

Tencent Holdings Ltd.

Asia Satellite*

Recommended since 01.04.2021

28.03.2023

ASIE

Country HK	Market capitalization (bn) HKD 3492,7	Perf. since reco. (%)
Sector Communication Services	Free float 64,1%	Tencent Holding -39,8
Factset 700-HK	Closing price HKD 362,80	Sector -23,4
ISIN KYG875721634	ESG Risk score* 21,8 Medium risk	



Profile

Tencent is a Chinese online giant with one of the world's largest online communities. Key services include communication and social media (WeChat and QQ), gaming, content (news, videos, music, manga and literature), services (e-mail, app store, mobile security), cloud services and financial services (Tenpay). Tencent's services are broken down into three segments: Value-added services or VAS (online gaming and social networking), online advertising and everything else (payment services, cloud services and other business services). Tencent has a monthly active user base of around 600m people on QQ and more than 1.2bn on WeChat.

Strengths/opportunities

- Diversified portfolio of services and high capacity for innovation.
- Monopoly and/or dominant position in a number of segments.
- Strategic investments in content, the cloud and FinTech.

Weaknesses/threats

- Anti-monopoly legislation and government regulations could affect Tencent's profitability.
- Fierce competition (Alibaba, Sony, ByteDance, NetEase) with a negative impact on margins.

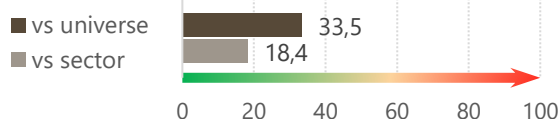
Investment case

- Tencent is at the heart of the internet, enjoying some of the most powerful network effects of any company in the world. The group runs various high free cash flow businesses and has substantial opportunities for growth both in China and worldwide. Tencent stands out for its ability to monetise an ecosystem based around fast-growing businesses and investments: video games, subscription music and video services, e-commerce, mobile payments and online advertising.
- Tencent's flagship product is WeChat, a unique mobile app that plays a vital role in consumers' day-to-day lives. WeChat is used for everything in China: from messaging to paying bills, it includes all kinds of functionality that makes it both a must-have product and a highly valuable source of user data.
- In online advertising (c.15% of 2021 revenue), Tencent is well placed to generate long-term revenue with WeChat: this largely unmonetised asset is ideally positioned to capitalise on an advertising rebound in 2023. Another major growth driver is video games (c.33% of revenue), with the group offering a very wide range of popular games. Global growth in mobile gaming is set to average 15% a year over the period 2020-2024 – a rate Tencent is set to top.
- The group is also well placed to monetise its user base over the long term via FinTech and business services (c.27% of revenue).

Valuation

The share is trading at high ratios (P/E: 22x for 2023e and 18x for 2024e), which we consider reasonable given the company's strong growth (with EPS growth set to average 15% a year over the period 2022-2024) and lower risk than its peers. The discount is explained by the intense competition, regulations and the Zero-covid policy

ESG risk vs. universe & sector (percentile)*



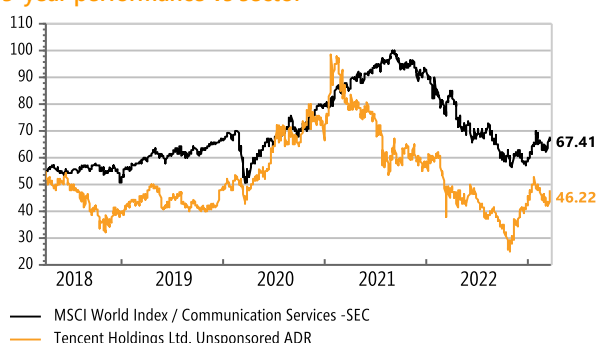
USD	12/2022	2023e	2024e
Sales revenue (mio)	82 355	89 688	100 192
Sales growth	-5,2%	8,9%	11,7%
EBIT adjusted (mio)	15 270	25 333	28 998
% of sales	18,5%	28,2%	28,9%
Net income (mio)	27 955	20 388	24 010
Net income growth	-19,8%	-27,1%	17,8%
FCF/Sales	#N/A	220,6%	231,7%
Net debt/Ebitda	0,4x	-0,4x	-0,8x
Dividend yield	0,7%	0,5%	0,6%
PE	14,5x	21,7x	18,2x
P/BV	3,9x	3,2x	2,7x

Factset estimates

ESG - risks and key points

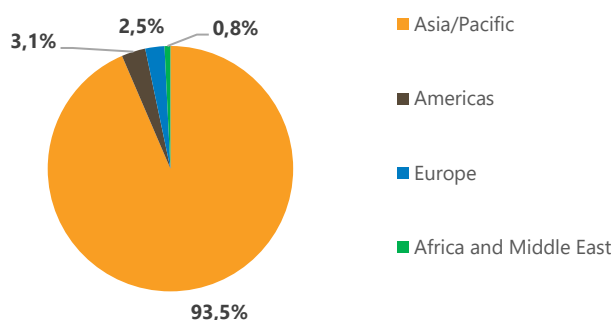
- Ranked medium risk due to its use of personally identifiable information (PII).
- Tencent remains exposed to antitrust investigations by Chinese regulators (anti-competitive practices, compliance with legislation governing online behaviours and its Variable Interest Entity structure).
- Strict supervision of FinTech sector risks and cooperation with financial institutions in this area.

5-year performance vs sector



Source: FactSet

Sales breakdown - 12/2021



*: see overleaf

Source: Factset, Sustainalytics

Glossary

Satellite

From 2015, B&Cie separates its investment recommendations into Core Holdings (higher organic growth potential, high free cash flow, ROCE in excess of the cost of capital and balance sheet efficiency throughout the cycle) and Satellite Recommendations, which do not meet the above criteria but are likely to outperform in the short-to-medium term.

ESG Risk Score

At B&Cie, we take particular care to ensure that the companies in which we recommend investing are sustainable. Accordingly, our selection process takes account of risks relating to environmental, social and governance (ESG) issues. This approach is underpinned by research from Sustainalytics, the global leader in ESG and corporate governance analysis, whose methodology aims to identify major controversies and risks and assess a company's ESG risks relative to both its sector and the investment universe as a whole. The corresponding score is expressed as a percentile: the lower the overall risk score, the lower the risk within the investment universe.

b-Digital, b-Transition & b-Well

Over and above the conventional geographical and sectoral approaches to asset management, at B&Cie we believe the world of tomorrow is being shaped by structural trends. We have identified three main megatrends: ongoing digital globalisation of the economy; economic transition, particularly in the energy sector; and the quest for wellness. We believe selecting and investing in companies that play an active role in these transformations should lead to more resilient portfolios that generate higher long-term returns. Our investment recommendations in the digital globalisation space are labelled "b-Digital", those in the economic transition space "b-Transition" and those in the wellness space "b-Well". A given recommendation may fall under more than one theme, in which case it will carry the relevant matching labels.

Offices & Branches

Bordier & Cie Genève

Rue Rath 16
CH-1204 Genève
Case postale
CH-1211 Genève 3
T + 41 58 258 00 00
F + 41 58 258 00 40

Bordier & Cie Berne

Spitalgasse 40
Case postale
CH-3001 Berne
T + 41 58 258 07 00
F + 41 58 258 07 10

Bordier & Cie Nyon

Rue de la Porcelaine 13
CH-1260 Nyon
Case postale 1045
CH-1260 Nyon 1
T + 41 58 258 07 50
F + 41 58 258 07 70

Bordier & Cie Zurich

Talstrasse 83
CH-8001 Zürich
T + 41 58 258 05 00
F + 41 58 258 05 50

Bordier & Cie (France) S.A.

1, rue François 1er
75008 Paris – France
T + 33 1 55 04 78 78
F + 33 1 49 26 92 48

Bordier & Cie (Uruguay) S.A.

Edificio Beta 3, oficina 102
Zonamerica
91600 Montevideo
Uruguay
T + 598 2 518 2700
F + 598 2 518 2703

Bordier & Cie (Singapore) Ltd

CapitaGreen #14-00
138 Market Street
Singapore 048946
T + 65 6239 9999
F + 65 6239 9998

Bordier Bank (TCI) Ltd

Leeward Highway
Caribbean Place
Providenciales
Turks and Caicos
T + 1 649 946 45 35
F + 1 649 946 45 40

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