

NetEase (NTES US)

1Q26 results: strong profit beat on margin expansion; solid game pipeline in 2H26E

NetEase announced 1Q26 financial results: total revenue was up by 6% YoY to RMB30.6bn, 4%/2% ahead of Bloomberg consensus/our estimate due to the solid performance of established game titles; non-GAAP net income was flattish YoY at RMB11.3bn, beating consensus/our estimate by 13%/4% thanks to the better-than-expected GPM expansion (+5.3ppt YoY) and prudent opex control. Looking ahead, several highly-anticipated game titles like *Sea of Remnants* and *ANANTA* are lined up for launch in 2H26/FY27, which we expect to drive acceleration of games revenue growth from 2H26E onwards. In view of the strong margin expansion, we raise our FY26-28E earnings forecast by 3-4%; but we trim our SOTP-derived target price to US\$155.0 (previous: US\$161.5) given the decline in game sector valuation. Maintain BUY on the quality game pipeline and resilient earnings growth outlook.

■ **1Q26 games revenue above expectation.** Games & related VAS revenue increased by 7% YoY to RMB25.7bn in 1Q26, 4% ahead of consensus estimate. Contract liabilities also maintained a solid growth of 23%/6% YoY/QoQ as of Mar 2026. Despite a lack of new titles in 1H26, evergreen titles maintained strong performance in 1Q26: 1) *Where Winds Meet* achieved record-high quarterly revenue and ranked the 2nd on Steam global top-selling chart following its overseas launch of version 1.6; 2) *Fantasy Westward Journey Online*'s peak concurrent users reached a new high of 3.9mn and also achieved record-high quarterly revenue thanks to the introduction of unlimited server; 3) *Identity V* sustained steady user engagement through continuous upgrade of its gameplay systems. Looking ahead, we expect several highly anticipated titles in the pipeline to drive revenue growth acceleration, including *Sea of Remnants* (3Q26E), *ANANTA* (to be announced), *Floatopia* (TBA) and *Infinite Borders: Three Kingdoms* (TBA) and *Blood Message* (TBA).

■ **Steady Music and Youdao businesses.** NetEase Cloud music revenue grew by 7% YoY to RMB1.98bn in 1Q26, mainly driven by the growth of online music revenue. Youdao revenue increased by 4% YoY to RMB1.35bn in 1Q26, primarily fuelled by the solid growth of online marketing and learnings services. Innovative businesses and others revenue declined by 5% YoY to RMB1.55bn in 1Q26, due to the e-commerce and ad business headwinds.

■ **Strong margin expansion on favourable mix shift and opex control.** Overall/games GPM expanded by 5.3/6.0ppt YoY to 69.4/74.8% in 1Q26, thanks to channel cost optimization and revenue mix shift to higher-margin PC games. The company's prudent expense control led to 33% decline in G&A expenses in 1Q26, and thus overall OPM was up by 5.2ppt YoY to 41.4% in 1Q26. Supported by the margin expansion, we expect NetEase to maintain resilient non-GAAP net income growth of 14% YoY in FY26E.

Earnings Summary

(YE 31 Dec)	FY24A	FY25A	FY26E	FY27E	FY28E
Revenue (RMB mn)	105,295	112,626	120,522	129,042	137,396
Gross margin (%)	62.5	64.3	67.0	67.2	67.4
Adjusted net profit (RMB mn)	33,510.6	37,343.7	42,567.5	46,321.6	49,133.5
EPS (Adjusted) (RMB)	52.35	58.83	66.14	71.76	76.12
Consensus EPS (RMB)	52.35	58.83	62.49	69.52	75.47
P/S (x)	4.7	4.4	4.1	3.9	3.6
P/E (x)	16.8	14.6	12.8	11.6	10.9

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price **US\$155.00**
 (Previous TP **US\$161.50**)
 Up/Downside **35.6%**
 Current Price **US\$114.34**

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Stock Data

Mkt Cap (US\$ mn)	73,134.7
Avg 3 mths t/o (US\$ mn)	48.0
52w High/Low (US\$)	159.34/109.26
Total Issued Shares (mn)	639.6

Source: FactSet

Shareholding Structure

William Lei Ding	45.5%
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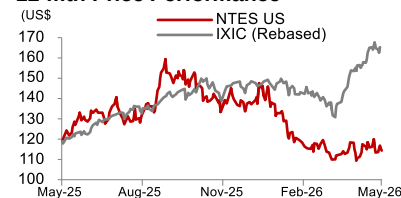
Source: Company data

Share Performance

	Absolute	Relative
1-mth	0.9%	-5.3%
3-mth	-3.4%	-15.9%
6-mth	-14.4%	-27.5%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: NetEase: earnings revision

RMB bn	Current			Previous			Change (%)		
	FY26E	FY27E	FY28E	FY26E	FY27E	FY28E	FY26E	FY27E	FY28E
Revenue	120.5	129.0	137.4	120.8	129.1	137.4	-0.2%	0.0%	0.0%
Gross profit	80.8	86.7	92.6	78.2	83.9	89.6	3.3%	3.3%	3.3%
Operating profit	43.9	47.8	51.9	39.8	43.8	47.7	10.2%	9.2%	8.8%
Adjusted net profit	42.6	46.3	49.1	41.4	44.7	47.5	2.7%	3.6%	3.4%
Adjusted EPS (RMB)	66.1	71.8	76.1	64.4	69.5	73.8	2.7%	3.3%	3.1%
Gross margin	67.0%	67.2%	67.4%	64.8%	65.0%	65.2%	2.2 ppt	2.1 ppt	2.2 ppt
Operating margin	36.4%	37.1%	37.8%	33.0%	33.9%	34.7%	3.4 ppt	3.1 ppt	3.1 ppt
Adjusted net margin	35.3%	35.9%	35.8%	34.3%	34.6%	34.6%	1.0 ppt	1.3 ppt	1.2 ppt

Source: CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

RMB bn	CMBIGM			Consensus			Diff (%)		
	FY26E	FY27E	FY28E	FY26E	FY27E	FY28E	FY26E	FY27E	FY28E
Revenue	120.5	129.0	137.4	120.1	130.6	140.3	0.3%	-1.2%	-2.1%
Gross profit	80.8	86.7	92.6	77.8	85.4	92.1	3.8%	1.5%	0.5%
Operating profit	43.9	47.8	51.9	39.0	44.2	48.6	12.4%	8.2%	6.8%
Adjusted net profit	42.6	46.3	49.1	40.3	45.2	48.8	5.7%	2.5%	0.7%
Adjusted EPS (RMB)	66.1	71.8	76.1	62.5	69.5	75.5	5.8%	3.2%	0.9%
Gross margin	67.0%	67.2%	67.4%	64.8%	65.4%	65.7%	2.2 ppt	1.7 ppt	1.7 ppt
Operating margin	36.4%	37.1%	37.8%	32.5%	33.8%	34.6%	3.9 ppt	3.2 ppt	3.2 ppt
Adjusted net margin	35.3%	35.9%	35.8%	33.5%	34.6%	34.8%	1.8 ppt	1.3 ppt	1.0 ppt

Source: Bloomberg, CMBIGM estimates

Figure 3: NetEase: key financial data forecasts

(RMB mn)	1Q25	2Q25	3Q25	4Q25	1Q26	Cons.	Diff%
Online games revenue	24,048	22,806	23,328	21,967	25,713	24,708	4.1%
YoY%	12.1%	13.7%	11.8%	3.4%	6.9%		
As % of total revenue	83.4%	81.8%	82.3%	79.7%	84.1%		
Youdao revenue	1,298	1,418	1,629	1,565	1,348	1,422	-5.2%
YoY%	-6.7%	7.2%	3.6%	16.8%	3.8%		
As % of total revenue	4.5%	5.1%	5.7%	5.7%	4.4%		
Cloud Music revenue	1,858	1,969	1,964	1,968	1,981	1,992	-0.5%
YoY%	-8.4%	-3.5%	-1.8%	4.7%	6.6%		
As % of total revenue	6.4%	7.1%	6.9%	7.1%	6.5%		
Innovative businesses	1,624	1,699	1,439	2,047	1,549	1,578	-1.8%
YoY%	-17.6%	-17.8%	-18.9%	-10.4%	-4.6%		
As % of total revenue	5.6%	6.1%	5.1%	7.4%	5.1%		
Total revenue	28,829	27,892	28,359	27,547	30,591	29,514	3.7%
YoY%	7.4%	9.4%	8.2%	3.0%	6.1%		
Gross profit margin (%)	64.1%	64.7%	64.1%	64.2%	69.4%	64.6%	4.7ppt
S&M expenses ratio (%)	9.4%	12.8%	15.7%	14.1%	11.2%		
R&D expenses ratio (%)	15.2%	15.6%	16.0%	16.1%	14.7%		
Non-GAAP net profit	11,237	9,532	9,502	7,073	11,275	10,003	12.7%
YoY%	32.0%	21.9%	26.7%	-26.9%	0.3%		
Non-GAAP NPM (%)	39.0%	34.2%	33.5%	25.7%	36.9%		

Source: Company data, Bloomberg, CMBIGM

We use sum-of-the-parts (SOTP) valuation methodology to value NetEase's four main business segments. Our SOTP-derived target price is US\$155.0, comprising:

- 1) US\$137.2 for the online game business (88.5% of total valuation), based on 15x 2026E EV/EBIT, which is at a premium to the industry average (14x) reflecting NetEase's strong game pipeline in 2H26/FY27.
- 2) US\$0.6 for Youdao (0.4% of total valuation), based on 0.7x 2026E EV/revenue, on par with the industry average;
- 3) US\$2.2 (1.4% of total valuation) for the NetEase Cloud Music business, based on 1.9x 2026E EV/revenue, on par with the industry average;
- 4) US\$1.2 (0.8% of total valuation) for the innovative businesses and others, based on 0.8x 2026E EV/revenue, on par with the industry average;
- 5) US\$13.9 for net cash.

Figure 4: NetEase: SOTP Valuation

(RMBmn)	Valuation basis	Multiple (x)	2026E sales	2026E EBIT	Valuation	Shareholding (%)	Valuation to NetEase	Valuation per ADS (US\$)
Online games	EV/EBIT	15.0	99,445	39,778	596,668	100.0%	596,668	137.2
Youdao	EV/revenue	0.7	6,204		4,343	57.1%	2,480	0.6
Cloud Music	EV/revenue	1.9	8,303		15,775	59.4%	9,370	2.2
Innovative businesses	EV/revenue	0.8	6,570		5,256	100.0%	5,256	1.2
Enterprise value							613,775	
Net cash							60,413	13.9
Equity value							674,188	
RMB/US\$							6.8	
Valuation (US\$mn)							99,145	
No. of ADSs (mn)							640	
Value per ADS (US\$)							155.0	

Source: Company data, CMBIGM estimates

Figure 5: Peer comparison: online games

Company	Ticker	Price (Local)	EBIT growth (YoY %)		EV/EBIT (x)	
			FY26E	FY27E	FY26E	FY27E
Tencent	700 HK	455.2	13	12	13	12
Electronic Arts	EA US	201.6	24	6	20	19
Nintendo	7974 JP	7,240.0	24	11	18	16
Bandai Namco	7832 JP	3,721.0	(12)	7	11	10
Perfect World	002624 CH	14.8	97	22	13	10
37 Interactive	002555 CH	20.8	5	11	12	11
Average EV/EBIT					14	13

Source: Bloomberg consensus estimates, CMBIGM

Note: data as of market close on 20 May

Figure 6: Peer comparison: education, online music, and e-commerce

Company	Ticker	Price	Revenue growth (YoY %)		EV/revenue (x)	
		(Local)	FY26E	FY27E	FY26E	FY27E
Education						
New Oriental	EDU US	49.9	14	12	0.8	0.7
TAL Education	TAL US	10.5	32	24	1.2	1.0
Gaotu	GOTU US	1.9	17	14	0.1	0.1
Average					0.7	0.6
Community						
TME	TME US	9.2	11	9	2.0	1.8
Spotify	SPOT US	433.3	12	14	3.5	3.1
BiliBili	BILI US	18.3	11	10	1.2	1.1
Kuaishou	1024 HK	47.7	6	7	1.1	1.0
Average					1.9	1.7
E-commerce						
Alibaba	BABA US	134.5	10	12	1.6	1.4
JD	JD US	32.5	8	6	0.2	0.2
Pinduoduo	PDD US	98.2	15	13	1.1	1.0
Vipshop	VIPS US	14.2	1	5	0.3	0.2
Average					0.8	0.7

Source: Bloomberg consensus estimates, CMBIGM

Note: data as of market close on 20 May

Financial Summary

INCOME STATEMENT	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec (RMB mn)						
Revenue	103,468	105,295	112,626	120,522	129,042	137,396
Cost of goods sold	(40,405)	(39,488)	(40,224)	(39,771)	(42,382)	(44,839)
Gross profit	63,063	65,807	72,402	80,751	86,660	92,557
Operating expenses	(35,354)	(36,223)	(36,567)	(36,880)	(38,842)	(40,669)
Selling expense	(13,969)	(14,148)	(14,620)	(15,668)	(16,775)	(17,862)
Admin expense	(4,900)	(4,551)	(4,228)	(3,013)	(3,226)	(3,435)
R&D expense	(16,485)	(17,525)	(17,719)	(18,199)	(18,840)	(19,373)
Operating profit	27,709	29,584	35,835	43,871	47,818	51,888
Investment gain/loss	1,307	355	732	219	176	53
Other gains/(losses)	1,054	602	1,087	439	0	0
Interest income	4,120	4,921	3,953	3,603	3,157	2,299
Foreign exchange gain/loss	(133)	255	(776)	(622)	0	0
Pre-tax profit	34,057	35,718	40,830	47,511	51,151	54,240
Income tax	(4,700)	(5,461)	(6,033)	(8,077)	(8,184)	(8,678)
After tax profit	29,357	30,256	34,798	39,434	42,966	45,561
Minority interest	59	(559)	(1,038)	(683)	0	0
Net profit	29,417	29,698	33,760	38,751	42,966	45,561
Adjusted net profit	32,608	33,511	37,344	42,567	46,322	49,134

BALANCE SHEET	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec (RMB mn)						
Current assets	142,693	153,325	180,615	213,638	249,172	285,066
Cash & equivalents	21,429	51,383	47,168	68,945	92,148	114,675
Restricted cash	2,777	3,086	4,319	4,535	4,762	5,000
Account receivables	6,422	5,669	5,338	5,598	5,874	6,129
Inventories	695	572	689	681	726	768
Prepayment	6,077	6,417	7,658	8,031	8,427	8,793
ST bank deposits	100,856	75,441	92,639	101,903	112,094	123,303
Other current assets	4,436	10,756	22,804	23,944	25,141	26,398
Non-current assets	43,232	42,667	40,800	37,965	35,533	33,430
PP&E	8,075	8,520	8,425	8,332	8,239	8,147
Other non-current assets	35,157	34,147	32,374	29,634	27,294	25,282
Total assets	185,925	195,992	221,415	251,603	284,704	318,496
Current liabilities	53,842	49,668	52,369	55,983	59,923	62,747
Short-term borrowings	19,240	11,805	6,384	8,532	9,225	8,921
Account payables	881	721	643	636	678	717
Tax payable	2,572	2,759	3,874	4,146	4,439	4,726
Other current liabilities	18,219	19,982	25,404	26,788	28,657	30,477
Accrued expenses	12,930	14,401	16,063	15,882	16,925	17,906
Non-current liabilities	3,998	3,830	3,942	4,112	4,397	4,672
Other non-current liabilities	3,998	3,830	3,942	4,112	4,397	4,672
Total liabilities	57,841	53,497	56,311	60,095	64,320	67,419
Total shareholders equity	124,286	138,686	160,296	186,017	214,894	245,587
Minority interest	3,798	3,809	4,808	5,491	5,491	5,491
Total equity and liabilities	185,925	195,992	221,415	251,603	284,704	318,496

CASH FLOW	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	34,057	35,718	40,830	47,511	51,151	54,240
Depreciation & amortization	3,055	2,418	2,247	4,213	4,166	4,119
Tax paid	(4,700)	(5,461)	(6,033)	(8,077)	(8,184)	(8,678)
Change in working capital	376	3,652	8,721	842	2,530	2,465
Others	2,543	3,351	4,973	0	0	0
Net cash from operations	35,331	39,677	50,740	44,488	49,663	52,145
Investing						
Capital expenditure	(4,266)	(2,192)	(2,007)	(3,998)	(3,955)	(3,914)
Net cash from investing	(17,043)	17,916	(33,181)	(11,616)	(12,837)	(14,208)
Financing						
Dividend paid	(8,014)	(11,165)	(13,826)	(11,830)	(12,890)	(13,668)
Net borrowings	(8,305)	(7,476)	(5,799)	2,147	694	(304)
Proceeds from share issues	0	0	0	0	0	0
Others	(5,148)	(8,694)	(536)	(1,200)	(1,200)	(1,200)
Net cash from financing	(21,467)	(27,336)	(20,160)	(10,883)	(13,396)	(15,173)
Net change in cash						
Cash at the beginning of the year	24,889	21,429	51,383	47,168	68,945	92,148
Exchange difference	(202)	11	(382)	0	0	0
Others	0	0	0	0	0	0
Cash at the end of the year	21,429	51,383	47,168	68,945	92,148	114,675
GROWTH	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
Revenue	7.2%	1.8%	7.0%	7.0%	7.1%	6.5%
Gross profit	19.5%	4.4%	10.0%	11.5%	7.3%	6.8%
Operating profit	41.2%	6.8%	21.1%	22.4%	9.0%	8.5%
Net profit	49.2%	1.0%	13.7%	14.8%	10.9%	6.0%
Adj. net profit	43.0%	2.8%	11.4%	14.0%	8.8%	6.1%
PROFITABILITY	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
Gross profit margin	60.9%	62.5%	64.3%	67.0%	67.2%	67.4%
Operating margin	26.8%	28.1%	31.8%	36.4%	37.1%	37.8%
Adj. net profit margin	31.5%	31.8%	33.2%	35.3%	35.9%	35.8%
Return on equity (ROE)	25.7%	22.6%	22.6%	22.4%	21.4%	19.8%
GEARING/LIQUIDITY/ACTIVITIES	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
Net debt to equity (x)	(0.8)	(0.8)	(0.8)	(0.9)	(0.9)	(0.9)
Current ratio (x)	2.7	3.1	3.4	3.8	4.2	4.5
Receivable turnover days	22.7	19.7	17.3	17.0	16.6	16.3
Payable turnover days	8.0	6.7	5.8	5.8	5.8	5.8
VALUATION	2023A	2024A	2025A	2026E	2027E	2028E
YE 31 Dec						
P/E	17.0	16.8	14.6	12.8	11.6	10.9
P/E (diluted)	17.2	16.9	14.8	12.9	11.7	11.0
P/B	4.0	3.6	3.1	2.7	2.3	2.0

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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