

Corporate Flash

# China Mobile Games and Cultural Investment 8081 HK

## Clear business model bodes well for a constructive year

- The company will acquire additional 6.0% issued shares of Mighty Eight Investment Ltd. with the cash of HKD52.6m
- New shares (approximately 9.9% of total shares upon completion the placement) will be issued at the price of HKD0.134 per share
- Cooperative agreement with Youle Holdings Ltd., Mighty Eight Investment Ltd., Shanghai Wangyan Network Technology and Shanghai Zhiqu Advertisement will bring significant profit to CMGC

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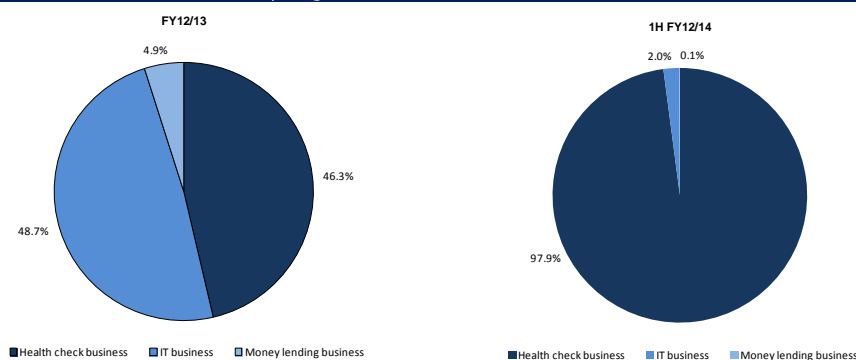
**Stock Data (8081 HK)**

Rating	Not Rated
Price (HKD)	0.187
Target Price (HKD)	n.a.
12m Price Range (HKD)	0.108-0.254
Market cap. (HKD m)	356.3
Daily t/o (HKD m)	5.6
Free float (%)	76.3
Source: Bloomberg	

**Background of CMGC.** China Mobile Games and Cultural Investment Ltd. (“CMGC”) is currently engaged in three areas of business: i) IT business which provides consultancy, technical support, systems integration, development and sales of relevant hardware and software products; ii) money lending business; and iii) provision of medical diagnostic and health check services. The medical business is a new business for the company, as it was kicked off after Lucky Key Group – a healthcare company engaged in the provision of medical diagnostic and health check services – was entirely acquired by the company in FY12/13.

IT business used to be the company’s major source of revenue, which accounted for 95.6% of its total revenue in FY12/12. However, after the acquisition of Lucky Key Group, medical business became its main revenue source. In FY12/13, revenue from the provision of medical diagnostic and health check services accounted for 46.3% of its total revenue for the year. The proportion increased further to 97.9% in 1H FY12/14. (See Figure 1). However, it is expected that sales contribution from the medical segment will go down in the future, as the company is transforming itself to a mobile game focused investment entity.

Figure 1. Revenue breakdown by segment in FY12/13 and 1H FY12/14



Source: Company data

On 13 Aug 2014, the company announced that it would place 209,592,000 shares at the price of HKD0.134 per share. Compared with the average closing price of HKD0.165 per share for the five consecutive trading days prior to the placing, a discount approximately 18.9% is provided in the placement. After the new placement, other public shareholders will account for approximately 77.1% of totals shares in CMGC. (See Figure 2)

**Figure 2. The shareholder structure of CMGC**

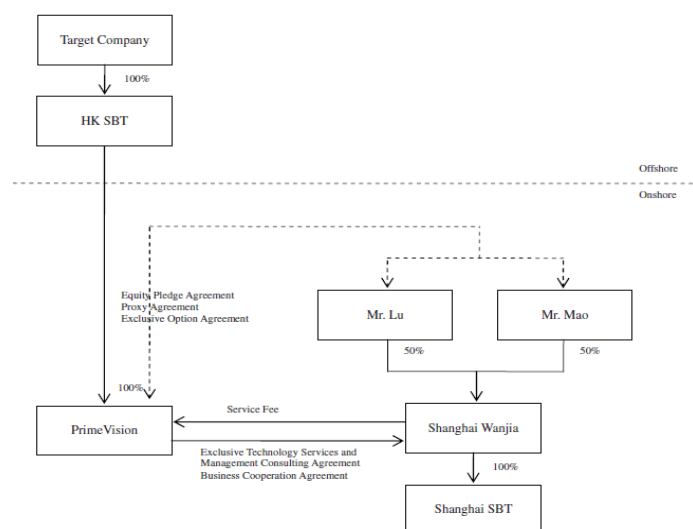
Shareholders	Before completion of the placement	After completion of the placement
China New Economy Fund Ltd	14.4%	13.0%
The placees	-	9.9%
Other public shareholders	85.6%	77.1%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>

Source: Company data

**Investment in Youle Holdings Ltd.** On 28 May 2014, CMGC announced that Timely Investments (a wholly-owned subsidiary of CMGC) entered into an S&P agreement with Youle Holdings Ltd. Under the agreement, Timely Investments will invest approximately RMB4.2m to get 12.5% of equity interest in Youle, which was completed on 14 August 2014. Youle Holdings Ltd. is a company established in Samoa and indirectly holds Shanghai WildHammer Digital Technology Co. Ltd (WildHammer). (上海蠻錘數碼科技有限公司), which was established in the PRC and principally engaged in the technological development of computer and digital products, information technology, technical services, development of computer and digital products, information technology, development and sales of software and hardware, and webpage design. Not only WildHammer's shares have been partly controlled by CMGC, but also its operations. On 28 May 2014, Golden Weapon (金矛有限公司) (a wholly-owned subsidiary of CMGC) also entered into the Licence Agreement with WildHammer, under which Golden Weapon has the right to authorise or appoint a third party to perform its obligation under the agreement. Meanwhile, Golden Weapon and WildHammer will share the monthly income from the service fees paid by the users of the games. WildHammer has cooperated with Shanghai Ji Ku Network Technology Co. Ltd. (上海極酷網絡科技有限公司) and Shanghai Re Zhua Digital Technology Co. Ltd. (上海熱爪數碼科技有限公司). On 14 August 2014, CMGC announced that WildHammer was granted with the worldwide exclusive licences to operate mobile online games namely "National Martial Arts Game" (developed by Shanghai Ji Ku) and "Monster Master" (developed by Shanghai Re Zhua). We think the cooperation with WildHammer can help CMGC become one of the leading players in the mobile-online game industry.

**Investment in Mighty Eight.** In January 2014, CMGC entered into an S&P agreement with Century Grand (世鴻控股有限公司) Holdings Ltd.. Under the agreement, the former will acquire from the latter 5.0% of equity interest in Mighty Eight Investment Ltd. (盛八投資有限公司), at a consideration of HKD43.6m. In April 2014, the company entered into another agreement regarding an acquisition of another 13.0% equity shares of Mighty Eight, with a consideration of HKD114.0m. On 13 Aug 2014, CMGC announced that it will acquire an additional 6.0% share of Mighty Eight Investment Ltd. with the total cash of HKD52.6m. Upon completing the deal, CMGC will hold 24.0% shares of Mighty Eight Investment Ltd.. Mighty Eight is a company incorporated in Samoa with limited liability and controlled Shanghai SBT through an "Exclusive Technology Services and Management Consulting Agreement Business Cooperation Agreement". (See Figure 3).

**Figure 3. Relationship between Mighty Eight and Shanghai SBT**



\*The Target Company here refers to Mighty Eight Investment Ltd.

Source: Company data

Shanghai SBT is primarily engaged in the operation and distribution of its self-development games in different regions with various language versions. The group launched its original SanGuo-Mobile (named as 手機三國 in Android version and 指戰三國 in iOS version) in 2011, which gained popularity in the Greater China and South East Asia regions. In 2012 and 2013, it

launched Keitaisangoku (named as 攜帶三國 in Android version and 三國神將傳 in iOS version) in Japan and Titans Mobile in North America regions in 2012 and Phonesamgukji in Korea 2013.

Notwithstanding, the group have actively developed several games in 2014. In March 2014, it launched a new mobile game, namely, Voyage-Mobile (手機大航海) in various digital distribution platforms for mobile application software, including Google Play, in South East Asia markets. It expects to launch a Sanguo themed card game-“Qcard-Sanguo” with a unique playing model and game features in the third quarter of 2014. Other than game development, it is also actively negotiating with certain game developers in the PRC to publish its developed games to other regions and expects to publish several games in 2014. Moreover, it will launch a new mobile-online game called “NBA Hero” in the 4Q FY12/14. “NBA Hero” will be established upon the cooperation with the National Basketball Association (NBA) governing body and such cooperation will last at least three years.

It deserves our attention that Shanghai SBT has encountered significant growth in recent years. For example, in FY12/13, the company recorded the revenue of RMB111.5m, an 89.0% YoY increase; gross profit of RMB96.4m, a 110.0% YoY increase; and profit attributable to shareholders of RMB57.9m, a YoY increase of 119.3%. Accordingly, we think CMGC will benefit from the growth of Shanghai SBT and encounter outstanding growth in the following years.

**Potential Capital Injection to Shanghai Wangyan Network Technology.** In July 2014, the company has entered into an MOU regarding a purchase of 20.0% equity interest in Shanghai Wang Yan Network Technology Co., Ltd. (Shanghai Wangyan), (上海網岩網路科技有限公司), with the capital of RMB3.0m. Meanwhile, CMGC has also received option from the above MOU, in which CMGC has the right to subscribe further shares in Shanghai Wangyan so that the maximum shares controlled by CMGC will be increased to 49.0%. The exercise price and period has not been determined.

Shanghai Wang Yan is a company engaged in the technology development of the IT products, technology transfer, technology advisory, technology services, development and sale of computer software, computer network engineering, repair and maintenance of computer auxiliary equipment, installation and sale of electronic products and parts. It has commenced the design and development of a new RPG mobile-online game, which is targeted to be launched in 4Q FY12/14. It is worth noting that one of the senior management of Shanghai Wangyan has been involved in the operation, management and marketing of “Kart Rider” (跑跑卡丁車). We believe the acquisition of Shanghai Wang Yan will not only strengthen CMGC’s position in the mobile game industry, but will also provide another source of revenue to the company.

Currently, CMGC has exposed itself to seven mobile games, namely Sanguo-Mobile, Qcard-Sanguo, VoyageMobile, NBA Hero, National Martial Arts Game, The Rune Run and Monster Master. Three of them have already been launched while four of them will be launch by the end of 2014. (See Figure 4).

**Figure 4. Existing games/games under development from Mighty Eighty or its subsidiaries and WildHammer**

Mighty Eighty or its subsidiaries		WildHammer	
Name	Information	Name	Information
Sanguo-Mobile	It has been developed by Mighty Eighty or its subsidiaries and got launched in 2011	National Martial Arts Game	It will be operated by WildHammer and will be launched in 4Q 2014
Qcard-Sanguo	It has been developed by Mighty Eighty or its subsidiaries and will be launched in 3Q 2014	The Rune Rush	It has been developed by WildHammer and got launched in August 2014
VoyageMobile	It has been developed by Mighty Eighty or its subsidiaries and got launched in 1Q 2014	Monster Master	It will be operated by WildHammer and will be launched in 4Q 2014
NBA Hero	It has been developed by Mighty Eighty or its subsidiaries and will be launched in 4Q 2014		

Source: Company data

**Potential capital injection to Shanghai Zhiqiu Advertisement.** On July 27 CMGC announced that Investor (投資者) (a wholly-owned subsidiary of CMGC) has signed the Capital Injection Agreement with Shanghai Zhiqiu Advertisement Co. Ltd., a company engaged in the business of mobile game integral marketing services. Under this agreement, Investor will inject RMB530,000 to Shanghai Zhiqiu Advertisement, after which CMGC will hold 51.0% share of Shanghai Zhiqiu Advertisement. We think such capital injection will bring good opportunities for CMGC to develop their mobile-online game business and help CMGC become an integrated mobile game investment entity. Specifically, after future mobile games being released in 2H FY12/14 and FY12/15, Shanghai Zhiqiu will be involved in the marketing process.

**Valuation.** Given the loss CMGC recorded in recent years, it has no P/E valuation. However, we think positive profit will be recorded after completing its transformation to a mobile game company.

As for the company's HK-listed peers, there are three companies that are engaged in mobile game business in HK and China. These companies include Boyaa Interactive International (0434 HK), Forgame Holdings Ltd. (0484 HK) and IGG (8002 HK) On average, these companies are trading at a trailing P/E of 49.4x for 2013 and a prospective P/E of 24.7x for 2014. As for the company's China-listed peers, there are also three companies that are engaged in mobile game business. These companies include Ourpalm (300315 CH), Shenzheng ZQGAME (300052 CH) and Beijing Bewinner Communications (002148 CH) On average, these companies are trading at a trailing P/E of 117.4x for 2013 and a prospective P/E of 48.2x for 2014.

Excluding China Mobile Games and Cultural Investment, the above-mentioned companies cumulatively on average trading at a trailing P/E of 75.2x for 2013 and a prospective P/E of 31.3x for 2014.

**Figure 5. Peer comparison**

Company	Ticker	Mkt Cap (HKD m)	3M avg turnover (HKD m)	2013 P/E (x)	2014E P/E (x)	P/book (x)	Net profit (RMB m)	ROIC (%)	ROE (%)	ROA (%)	Dvd Yield (%)	Net Debt/ Total Equity
<b>China Mobile Games and Cultural Investment</b>	<b>8081 HK</b>	<b>356.32</b>	<b>5.62</b>	<b>-</b>	<b>-</b>	<b>1.46</b>	<b>-8.85</b>	<b>-</b>	<b>-8.77</b>	<b>-7.14</b>	<b>0.00</b>	<b>(0.26)</b>
<b>HK-listed peers</b>												
Boyaa Interactive International	434 HK	6805.01	19.79	16.62	18.22	4.39	135.51	19.05	17.86	14.39	1.23	(1.10)
Forgame Holdings Ltd	484 HK	2268.90	14.79	-	42.32	1.29	-475.40	-	-	-44.99	0.00	(0.90)
IGG	8002 HK	6588.98	40.99	80.07	11.56	6.25	6.95	46.97	-	8.03	0.32	(1.00)
<b>Average*</b>		<b>5220.96</b>	<b>25.19</b>	<b>48.34</b>	<b>24.04</b>	<b>3.98</b>	<b>(110.98)</b>	<b>33.01</b>	<b>17.86</b>	<b>(7.52)</b>	<b>0.52</b>	<b>(1.00)</b>
<b>China-listed peers</b>												
Ourpalm Co Ltd	300315 CH	25866.67	452.34	110.12	44.72	11.72	153.62	9.33	12.77	10.81	0.22	(0.40)
Shenzhen ZQGAME	300052 CH	9730.69	362.49	145.24	52.14	7.98	51.03	-	5.61	4.55	-	(0.30)
Beijing Bewinner Communications	002148 CH	8055.27	310.48	119.85	57.47	6.26	56.31	-	6.13	5.92	-	(0.30)
<b>Average*</b>		<b>14550.88</b>	<b>375.10</b>	<b>125.07</b>	<b>51.44</b>	<b>8.65</b>	<b>86.98</b>	<b>9.33</b>	<b>8.17</b>	<b>7.09</b>	<b>0.22</b>	<b>(0.33)</b>
<b>Average of all*</b>		<b>9885.92</b>	<b>200.15</b>	<b>94.38</b>	<b>37.74</b>	<b>6.31</b>	<b>(12.00)</b>	<b>25.12</b>	<b>10.59</b>	<b>(0.21)</b>	<b>0.44</b>	<b>(0.67)</b>

\*The Average figures does not include CMGC

Source: Bloomberg

**Figure 6. Per share items**

	FY12/11	FY12/12	FY12/13	1H FY12/14
EPS (HKD cents)				
- Basic	(26.98)	(12.78)	(1.50)	(0.87)
- Diluted	(26.98)	(12.78)	(1.50)	(0.87)
DPS (HKD)	-	-	-	-
BVPS (HKD)	0.0	0.2	0.1	0.1

Source: Company data

**Figure 7. Ratio analysis**

	FY12/11	FY12/12	FY12/13	1H FY12/14
<b>Growth (YoY)</b>				
Revenue	-16.7%	393.5%	-6.6%	-8.5%
Net loss	-81.8%	-19.2%	-58.3%	267.0%
<b>Margins</b>				
Net profit margin	-120.9%	-19.8%	-8.8%	-35.5%
<b>Other ratios</b>				
Return on average assets	-90.4%	-22.1%	-5.2%	-14.1%
Return on average equity	-118.0%	-30.5%	-6.4%	-15.9%
Dividend payout ratio	-	-	-	-
<b>Valuation measures</b>				
P/E (x)	-	-	-	-
P/B (x)	8.3	0.8	1.2	1.3
Dividend yield	-	-	-	-

Source: Company data

**Figure 8. Income statement (HKD m)**

	FY12/11	FY12/12	FY12/13	1H FY12/14
<b>Revenue</b>	<b>21.6</b>	<b>106.6</b>	<b>99.6</b>	<b>91.1</b>
Cost of inventories sold/services	(17.4)	(99.6)	(54.5)	(14.3)
Employee benefits expenses	-	(7.0)	(30.1)	(48.6)
Depreciation	-	(0.4)	(8.7)	(15.0)
Other operating expense	-	(17.1)	(21.2)	(25.2)
Others	(29.8)	(0.9)	9.8	1.9
Finance costs	(0.6)	(2.7)	(4.0)	(0.7)
Loss before income taxation	(26.1)	(21.1)	(9.2)	(10.9)
Income tax	-	-	(0.4)	(0.1)
Fair value loss on available-for-sale investment	-	-	-	(21.6)
Total comprehensive loss for the period	(26.1)	(21.1)	(9.6)	(32.5)
<b>Loss attributable to shareholders</b>	<b>(26.1)</b>	<b>(21.1)</b>	<b>(8.8)</b>	<b>(32.3)</b>

Source: Company data

Figure 9. Balance sheet (HKD m)

	FY12/11	FY12/12	FY12/13	1H FY12/14
<b>Non-current assets</b>				
Property, plant and equipment	6.3	5.9	35.8	25.2
Investment in an associate	-	-	1.6	4.2
Others	0.4	20.4	39.9	65.4
<b>Total non-current assets</b>	<b>6.7</b>	<b>26.3</b>	<b>77.3</b>	<b>94.8</b>
<b>Current assets</b>				
Inventories	0.1	-	2.3	2.0
Debtors, deposits and prepayment	2.4	19.5	41.5	34.0
Cash and bank balances	11.8	77.2	42.1	149.8
Others	10.0	37.1	14.2	0.0
<b>Total current assets</b>	<b>24.3</b>	<b>133.8</b>	<b>100.1</b>	<b>185.8</b>
<b>Current liabilities</b>				
Creditors, accruals and other payables	(6.3)	(7.0)	(13.3)	(12.2)
Others	0.0	0.0	(1.4)	(24.0)
<b>Total current liabilities</b>	<b>(6.3)</b>	<b>(7.0)</b>	<b>(14.7)</b>	<b>(36.2)</b>
<b>Non-current liability</b>				
Convertible note	-	(39.6)	-	-
Deferred tax liability	-	-	0.0	0.0
<b>Total non-current liability</b>	<b>-</b>	<b>(39.6)</b>	<b>0.0</b>	<b>0.0</b>
<b>Net assets</b>	<b>24.8</b>	<b>113.5</b>	<b>162.7</b>	<b>244.4</b>
<b>Equity</b>				
Share capital	12.1	55.8	93.1	190.5
Share premium and reserves	12.7	57.8	68.8	53.3
Others	0.0	(0.1)	0.8	0.6
<b>Total Equity</b>	<b>24.8</b>	<b>113.5</b>	<b>162.7</b>	<b>244.4</b>

Source: Company data

Figure 10. Cash flow statement (HKD m)

	FY12/11	FY12/12	FY12/13	1H FY12/14
<b>Operating activities</b>				
Cash generated from operations	(29.7)	(53.4)	38.4	-
Tax paid	0.0	-	(0.2)	-
<b>Net cash generated from operating activities</b>	<b>(29.7)</b>	<b>(53.4)</b>	<b>38.2</b>	<b>11.0</b>
<b>Net cash flow from investing activities</b>	<b>(10.2)</b>	<b>(26.7)</b>	<b>(84.0)</b>	<b>(40.7)</b>
<b>Net cash flow from financing activities</b>	<b>30.4</b>	<b>145.5</b>	<b>13.3</b>	<b>137.3</b>
Net increase in cash and cash equivalent	(9.5)	65.4	(32.4)	107.7
Cash and cash equivalents at the beginning of the year	21.3	11.8	77.2	42.1
<b>Cash and cash equivalents at the end of the year</b>	<b>11.8</b>	<b>77.2</b>	<b>44.8</b>	<b>149.8</b>

Source: Company data

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