

Sea Ltd (SE US)

Tencent pares stake

BUY

Share Price	USD 195.32
12m Price Target	USD 379.00 (+94%)
Previous Price Target	USD 379.00

Stake sale is unrelated to fundamentals; BUY

Sea's share price fell 11.4% to USD197.84 following Tencent's decision to pare its stake in the company from 21.3% to 18.7%. Sentiment for pre-earnings stocks tend to be fragile and this move adds to the overhang. Nevertheless, this does not take away long-term growth prospects given Shopee's position as ASEAN's top e-commerce player and potential from Garena Free Fire MAX. Maintain BUY and SOTP-TP of USD379.

Tencent will continue to participate in Sea's growth

According Reuters, Tencent sold the shares at USD208 each to raise USD3b. This represents a 6.9% discount to the previous close of USD223.31. Tencent intends to use the proceeds raised to fund other investments, while retaining a majority of its stake to benefit from Sea's future growth. Tencent is also restricted from selling further Sea shares for the next 6 months.

Share price could be volatile in the near term...

Tencent's share sale is likely to create short-term sentiment overhang. In the past 3 months, Sea's share price has declined by 39%, likely due to i) concerns over normalising growth for Garena Free Fire, as well as ii) rotation away from pre-earnings growth stocks. We believe a near-term risk to the share price is wider-than-expected losses, especially as Sea deploys the USD6b it raised in 2021 to fund growth.

... however, our longer-term conviction is unchanged

That said, our optimism towards the stock's longer-term performance remains unchanged. Balance sheet is robust with c.USD12b of cash in FY21-23E (FY21E EBITDA loss: USD1.3b). Shopee continues to be the top ranked shopping app by MAU and total time spent in ASEAN (incl. Indonesia) and Taiwan, and e-commerce penetration in ASEAN remains low as compared to mature countries like China and the US. Meanwhile, while Free Fire's growth is normalising post-Covid, we expect Free Fire MAX to continue delivering growth, largely from new markets. These are likely to be from more affluent countries (which may drive up ARPPU) as Free Fire is already a top grossing mobile battle royale game in emerging markets like ASEAN, LatAm and India. Slower-than-expected e-commerce GMV, digital entertainment bookings, and revenue growth is the key risk to our view.

FYE Dec (USD m)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue	2,175	4,376	9,662	14,685	19,799
EBITDA	(770)	(1,123)	(1,228)	(581)	1,514
Core net profit	(1,463)	(1,618)	(1,948)	(1,712)	(56)
Core FDEPS (cts)	(315.8)	(327.5)	(336.1)	(301.2)	(9.6)
Core FDEPS growth(%)	nm	nm	nm	nm	nm
Net DPS (cts)	0.0	0.0	0.0	0.0	0.0
Core FD P/E (x)	nm	nm	nm	nm	nm
P/BV (x)	16.0	29.1	18.5	23.7	21.7
Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0
ROAA (%)	(39.4)	(20.6)	(14.3)	(9.9)	(0.3)
EV/EBITDA (x)	nm	nm	nm	nm	66.5
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	na	na	na
MKE vs. Consensus (%)	-	-	na	na	na

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Company Description

Sea is an internet company that has businesses in gaming, e-commerce and digital financial services.

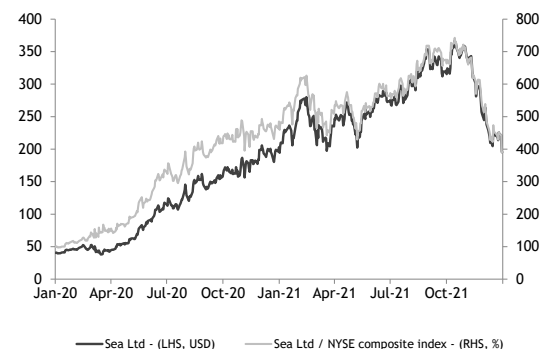
Statistics

52w high/low (USD)	366.99/194.37
3m avg turnover (USDm)	240.7
Free float (%)	100.0
Issued shares (m)	555
Market capitalisation	USD108.3B
	USD108.3B

Major shareholders:

T.Rowe Price Associates	8.4%
Gang Ye	8.1%
Sands Capital Management	6.7%

Price Performance



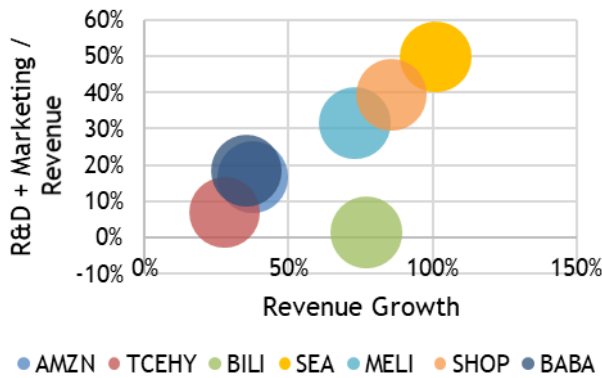
	-1M	-3M	-12M
Absolute (%)	(23)	(39)	(4)
Relative to index (%)	(27)	(42)	(20)

Source: FactSet

Value Proposition

- Sea is a Singapore-founded internet company with businesses in digital entertainment, e-commerce, and digital financial services.
- Sea is a beneficiary of accelerated digitisation in a post-Covid-19 landscape (e.g. increased usage and stickiness of e-commerce and digital payments).
- Sea believes in prioritising user acquisition and retention through aggressive marketing and providing compelling product proposition, so that it can maximise monetisation later on.
- Sea's strength is also in its ability to adapt for local preferences, which helps it excel in regions with heterogeneous cultures such as in Southeast Asia.
- We believe that Sea has a strong competitive advantage due to the network effects of its products - which are already leaders in their respective verticals.

Sea is among the fastest growing tech companies

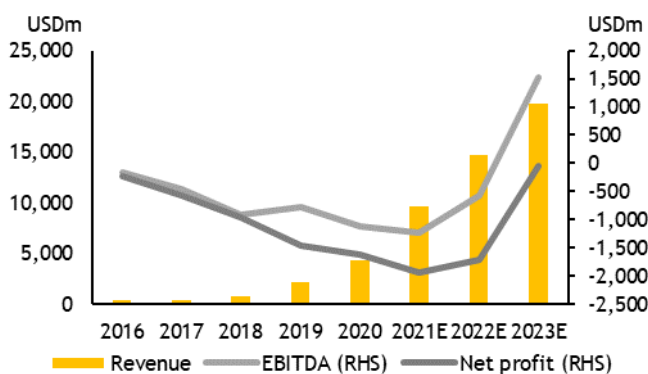


Source: Company

Financial Metrics

- We forecast FY20-23E revenue CAGR of 65%, driven by broad based strength.
- We also expect for Sea to turn profitable in FY24E on both EBITDA and net profit levels.
- We expect Sea to continue being in net cash position through FY23E, and for expansion needs to be funded by the digital entertainment business.

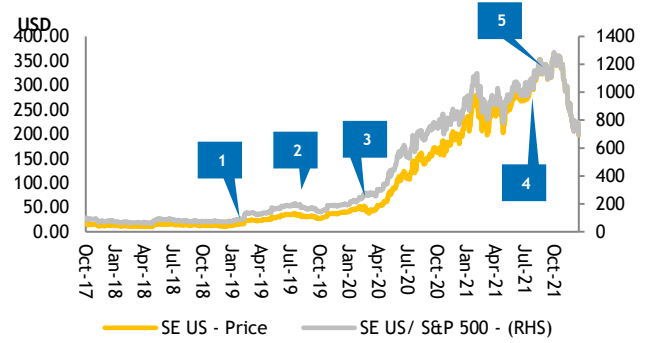
Revenue, EBITDA and net profit projections



Source: Company, Maybank IBG Research

Price Drivers

Historical share price trend



Source: Company, FactSet, Maybank IBG Research

- Strong 4Q18 and 1Q19 results on continual success of Free Fire
- 2Q19 loss widened despite results beat
- Sea was beneficiary of Covid-19, and share price rallied alongside e-commerce peers.
- Stronger than expected 2Q21 results, driven by Garena and Shopee, and company raising guidance.
- Sell-off due to concerns of normalising growth for Garena Free Fire, as well as broader weakness for pre-earnings growth companies amid hawkish Fed outlook.

Swing Factors

Upside

- Stronger than expected user growth (across all businesses)
- Stronger than expected GMV/TPV growth for e-commerce/ digital financial services.
- Stronger than anticipated monetisation rates across its businesses

Downside

- If investors are impatient with any delay in Sea's profitability turnaround.
- Slowing user growth metrics, especially if this is due to increasing competition across Sea's offerings.
- Signs of Free Fire losing market share, especially if Garena remains heavily reliant on Free Fire to drive revenue growth

Risk Rating & Score ¹	Not Rated
Score Momentum ²	NA
Last Updated	NA
Controversy Score ³	NA

Business Model & Industry Issues

- As an internet business, we believe social issues is the most relevant, followed by governance and then environmental.
- In the e-commerce business, driving social good (e.g. providing and teaching merchants how to use services) is integral to sustainably grow the platform and to retain merchants while monetising them. For instance, in Indonesia, 57% of MSMEs reported that they generated higher profits on Shopee than on other marketplaces.
- We believe the key issue for Garena are i) addiction and ii) compliance to local laws. For instance, Bangladesh is reportedly trying to ban Free Fire (alongside other addictive apps like PUBG and Tik Tok). Garena's response to appease authorities is important.
- The financial sector is also a highly regulated one. In our view SeaMoney's growth will be in part influenced by not just adherence to local laws, but how SeaMoney advances government agendas (e.g. facilitate roll-out of financial assistance in Malaysia and regulatory support for digital banking initiatives in ASEAN).
- Data security is also a critical ESG factor. Sea has employed various security measures to ensure this. (e.g. encryption of sensitive data, monitoring for unauthorized access etc).

Material E issues

- Aside the increased use of packaging materials associated with e-commerce as compared to traditional commerce, we do not see much environmental issues as the remaining businesses are digital based (i.e. gaming and digital financial services)
- We believe carbon emissions via the servers that Sea is also a key environmental footprint, although not much has been discussed in Sea's sustainability report pertaining environmental factors.

Material S issues

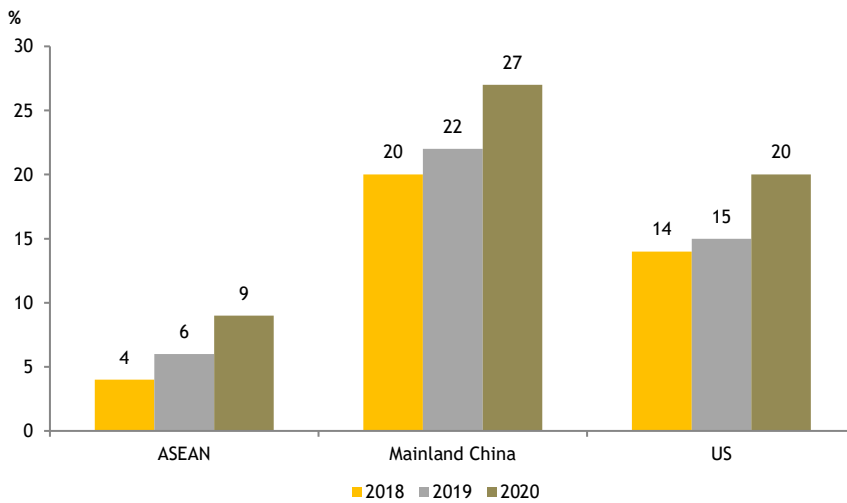
- Sea Limited aims to build highly diverse teams within the company.
- Of Sea's >30,000 global workforce, 46% are females. Furthermore, 46% of the middle to senior management positions are held by females. SEA also boast a diverse culture of over 50 different nationalities in their company.
- Sea strongly believes in hiring and grooming local talent, and is one of the largest employers of fresh graduates across Southeast Asia.
- In 2020, Sea conducted more than 5,000 training sessions for their employees.
During the Covid-19 pandemic, Shopee provided financial support and relief to SMEs by easing operational costs and attracting new customers. Shopee also provided the SMEs with online courses to help the SMEs to scale and succeed their business in the long run. Furthermore, SEA Limited committed more than USD 35m worth of COVID-19 Seller Support Packages across their markets, and provided monetary donation of more than USD 510,000.

Key G metrics and issues

- The board consist of 6 members. Out of which, 3 are non-executive.
- From a data security standpoint, Sea is committed in ensuring that the processing of personal data of consumers, employers and other stakeholders are carried out lawfully. Sea states that it uses its data collected to improve products to better serve its communities.
- Given a large part of Sea's competitive advantage is derived from the network effects from its large user base across multiple markets, compliance with laws is of utmost importance. Further, we believe complementing its growth strategies with government agenda.

¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company's exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company's enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company's score since the last update - a **negative** integer indicates a company's improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

Fig 1: ASEAN e-commerce sales as a % of total retail sales still low compared to mature e-commerce countries like China and US



Source: Euromonitor

Fig 2: ASEAN e-commerce web visits in 3Q21. Shopee was top ranked in all countries except Indonesia.

Indonesia		Singapore		Malaysia		Thailand		Philippines		Vietnam	
Tokopedia	158,137,700	Shopee	14,420,000	Shopee	57,566,700	Shopee TH	61,250,000	Shopee	73,650,000	Shopee Vietnam	77,826,700
Shopee	134,383,300	Lazada	8,650,000	Lazada	14,290,000	Lazada TH	37,923,300	Lazada	39,430,000	The Gioi Di Dong	50,923,300
Bukalapak	30,126,700	Amazon	4,703,300	PGMall	6,976,700	Central Online	2,580,000	Zalora	1,520,000	Dien May Xanh	27,043,300
Lazada	27,953,300	Qoo10	3,576,700	Zalora	1,100,000	HomePro	2,523,300	eBay	469,300	Lazada VN	21,413,300
Blibli	16,326,700	Castlery	1,286,700	GoShop	425,600	Advice	2,516,700	Beauty MNL	409,200	Tiki	17,500,000

Source: iPrice

Fig 3: Free Fire continued to be a top 10 mobile game by worldwide revenue in November 2021



Note: Does not include revenue from third-party Android stores in China or other regions. ▲ = Rank up over last month ▼ = Rank down over last month ★ = New to top chart

Source: Sensor Tower

Fig 4: SOTP

Methodology	Multiple	Item	Value (USDm)	Value of business (USDm)	Note
P/E	27	FY22E earnings	2,296	61,996	Premium to global peers on account of faster earnings growth rate
P/GMV	1.4	FY22E GMV	94,236	131,931	Higher than global peers on account of low ASEAN e-commerce penetration
P/TPV	0.4	FY22E TPV	30,596	12,238	In line with Paypal but higher than matured credit card payment companies like Visa and Mastercard
			FY22E EV	206,166	
			FY22E net cash	9,195	
			Equity value	215,361	
			Number of shares (m)	568.29	
			Value per share (USD)	379	

Source: Maybank IBG Research

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Key Metrics					
P/E (reported) (x)	nm	nm	nm	nm	nm
Core P/E (x)	nm	nm	nm	nm	nm
Core FD P/E (x)	nm	nm	nm	nm	nm
P/BV (x)	16.0	29.1	18.5	23.7	21.7
P/NTA (x)	16.1	29.1	18.5	23.6	21.6
Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0
FCF yield (%)	nm	0.2	nm	nm	0.9
EV/EBITDA (x)	nm	nm	nm	nm	66.5
EV/EBIT (x)	nm	nm	nm	nm	nm

INCOME STATEMENT (USD m)

Revenue	2,175.4	4,375.7	9,662.1	14,685.4	19,799.3
EBITDA	(769.6)	(1,122.6)	(1,228.2)	(581.1)	1,514.3
Depreciation	(121.6)	(180.8)	(302.7)	(538.0)	(854.4)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	(891.2)	(1,303.3)	(1,530.9)	(1,119.1)	659.9
Net interest income / (exp)	(14.3)	(123.4)	(88.5)	(173.9)	(196.8)
Associates & JV	(3.2)	0.7	0.7	0.7	0.7
Exceptionals	0.0	0.0	0.0	0.0	0.0
Other pretax income	(463.1)	(56.5)	0.0	0.0	0.0
Pretax profit	(1,371.9)	(1,482.5)	(1,618.7)	(1,292.2)	463.9
Income tax	(85.9)	(141.6)	(335.9)	(425.7)	(525.6)
Minorities	(5.1)	6.1	6.1	6.1	6.1
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	(1,462.8)	(1,618.1)	(1,948.5)	(1,711.8)	(55.7)
Core net profit	(1,462.8)	(1,618.1)	(1,948.5)	(1,711.8)	(55.7)

BALANCE SHEET (USD m)

Cash & Short Term Investments	3,553.9	7,026.1	12,266.2	11,628.9	12,640.5
Accounts receivable	187.0	363.0	608.8	965.6	1,301.9
Inventory	26.9	64.2	87.7	174.0	263.0
Property, Plant & Equip (net)	318.6	386.4	841.9	1,333.8	1,866.7
Intangible assets	15.0	39.8	36.6	34.7	33.3
Investment in Associates & JVs	0.0	0.0	0.0	0.0	0.0
Other assets	1,122.6	2,576.2	3,038.3	3,546.1	3,967.4
Total assets	5,224.2	10,455.7	16,879.6	17,683.0	20,072.8
ST interest bearing debt	1.3	0.0	0.0	0.0	0.0
Accounts payable	69.4	121.6	188.0	261.9	317.9
LT interest bearing debt	1,356.7	1,840.4	3,781.9	3,814.0	3,534.2
Other liabilities	2,624.0	5,073.0	6,988.0	8,944.0	11,111.0
Total Liabilities	4,051.5	7,035.4	10,957.8	13,019.5	14,962.9
Shareholders Equity	1,162.4	3,382.9	5,878.3	4,614.0	5,054.3
Minority Interest	10.2	37.3	43.4	49.5	55.6
Total shareholder equity	1,172.7	3,420.2	5,921.8	4,663.5	5,109.9
Total liabilities and equity	5,224.2	10,455.7	16,879.6	17,683.0	20,072.8

CASH FLOW (USD m)

Pretax profit	(1,371.9)	(1,482.5)	(1,618.7)	(1,292.2)	463.9
Depreciation & amortisation	121.6	180.8	302.7	538.0	854.4
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	0.0
Change in working capital	782.1	1,525.9	1,204.7	1,068.4	1,059.5
Cash taxes paid	0.0	0.0	0.0	0.0	0.0
Other operating cash flow	538.0	331.5	56.9	70.5	19.9
Cash flow from operations	69.9	555.6	(54.4)	384.7	2,397.7
Capex	(239.8)	(336.3)	(773.0)	(1,028.0)	(1,386.0)
Free cash flow	(170.0)	219.3	(827.4)	(643.3)	1,011.7
Dividends paid	0.0	0.0	0.0	0.0	0.0
Equity raised / (purchased)	1,538.8	2,970.2	3,498.0	0.0	0.0
Change in Debt	1,041.2	1,110.8	2,500.0	0.0	0.0
Other invest/financing cash flow	14.9	(374.8)	105.5	297.7	363.9
Effect of exch rate changes	0.0	0.0	0.0	0.0	0.0
Net cash flow	2,286.2	3,621.2	5,213.3	(637.3)	na

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Key Ratios					
Growth ratios (%)					
Revenue growth	163.1	101.1	120.8	52.0	34.8
EBITDA growth	nm	nm	nm	nm	nm
EBIT growth	nm	nm	nm	nm	nm
Pretax growth	nm	nm	nm	nm	nm
Reported net profit growth	nm	nm	nm	nm	nm
Core net profit growth	nm	nm	nm	nm	nm
Profitability ratios (%)					
EBITDA margin	nm	nm	nm	nm	7.6
EBIT margin	nm	nm	nm	nm	3.3
Pretax profit margin	nm	nm	nm	nm	2.3
Payout ratio	0.0	0.0	0.0	0.0	0.0
DuPont analysis					
Net profit margin (%)	nm	nm	nm	nm	nm
Revenue/Assets (x)	0.4	0.4	0.6	0.8	1.0
Assets/Equity (x)	4.5	3.1	2.9	3.8	4.0
ROAE (%)	na	na	na	na	na
ROAA (%)	(39.4)	(20.6)	(14.3)	(9.9)	(0.3)
Liquidity & Efficiency					
Cash conversion cycle	18.8	16.7	13.4	15.6	18.5
Days receivable outstanding	23.6	22.6	18.1	19.3	20.6
Days inventory outstanding	7.4	5.4	4.5	5.1	6.4
Days payables outstanding	12.2	11.4	9.2	8.8	8.5
Dividend cover (x)	nm	nm	nm	nm	nm
Current ratio (x)	1.9	1.9	2.5	1.9	1.7
Leverage & Expense Analysis					
Asset/Liability (x)	1.3	1.5	1.5	1.4	1.3
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Net gearing (%) (excl. perps)	net cash	net cash	net cash	net cash	net cash
Net interest cover (x)	na	na	na	na	3.4
Debt/EBITDA (x)	nm	nm	nm	nm	2.3
Capex/revenue (%)	11.0	7.7	8.0	7.0	7.0
Net debt/ (net cash)	(2,196.0)	(5,185.7)	(8,484.3)	(7,814.8)	(9,106.3)

Source: Company; Maybank

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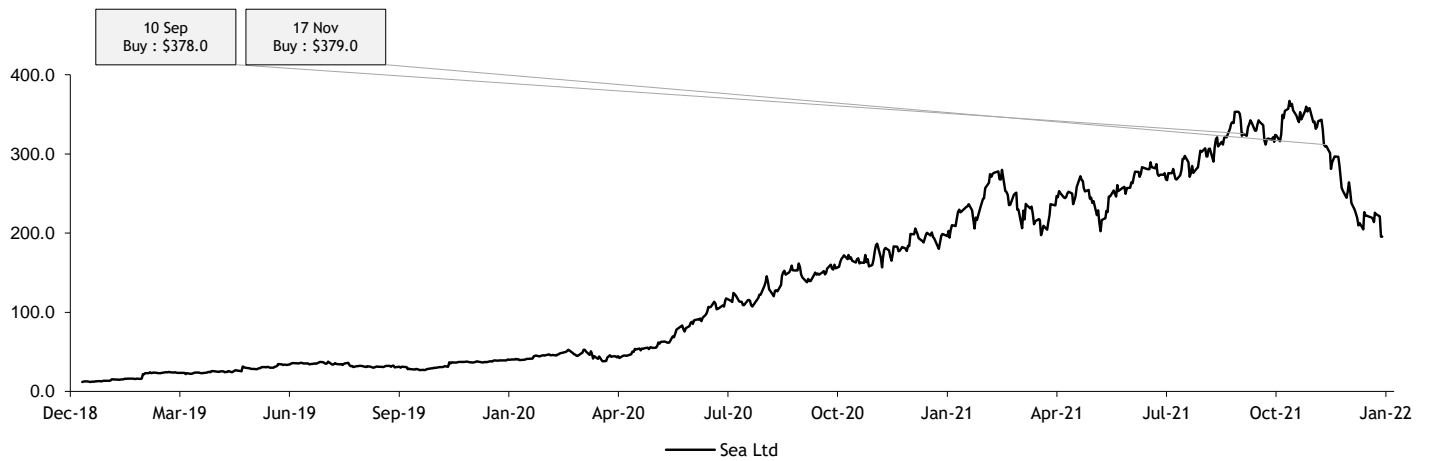
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