

14 August 2018

Technology | Software & Services

## Kingsoft

**Buy** (Maintained)

Target Price: HKD32.52

Price: HKD16.20

Market Cap: USD2,842m

Bloomberg Ticker: 3888 HK

### Profit Warning

Late last night, Kingsoft issued updates on its 2H18 results, indicating that 3Q18 and even full-year 2018 may be loss-making due mainly to three reasons:

1. Delay in the launching of *JX Mobile III* and lacklustre performance of *YSYY*;
2. Losses incurred at the competitive cloud business;
3. R&D investments for its office software businesses.

We place our rating, forecasts and TP under review, as we believe Kingsoft's share price has yet to fully price in these negative factors over the short term.

**Financial impact from a delay in the launching of *JX Mobile III*.** According to the most recent official update from the company (in Jun 2018), the launch date for *JX Mobile III* would be in Oct 2018. If the launch is delayed to early 2019, we estimate that Kingsoft will have CNY300-400m less profit in 2018. This is assuming the game can generate CNY1.3bn in gross billing during the first quarter of its launch, and Kingsoft takes 30% as its revenue (the remaining goes to publisher, Tencent).

#### Why we believe these negative factors have not been fully priced in:

- i. Firstly, although there have been market talk and reports over the past few weeks mentioning the potential delay of *JX Mobile III*, this is the first time the company has officially disclosed the news;
- ii. Secondly, it is the first time that the company is guiding that absolute losses at the cloud business will be larger than last year's. The company had previously said "similar loss amount compared to last year";
- iii. Thirdly, it is the first time that the company is guiding for a net loss for 3Q18 and even possibly full-year 2018. We believe this is going to hurt market sentiment and lead to potential downward correction;
- iv. Lastly, the launch date for *JX Mobile III* is now believed to be in early 2019. However, there could be further delays that may place uncertainties on the company's 2019 performance as well.

**Forecasts, rating and TP under review.** We place our BUY rating and HKD32.52 TP under review, pending the release of its annual results on 21 Aug 2018.

Forecasts and Valuations	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
Total turnover (CNYm)	3,834	5,181	6,872	9,652	12,394
Reported net profit (CNYm)	(271)	978	1,228	1,990	2,720
Recurring net profit (CNYm)	954	1,213	1,502	2,170	2,900
Recurring net profit growth (%)	73.4	27.2	23.8	44.5	33.6
Recurring EPS (CNY)	0.74	0.91	1.10	1.59	2.12
DPS (CNY)	0.09	0.09	0.09	0.09	0.09
Recurring P/E (x)	19.2	15.6	13.0	9.0	6.7
P/B (x)	2.33	1.61	1.47	1.29	1.10
P/CF (x)	19.8	11.0	8.9	7.3	5.0
Dividend Yield (%)	0.6	0.6	0.6	0.6	0.6
EV/EBITDA (x)	6.64	1.04	1.41	1.00	0.61
Return on average equity (%)	(3.4)	9.8	9.7	14.1	16.6
Net debt to equity	net cash	net cash	net cash	net cash	net cash
Our vs consensus EPS (adjusted) (%)			(0.6)	5.8	13.9

Source: Company data, RHB

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