

11 July 2014

OURGAME (6899.HK)

From online to offline, the new business model likely brings in loyal customers

HONG KONG | SOFTWARE | COMPANY ANALYSIS

Rating: **Accumulate**

- Ourgame's 1Q14 revenue up 101.3% yoy. Among which 71.5% was coming from the self developed PC games and RMB 17.3Mn was the mobile games revenue, which already exceeded the 2013 total of RMB 15.6Mn. Gross profit margin maintained as 66.6% and net profit surged 12 times yoy and was over 60% of the 2013 net profit.
- To capture the fast growing card game market, the company started to organize poker tournaments in 2012, and as co-organizer in the 14th World Bridge Championships in 2014. It is expected to obtain huge publicity and goodwill through this kind of activities.
- It is now trading below the initial offering price and we give it an initial rating of "Accumulate" with target price HK\$ 4.10, equivalent to 28x of 2014 forecasted EPS plus cash per share HK\$ 0.15.

Financial Highlights

Ourgame listed on the main board at June 30, 2014. According to its listing prospectus, the 1Q14 revenue amounted to RMB 93Mn, up 101.3% yoy. Among which RMB 66.5Mn was coming from the self developed PC games, accounted for 71.5% of the total revenue. RMB 17.3Mn was the mobile games revenue, which already exceeded the 2013 total of RMB 15.6Mn. Gross profit was RMB 61.9Mn with gross profit margin maintained as 66.6%. Profit attributable to shareholder amounted to RMB 21.6Mn, which surged 12 times yoy and was over 60% of the 2013 net profit.

How we view this

Ourgame started to operate online card and board game since 1998, which the brand name is familiar to PRC customers. Since the share on PC games showed a continuous declining while revenue from mobile game keeps on increasing, to capture the fast growing card game market, the company started to organize poker tournaments in 2012, which is authorized by the World Poker Tour, and is chosen as co-organizer in the 14th World Bridge Championships in 2014. It is expected to obtain huge publicity and goodwill through this kind of activities.

Investment Action

With the online to offline operating model, the company is likely to capture high quality potential new customers through the matches. It can also increase the existing customers' involvement and thus their loyalty. Once the customers stay in the game, monetization becomes much easier. However, we believe Ourgame is priced a bit higher for its IPO of HK\$ 4.25. It is now trading below the initial offering price and we give it an initial rating of "Accumulate" with target price HK\$ 4.10, equivalent to 28x of 2014 forecasted EPS plus cash per share HK\$ 0.15.

Key Financial Summary

FYE Dec	FY12	FY13	FY14E	FY15E	FY16E
Revenue (RMB mn)	206	236	376	456	510
Net Profit (RMB mn)	29	35	89	119	132
EPS (HKD)	0.09	0.11	0.14	0.19	0.21
P/E (X)	42.5	35.5	26.7	20.0	18.0
BVPS (HKD)	0.33	0.45	0.38	0.56	0.77
P/B (X)	11.5	8.3	10.0	6.6	4.8
DPS (HKD)	0.00	0.00	0.00	0.00	0.00
Div. Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%

Source: PSR est.

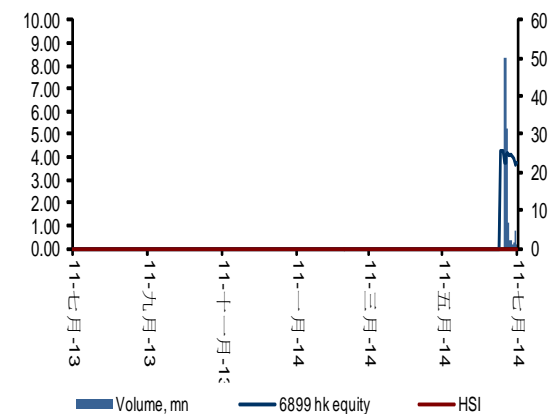
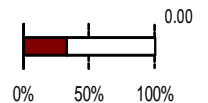
Target Price (HKD)	4.10
Forecast Dividend (HKD)	0.00
Closing Price (HKD)	3.75
Potential Upside	9.3%

Company Description

Ourgame is a mainland online card & board games developer and operator, which operated more than 200 PC and mobile games on a PC client portal Ourgame Hall. Besides, the company also organized offline tournaments with governments and official organizations such as the World Poker Tour.

Company Data

Raw Beta (Past 2yrs weekly data)	N/A
Market Cap. (HKD bn)	2,940
Enterprise Value (HKD mn)	2,810.00
52 week range (HKD)	3.50 - 4.25
Closing Price in 52 week range	0.00



Major Shareholders

1. Liu Jiang & ASSO	45.91%
2. CMC Ace Holdings Limited	15.00%

Valuation Method

PE

Analyst

Kay Ng

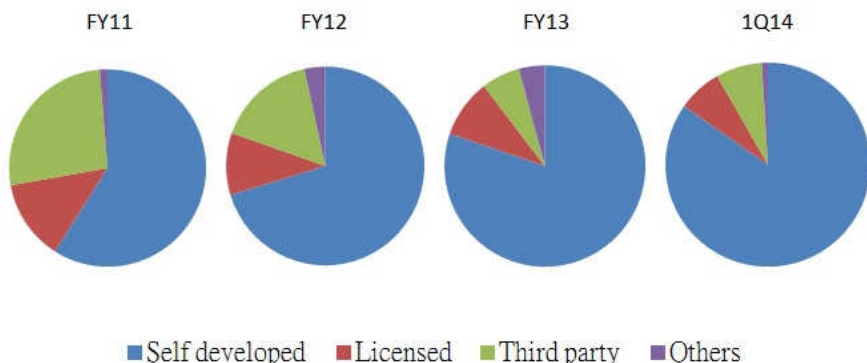
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Product mix shifts to self developed games

Ourgame operated over 200 PC games through its own online platform and the client portal Ourgame Hall. In 2011, only 59% of revenue was coming from self developed games, the figure increased to 80.2% in 2013 and further to 84.7% in 1Q14. However, the company did not rely on any single game category on the customer base or the revenue generated. No any single game category accounted for more than one-third of the total revenue.

Fig 1 Source of products

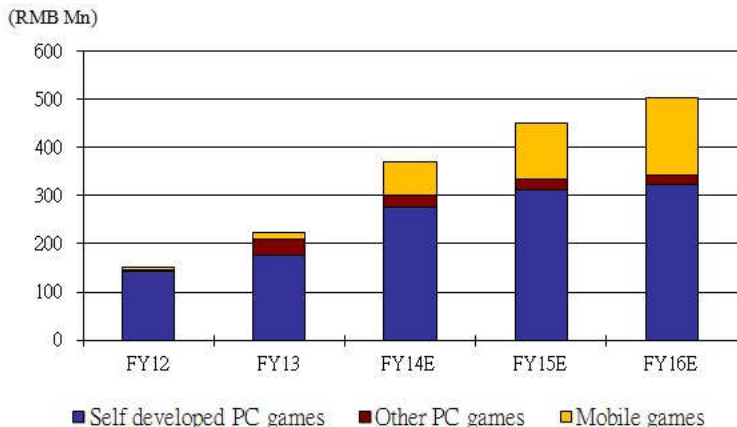


Source: Company reports

Revenue from mobile games ramp up

According to its listing prospectus, among the 1Q14 revenue, RMB 17.3Mn was obtained from mobile games, accounted for 18.6% of the total revenue, which already exceeded the 2013 total of RMB 15.6Mn. It is expected the share will keep going up since the company is actively shifting the existing PC games to the mobile market.

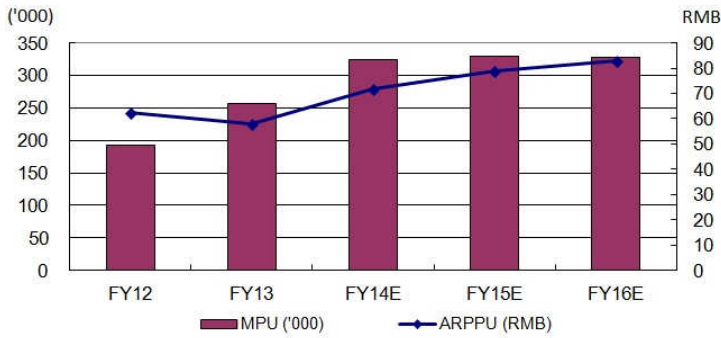
Fig 2 Revenue mix estimates



Source: PSR, Company report

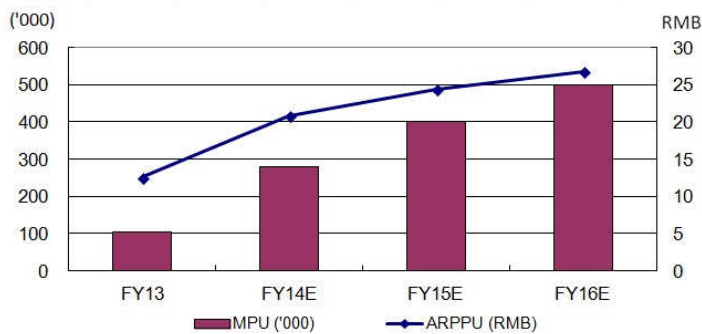
Both the MPU and ARPPU increased for PC games and mobile games in 2013. However, the MPU for PC games is expected to stay in 2015 and start to drop in 2016. Mobile games are believed as the future growth momentum which MPU and ARPPU are forecasted to ramp up in the coming years.

Fig 3 MPU & ARPPU estimate of PC games



Source: PSR, Company report

Fig 4 MPU & ARPPU estimate of mobile games



Source: PSR, Company report

Potential Risks

The growth on mobile games slows down;
 O2O model fails;

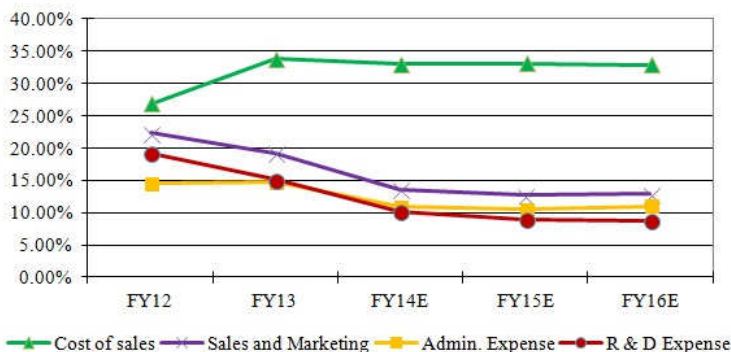
From online gaming to offline matching

In order to capture the fast growing card game market, the company started to organize poker tournaments in 2012, which is authorized by the World Poker Tour, and is chosen as co-organizer in the 14th World Bridge Championships in 2014. Meanwhile, it has also produced a game show which has been broadcasted in several PRC TV channels. It is expected to obtain huge publicity and goodwill through this kind of activities. With the online to offline operating model, the company is likely to capture high quality potential new customers through the matches. It can also increase the existing customers' involvement and thus their loyalty. Once the customers stay in the game, monetization becomes much easier.

Cost soars and expenses go reversely

The 2013 cost of sales soared 44.4% to RMB 79.8Mn which represented 33.8% of revenue, up from 26.9% in 2012. The expenses dropped, compared to the revenue in 2013. We estimate the cost to stay at current level and the expenses to further drop a bit since we expect the revenue will grow at the rate faster than the expenses.

Fig 5 Costs as percentage of revenue estimates



Source: PSR, Company report

	FY12	FY13	FY14E	FY15E	FY16E
Valuation Ratios					
P/E (X)	42.5	35.5	26.7	20.0	18.0
P/B (X)	11.5	8.3	10.0	6.6	4.8
EV/EBITDA (X)	75.6	62.8	24.4	18.6	16.7
Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Per share data (HKD)					
EPS	0.088	0.106	0.141	0.188	0.209
DPS	0.000	0.000	0.000	0.000	0.000
BVPS	0.326	0.450	0.377	0.564	0.773
Outstanding Shares (basic, mn)	411.60	411.60	784.00	784.00	784.00
Growth & Margins (%)					
Growth					
Revenue	33.7%	14.8%	59.1%	21.3%	11.8%
EBIT	19.2%	20.5%	156.9%	31.3%	11.3%
Margins					
Gross profit margin	73.1%	66.2%	67.0%	66.9%	67.1%
EBT margin	18.1%	18.9%	30.6%	33.1%	32.9%
Net Profit Margin	14.2%	14.8%	23.6%	26.1%	25.9%
Key Ratios					
ROE (%)	27.1%	23.5%	37.3%	33.3%	27.0%
ROA (%)	21.7%	3.7%	5.9%	5.3%	4.3%
Income Statement (RMB mn)					
Revenue	206	236	376	456	510
Cost of revenue	(55)	(80)	(124)	(151)	(168)
Gross profit	151	156	252	305	342
Selling & Marketing expenses	(46)	(45)	(51)	(58)	(66)
Administrative expenses	(30)	(35)	(41)	(48)	(56)
R & D expenses	(40)	(36)	(38)	(41)	(45)
Other income, net	3	5	3	3	3
Share-based compensation expense	(1)	(0)	(10)	(10)	(10)
Operating profit	37	45	115	151	168
Finance expense	0	0	0	0	0
Taxation	(6)	(4)	(13)	(16)	(18)
Profit After Tax	31	40	102	135	150
Minority interest	(2)	(5)	(13)	(16)	(18)
Profit for the year	29	35	89	119	132
EPS	0.071	0.085	0.113	0.152	0.168

Source: Company, PSR

PHILLIP RESEARCH STOCK SELECTION SYSTEMS

Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within \pm 5% from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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