

# Tencent Holdings

## 4Q in line; Honor of Kings' strength portends to a promising 2017

### Results Preview

#### 4Q revenue in line; bottom line to miss

**Tencent will announce its 4Q16 results on March 22:** we expect revenue to be in line; but seasonality & larger contribution of payments weighed on adjusted net margin (26.3% vs. 29.4% a year ago) will make adjusted net income miss by 2% (+29% to Rmb11.5bn). However, the strength of *Honor of Kings* in 1Q17 will more than offset the weakness in ads and margin pressure.

#### Trends to watch

**Ads may not be satisfactory, despite 4Q's strong seasonality, this is pretty much priced in already.** We estimate brand ads +10% QoQ to Rmb3.4bn in 4Q16, helped by its news app, while video ads' growth remains weak; P4P ads +19% QoQ to Rmb5.2bn, on OAs, Moments, and Myapp. This makes full year ad revenue reach Rmb27.3bn. We expect ads +40% in 2017 to Rmb38.2bn, led by Moments, OAs, Tencent News, and potential new format of ad products.

**Mobile game growth supported by *Honor of Kings* and *Fantasy ZX* in 4Q16.** Tencent has 1/2/4 games ranked in the top 10 in October/November/December, and 4/4 in January/February 2017. *Honor of Kings*' grossing is still climbing 15 months after launch, setting a record high grossing of >Rmb2bn in January/February, according to our channel checks. As its PvP nature helps extend its lifecycle without heavy efforts, we expect it to continue to support Tencent's mobile game revenue in 2017, and to contribute nearly half of grossing in 1Q17. We now model a 5% QoQ increase in 4Q16 for mobile game revenue (to Rmb10.4bn), and 44% YoY growth in 2017.

#### Valuation and recommendation

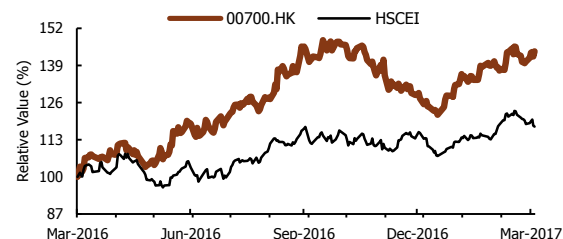
**The market is concerned over:** 1) weak ads; 2) potential suspension of Korean game launch in China; and, 3) margin pressure weighing on Tencent's share price for the last two months (+12% vs. sector average of +16%). We believe that: 1) is priced in; 2) has no impact on mobile DNF; and, 3) can largely be alleviated by the strength of *HoK*, which we believe has yet to be priced in, as the grossing may be even better than the data tracking company indicates. **Maintain BUY, but lift TP by 4% to HK\$240**, representing 35x/28x 2017/18 PER.

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### Maintain BUY

Ticker	00700.HK
CICC investment rating	BUY
Last close	HK\$212.40
CICC target	HK\$240.00
52wk price range	HK\$220.80~147.96
Market cap (bn)	HK\$2,013
Daily value (mn)	HK\$3,319.21
Shares outstanding (mn)	9,477
Free float (%)	100
Daily volume (mn sh)	15.80
Business sector	Internet



(Rmb mn)	2015A	2016E	2017E	2018E
Revenue	102,863	152,032	206,774	259,803
(+/-)	30.3%	47.8%	36.0%	25.6%
Net profit	28,806	40,772	50,732	65,310
(+/-)	21.0%	41.5%	24.4%	28.7%
Net profit (Non-GAAP)	32,261	44,635	57,349	73,624
(+/-)	33.2%	38.4%	28.5%	28.4%
EPS	3.05	4.29	5.34	6.88
EPS (Non-GAAP)	3.42	4.70	6.04	7.75
BPS	12.95	16.82	21.69	27.95
SPS	10.91	16.01	21.78	27.36
Cash flow per share	4.82	2.71	9.69	10.74
P/E	58.3	44.3	35.6	28.4
P/E (Non-GAAP)	52.0	40.4	31.5	25.2
P/B	13.7	11.3	8.8	7.0
P/S	16.3	11.9	8.7	7.1
ROAA	13.5%	14.0%	15.3%	15.8%
ROAE	31.6%	31.7%	31.4%	31.2%

Source: Wind, Bloomberg, company data, CICC Research



## Financial summary

Financial statement (Rmb mn)	2015A	2016E	2017E	2018E
<b>Income statement</b>				
Net revenue	102,863	152,032	206,774	259,803
COGS	-41,631	-67,497	-99,584	-125,392
SG&A expenses	-24,818	-34,257	-47,179	-57,936
R&D expenses	N.A.	N.A.	N.A.	N.A.
Other operating expenses	0	0	0	0
Operating profit	15,809	22,009	21,104	28,931
Finance costs	-1,618	-2,131	-2,319	-3,897
Other income (expense)	-2,793	-2,500	-2,000	-1,600
Profit before income tax	11,398	17,378	16,785	23,434
Income tax	7,108	10,375	12,632	15,460
Net profit	28,806	40,772	50,732	65,310
Minority interest	302	488	600	600
Non-GAAP net profit	32,261	44,635	57,349	73,624
EBITDA	19,430	26,236	26,587	36,148
<b>Balance sheet</b>				
Cash and bank balances	98,169	113,726	190,101	272,481
Trade and bill receivables	7,061	14,065	14,668	19,528
Inventories	222	222	222	222
Other current assets	49,926	48,609	52,670	58,037
Total current assets	155,378	176,622	257,660	350,268
Fixed assets and CIP	9,973	13,449	18,443	24,390
Intangible assets	13,439	13,439	13,439	13,439
Total non-current assets	151,440	154,916	159,910	165,857
Total assets	306,818	331,539	417,571	516,125
Short-term borrowings	11,429	11,429	11,429	11,429
Trade and bill payables	15,700	16,910	24,949	32,534
Other current liabilities	97,277	83,169	114,984	146,455
Total current liabilities	124,406	111,507	151,361	190,418
Long-term borrowings	50,014	50,014	50,014	50,014
Total non-current liabilities	60,312	60,312	60,312	60,312
Total liabilities	184,718	171,819	211,673	250,730
Minority interests	0	0	0	0
Total shareholders' equity	122,100	159,719	205,897	265,395
Total liabilities & equity	306,818	331,539	417,571	516,125
<b>Cash flow statement</b>				
Pretax profit	36,216	51,635	63,964	81,370
Depreciation & amortization	3,621	4,227	5,483	7,217
Change in working capital	52,049	-33,274	23,627	16,987
Others	-46,455	3,115	-1,069	-3,617
Cash flow from operations	45,431	25,703	92,005	101,957
Capital expenditure	-5,212	-7,703	-10,477	-13,164
Others	-58,393	1,198	0	0
Cash flow from investing	-63,605	-6,505	-10,477	-13,164
Equity financing	0	0	0	0
Lend from bank	27,693	0	0	0
Others	-9,165	-3,641	-5,154	-6,412
Cash flow from financing	18,528	-3,641	-5,154	-6,412
Foreign exchange gain (loss)	371	0	0	0
Net changes in cash	354	15,557	76,374	82,380

Source: Company data, CICC Research

Financial ratios	2015A	2016E	2017E	2018E
<b>Growth ability</b>				
Revenue	30.3%	47.8%	36.0%	25.6%
Operating profit	84.0%	39.2%	-4.1%	37.1%
EBITDA	65.8%	35.0%	1.3%	36.0%
Net profit	21.0%	41.5%	24.4%	28.7%
Non-GAAP net profit	33.2%	38.4%	28.5%	28.4%
<b>Profitability</b>				
Gross margin	59.5%	55.6%	51.8%	51.7%
Operating margin	15.4%	14.5%	10.2%	11.1%
EBITDA margin	18.9%	17.3%	12.9%	13.9%
Net margin	28.0%	26.8%	24.5%	25.1%
Non-GAAP net margin	31.4%	29.4%	27.7%	28.3%
<b>Liquidity</b>				
Current ratio	1.25	1.58	1.70	1.84
Quick ratio	1.25	1.58	1.70	1.84
Cash ratio	0.79	1.02	1.26	1.43
Liabilities / assets	60.2%	51.8%	50.7%	48.6%
Net debt / equity	net cash	net cash	net cash	net cash
<b>Return</b>				
RoA	13.5%	14.0%	15.3%	15.8%
RoE	31.6%	31.7%	31.4%	31.2%
<b>Per-share data</b>				
EPS (Rmb)	3.05	4.29	5.34	6.88
EPS (Non-GAAP) (Rmb)	3.42	4.70	6.04	7.75
BPS (Rmb)	12.95	16.82	21.69	27.95
SPS (Rmb)	10.91	16.01	21.78	27.36
CPS (Rmb)	4.82	2.71	9.69	10.74
<b>Valuation</b>				
P/E	58.3	44.3	35.6	28.4
P/E (Non-GAAP)	52.0	40.4	31.5	25.2
P/B	13.7	11.3	8.8	7.0
EV/EBITDA	84.5	66.8	63.0	45.4
Dividend yield	0.2%	0.3%	0.4%	0.4%

## Company description

Tencent, incorporated in November, 1998, is one of the biggest internet companies in China by market cap. It mainly provides IM services, develops and operates online games, and provides other internet value-added services. Its platforms, QQ, Weixin and Qzone, comprise the largest internet community in China. It has leading market share in China's online games industry in both client-based and mobile games. Its portal, qq.com, is the biggest in China by traffic. Tencent has made a series of strategic investments, including JD.com, Dianping, Dididache, and 58.com. Its major revenue contributors include online games, advertising, and VIP services.



Figure 1: Tencent's client-based game pipeline

PC Titles pipeline		Developer	Genre	Remark
Title (English)	Title (Chinese)			
Three Kingdoms	霸三国	Tencent	RTS	Latest round of CBT to start on Aug 20, 2016
Master x Master	全职大师	Ncsoft	3D MOBA	CP closed beta test started on Jul 7, 2016
Metro Conflict: Presto	重火力	Redduck	FPS	2nd round of CBT finished on May 26, 2014
HON	超神英雄	S2 Games	3D MOBA	Latest round of CBT started from Nov 6, 2015
Orcs Must Die	兽人必须死	Robot Entertainment	3D TOBA	Latest round of CBT finished on Jun 23, 2016
Sura	天刹	NSE	3D next-generation high-end fighting MMOG	TBD;
Maple Story 2	冒险岛2	Nexon	3D cartoon style MMORPG	Latest round of CBT started on Mar 7, 2017
Rising Fire	火源计划	Yingpei Games	FPS	Latest round of CBT finished on Sep 28, 2016
Path of Exile	流放之路	Grinding Gear Games	3D ARPG	Latest round of CBT started on Oct 18, 2016
Need for Speed(online)	极品飞车Online	EA	Racing	Latest round of CBT to start on Mar 16, 2017
Transformers OL	变形金刚	Tencent	FPS	Latest round of CBT to start on Jan 12, 2017
Rage of the Gods	众神争霸	Tencent	MOBA	Latest round of CBT started from Mar 14, 2016
NX	飞行战机	TOPPIG	Action	TBD
Lost Ark	失落的方舟	Smilegate	MMORPG	Latest round of CBT started on Aug 24, 2016 in Korea
Project Mercury	水星计划	Sonov	FPS	TBD
Master of Meteor Blades	新流星搜剑录	Kong Zhong	MOFA	Latest round of CBT started on Dec 1, 2016
Mountain Romance	灵山奇缘	Tencent	TBS	First round of CBT started on Dec 15, 2016
Paladins	枪火游侠	Hi-Rez Studios	FPS	Latest round of CBT started on Dec 15, 2016
Epic Paragon	虚幻争霸	Epic Games	MOBA	TBD
Shadow Tracker	猎影计划	Tencent	VR FPS	TBD

Source: Company disclosure, CICC Research

Figure 2: Tencent's mobile game pipeline

Title - English	Title -Chinese	Genre	Licensed/In-house developed	Remark
Stone Age	石器时代	MMORPG	Licensed	First round of Android CBT to start on Mar 15, 2017
DnF Mobile	地下城与勇士	Action	Licensed	TBD
Contra Mobile	魂斗罗	Shooting	Licensed	Latest round of CBT started on Nov 8th, 2016
Legacy TLBB 3D	天龙八部经典版	MMORPG	Licensed	Latest round of CBT started on Mar 7, 2017
The Legend of Sword and Fairy Mobile	仙剑奇侠传OL	MMORPG	Licensed	Latest round of CBT finished on Nov 22nd, 2016
DDTank Mobile	弹弹堂	Casual	Licensed	Latest round of CBT started from Dec 27, 2016
Mobile JX3	剑网3: 指尖江湖	MMORPG	Licensed	Latest round of CBT to start from Aug 28th, 2016
Legend of Ravaging Dynasties	爵迹	MMORPG	IP licensed	TBD
Starline	星际火线	Action x Shooting	In-house developed	Latest round of CBT started from Dec 29, 2016
BNB	泡泡堂	Casual	Licensed	TBD
Lineage II	天堂2	MMORPG	Licensed	TBD
Freestyle Mobile	街头篮球	Sports	Licensed	Latest round of CBT started on Jan 6th, 2016
Star NBA	王牌NBA	Sports	In-house developed	Latest round of CBT started on Feb 24, 2017
Fishing Man	猎鱼达人	Casual	Licensed	Latest round of CBT started on Feb 16, 2017

Source: Company disclosure, CICC Research



Figure 3: Earnings revisions

(Rmb mn)	Before		After		+/-	
	4Q16E	2016E	4Q16E	2016E	4Q16E	2016E
Revenue	43,549	151,624	43,958	152,032	0.9%	0.3%
Income from operations	14,243.0	56,430	14,079	56,267	-1.1%	-0.3%
Non-GAAP net income (loss)	11,670	44,759	11,547	44,635	-1.1%	-0.3%

Source: Company data, CICC Research

Figure 4: Quarterly financials

Income Statement (Rmb mn)	2014	2015	1Q16	2Q16	3Q16	4Q16E	2016E	1Q17E	2Q17E	3Q17E	4Q17E	2017E	2018E
Gross Revenue	78,932	102,863	31,995	35,691	40,388	43,958	152,032	46,643	50,086	53,600	56,445	206,774	259,803
cost of revenue	(30,873)	(41,631)	(13,406)	(15,235)	(18,560)	(20,296)	(67,497)	(21,630)	(23,583)	(26,461)	(27,911)	(99,584)	(125,392)
Gross profit	48,059	61,232	18,589	20,456	21,828	23,662	84,536	25,014	26,503	27,140	28,534	107,191	134,411
Sales and marketing expenses	(7,797)	(7,993)	(2,032)	(2,365)	(3,277)	(4,396)	(12,070)	(3,265)	(3,506)	(4,395)	(5,644)	(16,811)	(20,265)
General and administrative expenses	(14,155)	(16,825)	(4,368)	(5,299)	(5,883)	(6,638)	(22,188)	(6,763)	(7,313)	(7,826)	(8,467)	(30,368)	(37,671)
Other operating (loss)/income, net	4,435	4,213	1,209	1,537	1,792	1,451	5,989	1,866	2,003	2,144	2,258	8,271	10,392
Income (loss) from operations	30,542	40,627	13,398	14,329	14,460	14,079	56,267	16,851	17,688	17,063	16,681	68,283	86,867
Financial income, net	(1,182)	(1,618)	(491)	(377)	(604)	(659)	(2,131)	(491)	(377)	(604)	(847)	(2,319)	(3,897)
Share of loss of a jointly controlled e	(347)	(2,793)	(1,089)	(292)	(619)	(500)	(2,500)	(500)	(500)	(500)	(500)	(2,000)	(1,600)
Profit before income tax	29,013	36,216	11,818	13,660	13,237	12,920	51,635	15,860	16,811	15,959	15,334	63,964	81,370
Income tax expense	(5,125)	(7,108)	(2,550)	(2,780)	(2,461)	(2,584)	(10,375)	(3,331)	(3,362)	(2,873)	(3,067)	(12,632)	(15,460)
Net income (loss)	23,810	28,806	9,183	10,737	10,646	10,206	40,772	12,379	13,299	12,936	12,117	50,732	65,310
Non-GAAP net income (loss)	24,224	32,261	10,032	11,319	11,737	11,547	44,635	13,872	14,902	14,651	13,923	57,349	73,624
<b>Growth Analysis</b>													
Gross revenue- YoY	30.6%	30.3%	42.8%	52.3%	51.9%	44.4%	47.8%	45.8%	40.3%	32.7%	28.4%	36.0%	25.6%
Gross Revenue- QoQ			5.1%	11.6%	13.2%	8.8%		6.1%	7.4%	7.0%	5.3%		
Net profit-YoY	53.6%	21.0%	33.4%	46.8%	43.0%	42.5%	41.5%	34.8%	23.9%	21.5%	18.7%	24.4%	28.7%
Net profit-QoQ			28.2%	16.9%	-0.8%	-4.1%		21.3%	7.4%	-2.7%	-6.3%		
<b>Margin Analysis</b>													
Gross margin	60.9%	59.5%	58.1%	57.3%	54.0%	53.8%	55.6%	53.6%	52.9%	50.6%	50.6%	51.8%	51.7%
Total expenses /Revenue (%)	22.2%	20.0%	16.2%	17.2%	18.2%	21.8%	18.6%	17.5%	17.6%	18.8%	21.0%	18.8%	18.3%
Selling expense /Revenue (%)	9.9%	7.8%	6.4%	6.6%	8.1%	10.0%	7.9%	7.0%	7.0%	8.2%	10.0%	8.1%	7.8%
G&A /Revenue (%)	17.9%	16.4%	13.7%	14.8%	14.6%	15.1%	14.6%	14.5%	14.6%	14.6%	15.0%	14.7%	14.5%
Operating margin	38.7%	39.5%	41.9%	40.1%	35.8%	32.0%	37.0%	36.1%	35.3%	31.8%	29.6%	33.0%	33.4%
Net margin	30.2%	28.0%	28.7%	30.1%	26.4%	23.2%	26.8%	26.5%	26.6%	24.1%	21.5%	24.5%	25.1%
Effective tax rate	17.7%	19.6%	21.6%	20.4%	18.6%	20.0%	20.1%	21.0%	20.0%	18.0%	20.0%	19.7%	19.0%

Source: Company data, CICC Research



Figure 5: Comparable valuations

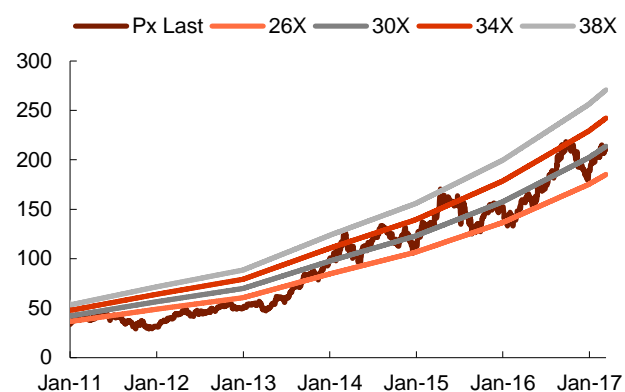
Company Name	Ticker	Trading CCY	Reporting CCY	Rating	Share Px 2017-03-12	Mkt Cap (US\$ mn)	Vol (mn)	PEG 16E	P/E			Non-GAAP P/E			Non-GAAP P/E (excl. cash)			P/S		
									15A	16E	17E	15A	16E	17E	15A	16E	17E	15A	16E	17E
<b>China Internet</b>																				
<b>Conglomerate</b>																				
Tencent	700-HK	HKD	CNY	BUY	212.4	259,253	15.2	1.2	55.6	43.0	32.8	49.4	39.3	31.0	48.9	38.4	29.2	15.9	11.8	8.7
Baidu Inc.	BIDU-US	USD	CNY	HOLD	172.74	59,925	2.1	n.a.	11.3	42.2	34.6	33.4	36.6	31.1	29.8	31.9	25.4	4.4	4.6	3.8
NetEase Inc.	NTES-US	USD	CNY	BUY	289.4	38,375	1.3	0.5	35.5	23.8	18.8	32.4	21.9	17.6	29.4	20.1	15.8	10.6	7.1	5.1
Sina Corp.	SINA-US	USD	USD	BUY	69.26	4,839	0.8	n.a.	161.1	21.5	33.4	77.8	50.3	31.5	154.5	25.9	24.2	5.5	4.8	3.5
Sohu.com	SOHU-US	USD	USD	HOLD	41.71	1,619	0.2	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	0.8	1.0	0.9
58.com	WUBA-US	USD	USD	HOLD	37.77	5,470	1.8	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	72.1	n.a.	n.a.	69.1	6.4	4.0	3.5
<b>E-Commerce</b>																				
JD.com	JD-US	USD	CNY	BUY	31.06	44,362	6.5	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	153.0	n.a.	n.a.	136.2	1.3	1.0	0.7
Jumei Int'l	JMEI-US	USD	USD		3.91	573	0.3	0.3	27.9	n.a.	n.a.	30.1	7.8	6.1	n.a.	n.a.	n.a.	0.3	0.2	0.2
Vipshop	VIPS-US	USD	CNY	HOLD	13.02	7,682	6.0	0.3	29.8	26.7	20.0	23.5	19.3	16.0	30.4	18.5	14.7	1.0	0.8	0.6
<b>Online Travel</b>																				
Qunar	QUNR-US	USD	CNY	BUY	30.41	4,506	0.1	n.a.	n.a.	n.a.	334.2	n.a.	n.a.	90.0	n.a.	n.a.	81.4	6.7	6.5	4.7
Tuniu Corp.	TOUR-US	USD	CNY	BUY	8.51	1,073	0.2	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	0.8	0.7	0.5
<b>Online Game</b>																				
Changyou	CYOU-US	USD	USD	HOLD	31	1,620	0.2	n.a.	7.6	12.3	9.1	7.4	11.4	9.5	1.7	n.a.	n.a.	0.7	1.0	0.9
Boyaa	434-HK	HKD	CNY		4.02	396	1.8	n.a.	6.4	8.7	8.3	18.9	9.4	9.0	9.0	5.0	4.1	3.1	3.7	3.5
Forgame	484-HK	HKD	CNY		8.2	145	0.1	n.a.	n.a.	16.2	7.6	n.a.	16.2	7.6	1.3	n.a.	n.a.	1.8	n.a.	n.a.
IGG Inc.	799-HK	HKD	USD	BUY	6.41	1,109	9.0	n.a.	27.6	16.5	7.5	27.6	16.4	10.9	23.0	13.8	8.8	5.5	3.4	2.4
Net Dragon	777-HK	HKD	CNY		22.1	1,408	0.6	n.a.	n.a.	n.a.	789.3	n.a.	n.a.	789.3	n.a.	n.a.	766.4	7.0	3.5	2.9
Ourgame	6899-HK	HKD	CNY	BUY	2.87	291	0.6	n.a.	16.0	12.2	8.9	15.9	11.3	9.0	12.8	8.9	6.9	2.4	2.1	1.7
TianGe	1980-HK	HKD	CNY		4.38	733	1.5	n.a.	29.1	22.3	15.3	29.1	23.1	15.7	20.6	n.a.	n.a.	6.8	6.0	4.6
YY Inc.	YY-US	USD	CNY	BUY	46.81	2,592	0.8	n.a.	16.0	14.0	10.9	13.9	12.4	10.2	13.6	10.2	7.2	1.9	1.5	1.2
<b>Verticals</b>																				
Phoenix New Media	FENG-US	USD	CNY	BUY	3.7	264	0.1	n.a.	22.4	105.7	20.3	11.6	56.1	25.7	n.a.	37.0	3.0	0.5	0.6	0.5
500.com	WBAI-US	USD	CNY		12.91	536	0.2	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	27.8	n.a.	n.a.
51Job	JOBS-US	USD	CNY		35.5	2,093	0.1	n.a.	21.5	30.1	20.5	19.7	22.5	18.6	14.1	19.0	14.4	6.6	6.1	5.3
AutoHome	ATHM-US	USD	CNY	BUY	35.61	4,095	0.9	n.a.	25.3	25.2	20.1	23.5	21.8	18.0	24.2	18.6	14.5	7.4	4.7	4.8
BitAuto	BITA-US	USD	CNY	HOLD	24.48	1,731	0.9	n.a.	n.a.	n.a.	n.a.	28.1	36.3	19.4	26.0	30.6	21.7	2.7	2.1	1.7
<b>Education</b>																				
TAL Education Group	TAL-US	USD	USD	BUY	91.57	7,528	0.4	1.2	71.5	72.0	46.2	61.5	60.1	39.0	58.1	53.4	30.9	6.9	4.2	2.8
New Oriental Education	EDU-US	USD	USD	BUY	51.11	8,059	0.9	1.2	35.7	31.2	23.7	33.2	28.5	21.7	28.5	23.8	17.1	5.5	4.6	3.8
China Online Education	COE-US	USD	CNY		14.2	284	0.0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	1.2	2.2	0.9	0.4
Tarena Int'l Inc.	TEDU-US	USD	USD		18.1	1,045	0.3	0.6	34.2	28.8	21.9	31.2	23.4	20.5	33.5	20.1	16.7	4.5	3.6	2.9

Note: CICC-covered companies are highlighted in green; all financials based on Bloomberg Consensus.

Source: Bloomberg, Company data, CICC Research

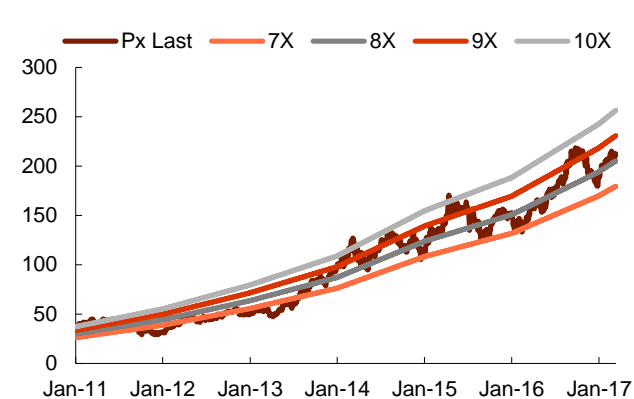


Figure 6: P/E bands



Source: Bloomberg, Company data, CICC Research

Figure 7: P/B bands



Source: Bloomberg, Company data, CICC Research

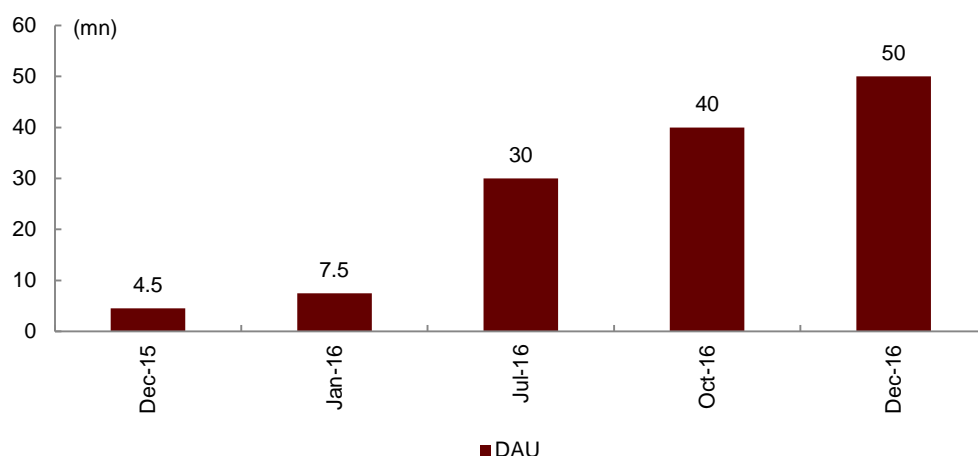


## Honor of Kings sets a mobile gaming record

**Honor of Kings (王者荣耀) is a multi-player online battle-arena (MOBA) mobile game developed and published by Tencent;** it was launched on November 26, 2015, although OBT started in October. So far, it might be the most successful mobile game in China mobile game history with >70mn DAUs and >Rmb2bn grossing recorded in January~February 2017, according to our channel checks.

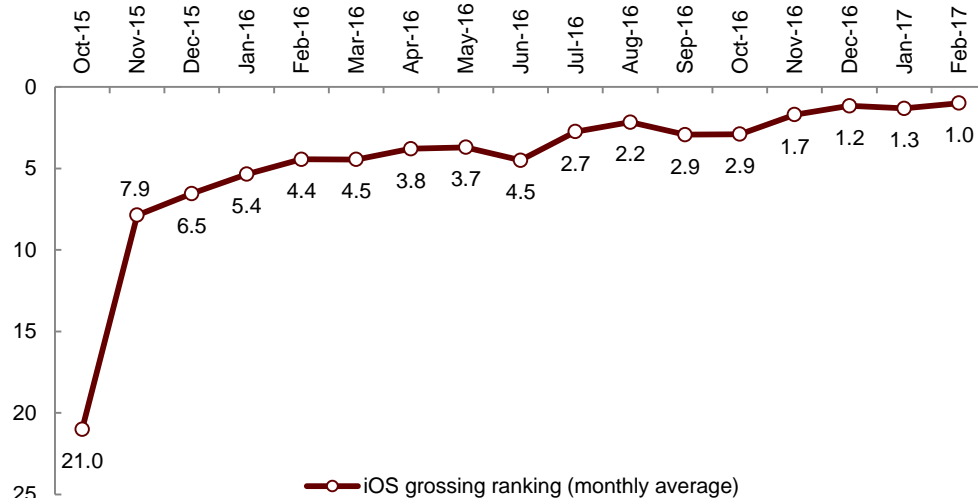
As it follows the typical MOBA gameplay set by the hit PC title *League of Legends* with extensive adaptations to the mobile play scenarios (including simplified controls, faster battle pace and embedded social functions, etc.), it has penetrated into a large range of gamers from both hardcore to newly acquired casual gamers. According to Questmobile, *HoK* ranked #1 in terms of device penetration on both iOS (17.1%) and Android (18.9%). And after 17 months of launch, it's still growing its player base and monetization potential.

Figure 8: DAUs announced by Tencent



Source: Company announcement, CICC Research

Figure 9: HoK's iOS grossing ranking (monthly average)

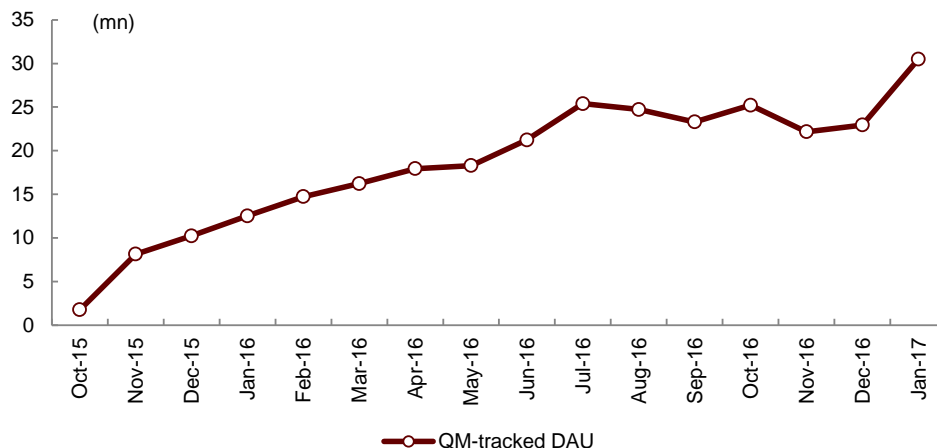


Source: AppAnnie, CICC Research



During Chinese New Year, thanks to its teamwork nature, social engaging environment and Tencent's strong promotional efforts (intensive schedule of events and new content), it boosted its momentum even further and stepped up its monthly grossing to >Rmb2bn, the first time ever a Chinese online game has hit such heights.

**Figure 10: QuestMobile-tracked DAU jumped significantly in January 2017**



Source: QuestMobile, CICC Research

**Figure 11: HoK event list since January 2017**

Chinese Summary	English Summary	Event Type	Start Date	End Date
王者荣耀肯德基人气荣耀餐	HoK special meal with KFC	Marketing	1.01	
王者QGC决赛: Hero战队斩获总冠军	QGC Finals	e-Sports	1.07	1.11
“王者荣耀赛事”微信小程序上线	Wechat Mini-App for HoK Tournaments	New functions	1.09	
无限荣耀版本更新三重礼	Gifts for new version updates	Log-in rewards	1.12	1.14
S6新赛季专属皮肤帅气出场, 分享有礼	Season S6 starts with sharing gifts	Marketing	1.12	1.18
新英雄哪吒登场! 限时折扣中	New hero available with discounts	New content / Discounts	1.12	1.18
重塑达摩登场! 英雄限时折扣中	New hero available with discounts	New content / Discounts	1.12	1.18
点券夺宝限时折扣	Discounts on random draws	Lottery	1.16	1.18
全民COS等你来, 鸡年限定抢先玩	Cosplay events with Tencent's image-editing app	Marketing	1.18	
【新春佳节】壕礼相送! 错过再等一年	Chinese New Year in-game missions with rewards	In-game events	1.19	2.10
幸运英雄宝箱, 2元来抽划关张	New lottery draw	Lottery	1.19	1.22
每日充值: 充1元送皮肤碎片	New daily charging gifts	Charging incentives	1.19	1.22
小年登录送元宝, 最高可开2017钻石	Chinese New Year log-in gifts	Log-in rewards	1.20	1.20
关羽新皮肤龙腾万里上架! 限时折扣中	New hero skin available with discounts	Promotions / Discounts	1.20	1.26
新春专属-首套五黑系列皮肤-限时八折!	Popular hero skins at discount	Promotions / Discounts	1.20	1.26
【新春专属皮肤】拥有即送皮肤碎片!	Rewards for purchasing CNY-special hero skins	Charging incentives	1.20	1.26
KPL大神齐拜年, 送祝福赢钻石周边	KPL tournament events on weibo with in-game lottery	e-Sports / Marketing	1.22	2.04
王者荣耀给2亿召唤师拜年啦!	CNY gifts through emails	Promotions	1.27	1.27
新英雄魂燃重炮-黄忠上架	New hero available with discounts	New content / Discounts	2.08	2.21
体验服【资格申请活动】	New test server open for applications	New content	2.10	
《大话西游》电影正版授权-至尊宝皮肤	New hero skin licensed with the classic movie <i>A Chinese Odyssey</i>	Marketing / Promotions	2.11	3.14
月光宝盒兑换情侣头像框、高级铭文	Movie ( <i>A Chinese Odyssey</i> )-themed in-game rewards	In-game events	2.11	2.18
元宵佳节-登录送好礼	Lantern Festival log-in gifts	Log-in rewards	2.11	2.11
2月13日登录领开学福利!	School semester opening log-in gifts	Log-in rewards	2.13	2.13
累计登录-送非卖皮肤	Accumulated log-in gifts	Log-in rewards	2.14	2.26
“小绵羊”张艺兴直播《王者荣耀》开团!	Live broadcasting of celebrities playing HoK	e-Sports / Marketing	2.18	
《王者荣耀》跨界造星, 携手BMW深度合作	BMW-themed hero skin available (joint marketing with Tencent)	Marketing	2.28	
周末狂欢! 点券大赠送, 仅此一天	Weekend charging gifts	Charging incentives	3.03	3.03
皮肤抽奖宝箱限时上架, 李白貂蝉等皮肤开出来!	Hero skin lottery	Lottery	3.03	3.05
英雄抽奖宝箱限时上架, 赢政夏侯惇开出来!	Hero lottery	Lottery	3.03	3.05
第三届王者荣耀城市赛 首站	HoK Offline Tournament in Shanghai, Guangzhou, Haikou and Nanning	e-Sports	3.04	3.05
新皮肤-赵云-限定史诗皮肤引擎之心正式上线	New hero skin available at discounts	New content	3.07	3.13
皮肤礼包【引擎之心-守护】-八折特惠	Bundled new skin promotions available	New content / Discounts	3.07	3.13
参与排位累计送	Accumulated gifts for ranking battles	In-game events	On-going	On-going
【寒假开团】参与得好礼!	Gifts for in-game team battle mode	In-game events	On-going	On-going
娱乐模式3连开, 海量钻石拿不停!	Gifts for in-game entertainment mode	In-game events	On-going	On-going
疯狂对战2连开, 钻石碎片换换换!	Gifts for in-game missions (consecutive wins)	In-game events	On-going	On-going
周一惊喜	Monday log-in gifts	Log-in rewards	On-going	On-going

Source: HoK official website, CICC Research





On December 17~18, *Honor of Kings* closed its first season of professional e-sports tournament KPL with a grand finale of tournament finals and celebrations (celebrity games, cosplay, exhibition games, etc.). During the 3-month tournament, total viewership surpassed 350mn with daily numbers peaking at >8mn. Unique viewers reached 40mn with 36mn viewers participating in the process (commenting, voting, gifting, etc.). In 2017, KPL will last for >100 game days divided into two seasons; we expect a higher still engagement level 2017.

Figure 12: KPL Season Finale and Annual Campaigns



Source: QQ game portal, CICC Research

Given *HoK's* strong momentum in player base, monetization and publicity, we expect it to contribute further to Tencent's mobile game revenue and to continue to grow into 2017.



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