

23 Jan, 2024

## Newborn Town | 09911.HK

### Potential delivery of a solid outlook

STOCK RATING

**BUY**

TARGET PRICE

**HK\$ 3.78**

Newborn Town (09911.HK) announced the latest operating data for the year ended 31 Dec, 2023. The revenue from the social networking business is expected to increase by YoY 15.4% - YoY 19.3% to RMB 2,950mn – RMB 3,050mn, and the revenue from the innovative business is expected to grow by YoY 32.2% - YoY 48.8% to RMB 320mn – RMB 360mn.

**Our expectations for the social networking business:** Newborn Town (09911.HK) recorded a strong profit margin after carrying out a series of improvement policies, but the adjustments dragged the top-line growth of the social networking business to a certain extent. After the completion of the streamers replacement, we expect to see a stable gross profit margin in 2023 2H, and a slight improvement in the top-line of the social networking business (before the consolidation of BlueCity) may be driven by the booming performance of SUGO and TopTop.

**Our expectations for the innovative business:** We expect that the revenue generated from Alice's Dream will grow on a QoQ basis in the last two quarters. Newborn Town (09911.HK) launched 2 games in 2023, and about 2 more games will be released in the coming year, bringing the innovative business to a higher level. We, thus, further estimate that the Group may record a similar level of YoY growth in FY 2024 in the innovative business, and Alice's Dream may realize a profit in the coming year.

**Potential delivery of a solid outlook:** We expect that i) the completion of streamers replacement, ii) growing contribution from TopTop, and iii) the adoption of external payment gateways will contribute to the improvement in the profit margin in FY 2023 and the future, offsetting the slower top-line growth when compared to our previous estimations. However, we may still see a sharp decrease in the net profit margin in FY 2023 and FY 2024 due to the consolidation of BlueCity, but it will be a new normal and nothing about the deterioration of business operation. We believe that Newborn Town (09911.HK) will deliver a strong result for FY 2023 and a solid outlook for its innovative business, the ability to achieve breakeven for the innovative business and new social networking APPs is our primary concern. We slightly upward adjust the TP to HKD 3.78/share, maintaining "BUY".

## COMPANY UPDATE

H F NGO, Brian, CFA

**SENIOR ANALYST**

brianngo@westbullsec.com.hk

+852 3896 2965

 2701 – 2703, 27/F, Infinitus Plaza, 199 Des Voeux Rd  
 Central, Sheung Wan, HK

### Newborn Town (09911.HK)

**Stock Rating** (Previous Rating) **BUY** (BUY)

**Target Price** (Previous TP) **HK\$ 3.78** (HK\$ 3.73)

 Current Price **HK\$ 1.85**

 52-Week Range **HK\$ 1.33 – 2.76**

 Market cap. (HKD, bn) **HK\$ 2.2**

RMB, mn	22(A)	23(E)	24(E)	25(E)
Revenue	2,799.7	3,280.0	4,074.8	4,379.2
Gross Profit	1,057.9	1,645.2	1,988.9	2,162.2
Gross Margin	37.8%	50.2%	48.8%	49.4%
Net Profit attr.	130.1	352.1	385.0	475.4
EPS	0.114	0.296	0.323	0.399
P/S	0.9	0.6	0.6	0.5
P/E	19.9	5.7	5.2	4.2
ROE	27.7%	35.5%	27.9%	23.7%

Performance	1 mth	3 mth	6 mth	1 year
Absolute	-1.1%	-21.9%	29.4%	-6.1%
Relative to HSI	6.2%	-10.5%	48.6%	23.2%



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We are concerned about the profitability of the Group after a series of changes carried out by the Group, it i) completed the replacement of the less effective streamers with the streamers providing higher marginal benefits, and ii) increased the adoption of external payment gateways, any signal showing an improvement in the profit margin (ex. BlueCity) in 2023 2H is our primary focus for the coming annual result.

#### **Our expectations for the social networking business**

Newborn Town (09911.HK) recorded a strong profit margin in 2023 1H after carrying out a series of improvement policies, but the adjustments dragged the top-line growth of the social networking business to a certain extent. After the completion of the streamers replacement, we expect to see a stable gross profit margin in 2023 2H, and a slight improvement in the top-line of the social networking business (before the consolidation of BlueCity) may be driven by the booming performance of SUGO and TopTop.

#### **Our expectations for the innovative business**

We expect that the revenue generated from Alice's Dream will grow on a QoQ basis in the last two quarters. Newborn Town (09911.HK) launched 2 games in 2023, and about 2 more games will be released in the coming year, bringing the innovative business to a higher level. We, thus, further estimate that the Group may record a similar level of YoY growth in FY 2024 in the innovative business, and core product, Alice's Dream, may realize a profit in the coming year.

#### **HeeSay, the international version of Blued**

Newborn Town (09911.HK) announced a new LGBTQ+ platform called HeeSay for overseas users in early 2024, features like posting, live streams, and voice chat are added to transform the platform from a dating APP to an online community. Social networking, instead of matchmaking, for LGBTQ+ will be the primary positioning for HeeSay, a broader range of thematic activities will also be carried out in the future because the sense of belonging to a platform is essential for LGBTQ+ people, according to the research conducted by the Group.

Exhibit: Logo of HeeSay



Source: Company data

Exhibit: Presence of Blued in the Metro Manila Pride



Source: Company data

It is the first half year for Newborn Town (09911.HK) to consolidate the financial statement of BlueCity, we expect that about RMB 300mn – RMB 350mn revenue will be recognized in 2023 2H. After the announcement of HeeSay, Blued will explore the overseas market more aggressively, especially Thailand, in the coming years, and we expect that the top-line of BlueCity may reach RMB 900mn – RMB 1,000mn in the next year.

#### Potential delivery of a solid outlook

We expect that i) the completion of streamers replacement, ii) growing contribution from TopTop, and iii) the adoption of external payment gateways will contribute to the improvement in the profit margin in FY 2023 and the future, offsetting the slower top-line growth when compared to our previous estimations. However, we may still see a sharp decrease in the net profit margin in FY 2023 and FY 2024 due to the consolidation of BlueCity, but it will be one-off and nothing about the deterioration of business operation. We believe that Newborn Town (09911.HK) will deliver a strong result for FY 2023 and a solid outlook for its innovative business. The ability to achieve breakeven for the innovative business and new social networking APPs is our primary concern in the coming years. We slightly upward adjust the TP to HKD 3.78/share, maintaining “BUY”.

## Peers comparison

		Mkt. Cap.	P/E	Fw. P/E	P/B	P/S	Revenue	GM	ROE
		(HKD, mn)	(x)	(x)	(x)	(%)	(HKD, mn)	(%)	(%)
00302.HK	CMGE	3,027.94	-	4.05	0.48	0.93	3,160.15	40.96	(2.18)
00700.HK	Tencent	2,485,979.46	11.81	13.41	2.99	3.83	645,740.38	43.05	25.51
00799.HK	IGG	3,690.45	-	-	1.60	0.79	4,591.33	68.63	(25.41)
02100.HK	Baioo	649.26	18.28	4.16	0.36	0.50	1,093.12	38.42	1.84
02400.HK	XD Inc.	3,608.20	-	17.64	1.65	0.91	3,995.11	53.49	(3.84)
02660.HK	Zengame	5,266.39	5.53	-	2.43	2.17	2,058.09	64.39	49.13
03798.HK	Homeland	3,144.34	5.97	-	1.42	1.65	1,819.94	65.30	24.89
06633.HK	Qingci Games	2,869.02	54.58	-	1.50	4.19	734.02	66.96	2.95
06820.HK	FriendTimes	2,638.83	224.13	5.89	1.85	1.84	1,775.06	68.49	1.27
06933.HK	Sino Entertainment	100.81	-	-	0.50	29.72	14.32	(30.19)	(40.83)
09990.HK	Archosaur Games	1,191.05	-	-	0.44	1.64	679.22	72.48	(25.61)
09999.HK	NTES	443,404.54	-	12.35	-	-	112,363.21	54.68	23.77
	<i>Average - Gaming</i>	<i>293,339.6</i>	<i>246,297.52</i>	<i>53.38</i>	<i>9.58</i>	<i>1.38</i>	<i>4.38</i>	<i>64,835.33</i>	<i>50.56</i>
BMBL.US	Bumble	14,725.64	41.73	24.63	1.11	1.81	7,075.00	72.39	(5.24)
MTCH.US	Match Group	76,648.26	17.42	15.57	-	3.05	24,970.67	69.90	-
YALA.US	Yalla Group	6,585.45	9.57	-	1.33	2.73	2,377.41	62.51	23.72
MOMO.US	Hello Group	9,030.90	4.62	4.20	0.71	0.68	14,793.20	41.58	17.06
YY.US	Joyy	14,191.37	-	11.06	0.36	0.88	18,883.70	35.34	(1.43)
	<i>Average - Social Networking</i>	<i>28,299.7</i>	<i>24,236.32</i>	<i>18.33</i>	<i>13.87</i>	<i>0.88</i>	<i>1.83</i>	<i>13,620.00</i>	<i>56.34</i>
09911.HK	Newborn Town	2,144.19	8.17	5.35	2.14	0.67	3,260.07	37.79	25.88

Source: Bloomberg, West Bull Securities

## Risk Factors

- The paying ratio or ARPPU drops after the replacement of live streamers
- The overseas expansion of BlueCity is slow, leading to a loss to the overseas business
- Unable to achieve breakeven / monetize the new games or social networking APPs
- The new games launched by the Group do not meet the expectation
- Costs incurred in the expansion of innovative business and HeeSay are higher than the expectation

## Financial Statement

PnL					Balance Sheet				
(RMB, mn)	2022 (A)	2023 (E)	2024 (E)	2025 (E)	(RMB, mn)	2022 (A)	2023 (E)	2024 (E)	2025 (E)
<b>Revenue</b>	<b>2,799.7</b>	<b>3,280.0</b>	<b>4,074.8</b>	<b>4,379.2</b>	PPE	122.2	140.8	150.0	160.9
<i>YoY growth</i>	<i>18.6%</i>	<i>17.2%</i>	<i>24.2%</i>	<i>7.5%</i>	Intangible assets	382.9	468.3	443.3	419.0
COGS	(1,741.8)	(1,634.8)	(2,086.0)	(2,216.9)	Others	238.5	132.2	163.6	211.4
<b>Gross profit</b>	<b>1,057.9</b>	<b>1,645.2</b>	<b>1,988.9</b>	<b>2,162.2</b>	<b>Non-current assets</b>	<b>743.6</b>	<b>741.4</b>	<b>756.9</b>	<b>791.3</b>
Other income	20.9	1.5	1.8	2.1	Inventories	-	-	-	-
Operating expenses	(809.5)	(1,136.6)	(1,401.0)	(1,497.2)	Trade receivables	164.9	187.0	254.7	295.5
<b>Operating profit</b>	<b>269.3</b>	<b>510.1</b>	<b>589.6</b>	<b>667.1</b>	Cash & cash equivalents	596.7	923.4	890.7	1,027.5
Finance expenses	(0.5)	(0.5)	(0.2)	(0.3)	Others	215.0	459.3	1,129.6	1,734.8
JV & Ass.	18.6	34.8	-	-	<b>Current assets</b>	<b>976.6</b>	<b>1,569.7</b>	<b>2,275.0</b>	<b>3,057.8</b>
<b>Profit before tax</b>	<b>287.4</b>	<b>544.4</b>	<b>589.4</b>	<b>666.8</b>	<b>Total assets</b>	<b>1,720.2</b>	<b>2,311.1</b>	<b>3,031.9</b>	<b>3,849.1</b>
Tax	(0.0)	(19.1)	(20.6)	(23.3)	LT borrowings	-	-	-	-
<b>Net profit</b>	<b>287.3</b>	<b>525.3</b>	<b>568.8</b>	<b>643.5</b>	Others	133.1	145.7	152.1	157.8
<i>YoY growth</i>	<i>N.A.</i>	<i>82.8%</i>	<i>8.3%</i>	<i>13.1%</i>	<b>Non-current liabilities</b>	<b>133.1</b>	<b>145.7</b>	<b>152.1</b>	<b>157.8</b>
					Trade payables	189.7	131.5	156.9	177.3
					ST borrowings	-	-	-	-
					Others	159.3	312.7	366.2	436.8
					<b>Current liabilities</b>	<b>349.1</b>	<b>444.3</b>	<b>523.2</b>	<b>614.1</b>
					<b>Total liabilities</b>	<b>482.2</b>	<b>589.9</b>	<b>675.2</b>	<b>771.9</b>
					Non-controlling interests	530.2	603.4	787.2	955.3
					Controlling interests	707.8	1,117.7	1,569.5	2,121.9
					<b>Total equities</b>	<b>1,238.0</b>	<b>1,721.1</b>	<b>2,356.7</b>	<b>3,077.2</b>

Cash Flow					Financial Ratio				
(RMB, mn)	2022 (A)	2023 (E)	2024 (E)	2025 (E)		2022 (A)	2023 (E)	2024 (E)	2025 (E)
Profit before tax	287.4	544.4	589.4	666.8	Gross margin	37.8%	50.2%	48.8%	49.4%
Finance expenses	-	-	-	-	Operating margin	9.6%	15.6%	14.5%	15.2%
Finance income	0.5	0.5	0.2	0.3	Net profit margin	10.3%	16.0%	14.0%	14.7%
D&A	59.6	53.0	47.0	47.9	Adj. EBITDA profit margin	13.4%	20.3%	17.6%	18.5%
Others	9.4	50.3	61.4	73.6	Return on Equity	27.7%	35.5%	27.9%	23.7%
Change in working capital	(44.2)	(227.2)	(85.1)	(102.0)	Return on Asset	17.2%	26.1%	21.3%	18.7%
<b>CFO</b>	<b>312.6</b>	<b>421.1</b>	<b>613.0</b>	<b>686.6</b>	Current ratio	279.8%	353.3%	434.8%	498.0%
					Quick ratio	277.6%	343.6%	425.1%	487.7%
CAPEX	(23.9)	(30.2)	(31.2)	(34.5)	Cash ratio	170.9%	207.9%	170.3%	167.3%
Others	(332.7)	(50.6)	(600.0)	(500.0)	Debt-to-Equity ratio	0.0%	0.0%	0.0%	0.0%
<b>CFI</b>	<b>(356.6)</b>	<b>(80.8)</b>	<b>(631.2)</b>	<b>(534.5)</b>	Net Debt-to-Equity ratio	-48.2%	-53.6%	-37.8%	-33.4%
					Inventory turnover days	-	-	-	-
Shares issuance	285.6	-	-	-	Receivable turnover days	25.1	24.0	23.5	26.5
Net borrowings	-	(0.0)	-	-	Payable turnover days	43.6	35.9	25.2	27.5
Interest paid	-	-	-	-					
Dividend paid	-	-	-	-					
Others	(425.2)	(13.6)	(14.5)	(15.4)					
<b>CFF</b>	<b>(139.6)</b>	<b>(13.6)</b>	<b>(14.5)</b>	<b>(15.4)</b>					
<b>FCFE</b>	<b>(85.7)</b>	<b>390.9</b>	<b>581.8</b>	<b>652.1</b>					
<b>FCFF</b>	<b>(85.7)</b>	<b>390.9</b>	<b>581.8</b>	<b>652.1</b>					

Source: Company data, West Bull Securities

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