoQ	YoY	Consensus	Diff %	CMBI	Diff %
Revenue	8,335	7,824	8,008	7,805	7,607	6,644	-12.7%	-15.1%	6,690	-1%	6,456	3%
Gross Profit	2,697	2,466	2,437	2,309	2,192	1,860	-15.1%	-24.6%	1,841	1%	1,735	7%
Operating Profit	1,018	911	1,035	919	682	749	9.8%	-17.8%	722	4%	787	-5%
Adj. net profit	1,364	1,235	1,161	1,063	873	939	7.6%	-24.0%	872	8%	902	4%
Adj. EPS (RMB)	0.81	0.69	0.66	0.61	0.50	0.54	8.3%	-21.6%	0.52	6%	0.55	-1%
Margin (%)												
Gross margin	32.4%	31.5%	30.4%	29.6%	28.8%	28.0%			27.5%		26.9%	
Operating margin	12.2%	11.6%	12.9%	11.8%	9.0%	11.3%			10.8%		12.2%	
Adj. net margin	16.4%	15.8%	14.5%	13.6%	11.5%	14.1%			13.0%		14.0%	
Growth (%)												
Revenue (YoY)	14.3%	24.0%	15.5%	3.0%	-8.7%	-15.1%			-14.5%		-17.5%	
Revenue (QoQ)	10.0%	-6.1%	2.4%	-2.5%	-2.5%	-12.7%			-12.1%		-15.1%	
Operating Profit	-4.9%	11.8%	-6.5%	-10.4%	-33.0%	-17.8%			-20.7%		-13.6%	
Adj. net profit	1.8%	12.0%	0.5%	-21.2%	-36.0%	-24.0%			-29.4%		-27.0%	

Source: Company data, Bloomberg, CMBIGM estimates

Figure 2: 1Q22 revenue breakdown

RMB mn, Dec-YE	3Q20	4Q20	1Q21	2Q21	3Q21	4Q21	1Q22	QoQ	YoY
Total revenue	7,575	8,335	7,824	8,008	7,805	7,607	6,644	-13%	-15%
Online music service	2,324	2,760	2,749	2,950	2,888	2,880	2,616	-9%	-5%
Subscription	1,460	1,580	1,690	1,790	1,900	1,950	1,990	2%	18%
Others	864	1,180	1,059	1,160	988	930	626	-33%	-41%
Social entertainment / others	5,251	5,575	5,075	5,058	4,917	4,727	4,028	-15%	-21%

Source: Company data

Figure 3: CMBIGM estimates vs consensus

RMB mn, Dec-YE	CMBIGM			Consensus			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	26,933	27,915	29,201	29,221	31,430	33,635	-7.8%	-11.2%	-13.2%
Gross profit	7,507	7,468	7,758	8,620	9,538	10,319	-12.9%	-21.7%	-24.8%
Operating profit	3,017	3,193	3,255	3,182	3,765	4,282	-5.2%	-15.2%	-24.0%
Adj. net profit	3,506	3,452	3,770	3,954	4,299	4,756	-11.3%	-19.7%	-20.7%
EPS (RMB)	2.08	2.05	2.24	2.16	2.38	2.72	-3.7%	-13.8%	-17.6%
Gross margin	27.9%	26.8%	26.6%	29.5%	30.3%	30.7%	-1.6ppts	-3.6ppts	-4.1ppts
Operating margin	11.2%	11.4%	11.1%	10.9%	12.0%	12.7%	+0.3ppts	-0.5ppts	-1.6ppts
Net margin	13.0%	12.4%	12.9%	13.5%	13.7%	14.1%	-0.5ppts	-1.3ppts	-1.2ppts

Source: Company data, Bloomberg, CMBIGM estimates

Figure 4: Earnings revision

RMB mn, Dec-YE	CMBIGM			Consensus			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	26,933	27,915	29,201	27,943	29,206	30,619	-3.6%	-4.4%	-4.6%
Gross profit	7,507	7,468	7,758	8,110	8,168	8,556	-7.4%	-8.6%	-9.3%
Operating profit	3,017	3,193	3,255	3,404	3,630	3,746	-11.4%	-12.0%	-13.1%
Adj. net profit	3,506	3,452	3,770	3,862	3,850	4,222	-9.2%	-10.4%	-10.7%
EPS (RMB)	2.08	2.05	2.24	2.30	2.29	2.51	-9.2%	-10.4%	-10.7%
Gross margin	27.9%	26.8%	26.6%	29.0%	28.0%	27.9%	-1.1ppts	-1.2ppts	-1.4ppts
Operating margin	11.2%	11.4%	11.1%	12.2%	12.4%	12.2%	-1.0ppts	-1.0ppts	-1.1ppts
Net margin	13.0%	12.4%	12.9%	13.8%	13.2%	13.8%	-0.8ppts	-0.8ppts	-0.9ppts

Source: Company data, CMBIGM estimates

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Net revenues	29,153	31,244	26,933	27,915	29,201
Online music service	9,349	11,467	12,090	13,326	14,917
Subscription	5,561	7,330	8,816	9,753	10,978
Others	3,788	4,137	3,274	3,573	3,939
Social entertainment	19,804	19,777	14,843	14,589	14,284
COGS	(19,851)	(21,840)	(19,426)	(20,447)	(21,444)
Gross profit	9,302	9,404	7,507	7,468	7,758
S&M	(2,475)	(2,678)	(2,289)	(2,512)	(3,066)
R&D	(1,859)	(2,031)	(1,751)	(1,787)	(1,810)
Admin. Exp.	(1,242)	(1,978)	(1,697)	(1,396)	(1,460)
Operating profit	3,726	2,717	1,771	1,773	1,421
Other income, net	906	915	1,246	1,420	1,834
Pre-tax Income	4,632	3,632	3,017	3,193	3,255
Income Tax	(456)	(417)	(453)	(479)	(488)
Net profit	4,176	3,215	2,564	2,714	2,767
Adj. net profit	4,971	4,332	3,506	3,452	3,770

Cash flow summary

YE 31 Dec (RMB mn)	FY20E	FY21A	FY22E	FY23E	FY24E
Pre-tax Income	4,632	3,632	3,017	3,193	3,255
D&A	455	767	525	566	619
Change in WC	(314)	(1,228)	(284)	134	125
Others	(38)	2,068	560	268	1,514
Operating CF	4,734	5,239	3,818	4,162	5,513
Capex	(330)	(354)	(305)	(316)	(331)
Investments	6	0	0	0	-
Others	(13,882)	(2,087)	(1,702)	(1,635)	(1,653)
Investing CF	(14,206)	(2,441)	(2,007)	(1,951)	(1,983)
Equity raised	0	0	0	0	0
Change of debts	0	0	0	0	0
Others	5,292	(3,710)	0	0	0
Financing CF	5,292	(3,710)	0	0	0
Net change in cash	(4,029)	2,293	1,406	1,867	2,178
Cash (beg of yr)	15,426	11,128	6,591	7,997	9,864
FX	(269)	0	0	0	0
Cash (end of yr)	11,128	13,421	7,997	9,864	12,043

Balance sheet

YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Non-current assets	36,586	40,597	56,082	57,242	58,371
Intangible assets, net	2,020	1,511	1,373	1,209	1,020
Goodwill	17,492	19,640	20,890	22,140	23,390
Financial assets	9,771	9,771	9,771	9,771	9,771
Others	7,303	9,675	24,047	24,122	24,190
Current assets	31,687	34,472	28,200	30,262	32,695
Cash, restricted cash	11,128	13,421	7,997	9,864	12,043
Accounts receivable	2,800	3,338	2,878	2,983	3,120
Other current assets	2,846	2,727	2,351	2,437	2,549
Term deposits	14,858	14,858	14,858	14,858	14,858
Others	55	127	117	121	125
Current liabilities	9,602	10,400	9,131	9,491	9,911
Accounts payables	3,565	3,291	2,927	3,081	3,231
Other payables	3,881	3,749	3,232	3,350	3,504
Deferred revenue	1,608	2,812	2,424	2,512	2,628
Others	548	548	548	548	548
Non-current liabilities	5,940	5,940	5,940	5,940	5,940
Notes payable	5,175	5,175	5,175	5,175	5,175
Deferred tax liability	265	265	265	265	265
Others	500	500	500	500	500
MI	486	486	486	486	486
Total Equity	52,731	58,729	61,942	65,102	68,572
Shareholders' equity	52,245	58,243	61,456	64,616	68,086

Key ratios

YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Sales mix (%)					
Online music service	32.1	36.7	44.9	47.7	51.1
Subscription	19.1	23.5	32.7	34.9	37.6
Others	13.0	13.2	12.2	12.8	13.5
Social entertainment	67.9	63.3	55.1	52.3	48.9
Total	100.0	100.0	100.0	100.0	100.0
Growth rate (%)					
Revenue	14.6	7.2	(13.8)	3.6	4.6
Gross profit	7.3	1.1	(20.2)	(0.5)	3.9
EBIT	(5.2)	(27.1)	(34.8)	0.2	(19.9)
Adj. net profit	1.4	(12.9)	(19.1)	(1.5)	9.2
P&L ratios (%)					
Operating margin	12.8	8.7	6.6	6.4	4.9
Pre-tax margin	15.9	11.6	11.2	11.4	11.1
Adj. net margin	17.1	13.9	13.0	12.4	12.9
Effective tax rate	(9.8)	(11.5)	(15.0)	(15.0)	(15.0)
Returns (%)					
ROE	9.4	7.4	5.7	5.3	5.5
ROA	7.3	5.8	4.2	3.9	4.1
Per share					
EPS (RMB)	3.0	2.6	2.1	2.1	2.2
DPS (RMB)	2.0	3.0	4.0	5.0	6.0
BVPS (RMB)	20.3	22.3	25.1	26.0	27.1

Source: Company data, CMBIGM estimates

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