

Sea Ltd (SE US)

Free Fire showing signs of stabilizing

1Q22 net loss narrower than street had expected

1Q22 net loss of USD580m (+37% YoY) was less than consensus and what we had expected. We trim our FY22E e-commerce GAAP revenue by 6% to USD8.5b, at the lower end of revised guidance as we take a more conservative view amid macro uncertainties. Free Fire is showing signs of stabilizing. Our SOTP-based TP is cut 13% to USD140 as we tweak multiples for the respective businesses. But retain BUY as we believe Sea is a proxy to ASEAN digitisation via e-commerce and digital financial services growth.

Guidance widened; Strong traction in Brazil

1Q22 e-commerce GAAP revenue rose 64% YoY to USD1.5b. Revenue guidance widened to USD8.5-9.1b (+71.8% YoY at midpoint) from USD8.9-9.1b as Sea observes a wider dispersion of outcomes amid macro uncertainties. Shopee has not yet seen material impact from the Covid-19 lockdowns in China. Moreover, the majority of e-commerce sales are local-to-local, and cross border is a minor portion. Shopee Brazil continued to top rankings for downloads (shopping category) and total time spent. In March and April, Shopee Brazil was also the top shopping app by monthly active users - suggesting strong traction in the country. Management continues to guide for Shopee to reach EBITDA breakeven before HQ costs in ASEAN + Taiwan this year.

Free Fire stabilizing

1Q22 digital entertainment bookings fell 28% YoY to USD0.8b on normalisation of users as economies reopened (QPU -23% YoY, ARPPU: -6%). Sea observes that towards end-1Q22, Free Fire started to show early signs of stabilizing. Free Fire maintains top global rankings and grossing metrics. In Indonesia, where SeaMoney has the most comprehensive product suite, over 30% of quarterly active users used multiple products in 1Q22.

Key risks

We believe key risk to our forecast is if we underestimate investments needed for Shopee and SeaMoney. Despite widening of the guidance range, management believes the original e-commerce GAAP revenue guidance is achievable. An additional risk to the e-commerce business is supply chain disruptions that may impair inventory availability in 2H22, in our view. But we see the ability of sellers to multi-source as a mitigating factor.

FYE Dec (USD m)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	4,376	9,955	13,461	19,190	24,106
EBITDA	(1,123)	(1,304)	(1,475)	(12)	1,930
Core net profit	(1,618)	(2,045)	(2,513)	(1,420)	67
Core FDEPS (cts)	(327.5)	(350.2)	(434.1)	(236.6)	11.0
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)	29.1	17.0	8.1	9.1	7.4
Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0
ROAA (%)	(20.6)	(14.0)	(13.8)	(7.8)	0.3
EV/EBITDA (x)	nm	nm	nm	nm	20.9
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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BUY

Share Price	USD 80.23
12m Price Target	USD 140.00 (+74%)
Previous Price Target	USD 160.00

Company Description

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

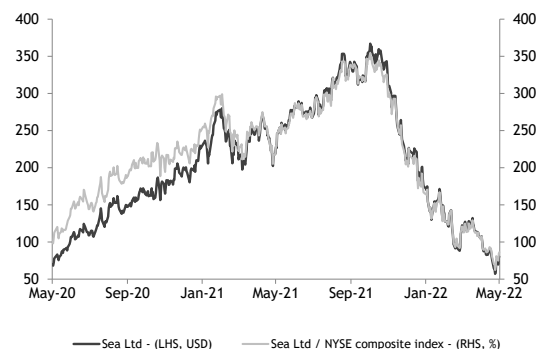
Statistics

52w high/low (USD)	366.99/57.04
3m avg turnover (USDm)	179.9
Free float (%)	100.0
Issued shares (m)	555
Market capitalisation	USD44.5B
	USD44.5B

Major shareholders:

Tencent	18.7%
Li Xiaodong	12.6%
Gang Ye	7.7%

Price Performance



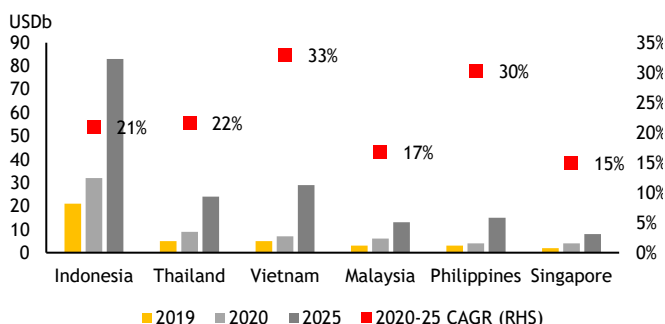
	-1M	-3M	-12M
Absolute (%)	(23)	(37)	(65)
Relative to index (%)	(17)	(33)	(62)

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.

Shopee is exposed to fast-growing ASEAN e-commerce GMV

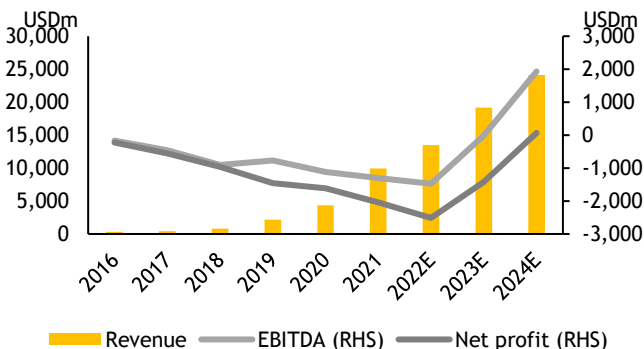


Source: Google, Temasek, Bain

Financial Metrics

- We forecast FY21-25E revenue CAGR of 26.5%, driven by e-commerce and digital financial services.
- We also expect Sea to achieve breakeven in FY24E.
- We expect Sea to continue being in a net cash position through FY24E, and have enough cash to fund investments in e-commerce and digital financial services. Digital entertainment is still an important source of cashflow.

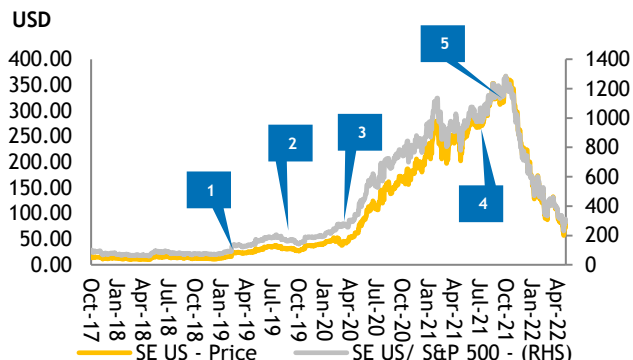
Revenue, EBITDA and net profit projections



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	na
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

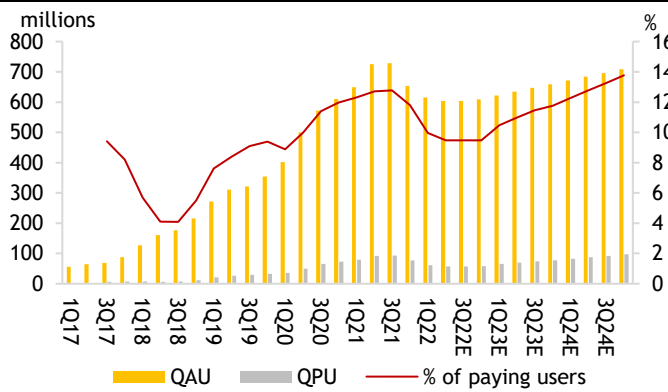
- Sea Limited aims to build highly diverse teams within the company.
- Of Sea's >30,000 global workforce, 46% are females. Furthermore, 46% of the middle to senior management positions are held by females. SEA also boast a diverse culture of over 50 different nationalities in their company.
- Sea strongly 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.

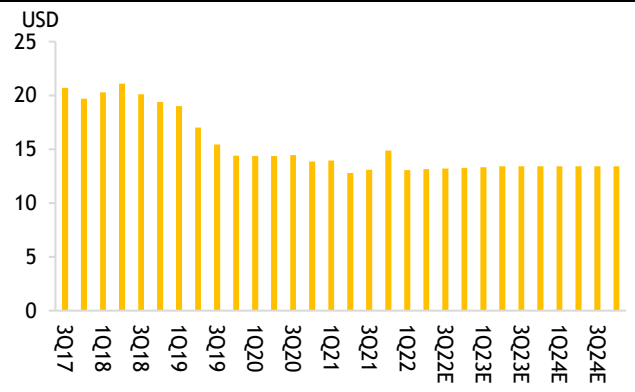
¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company's exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company's enterprise value, respectively, from ESG-driven 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: Garena user metrics



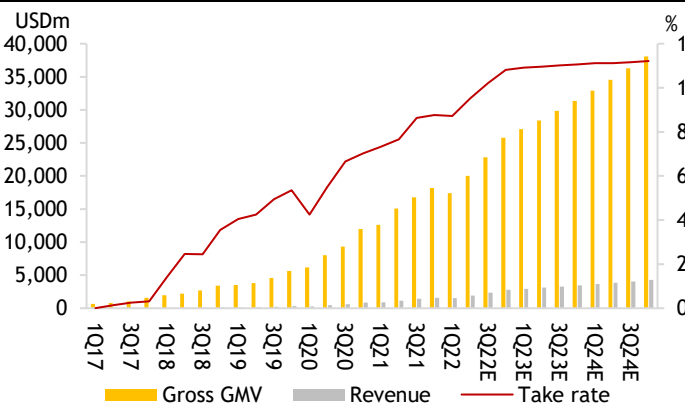
Source: Company, Maybank IBG Research

Fig 2: Garena ARPPU



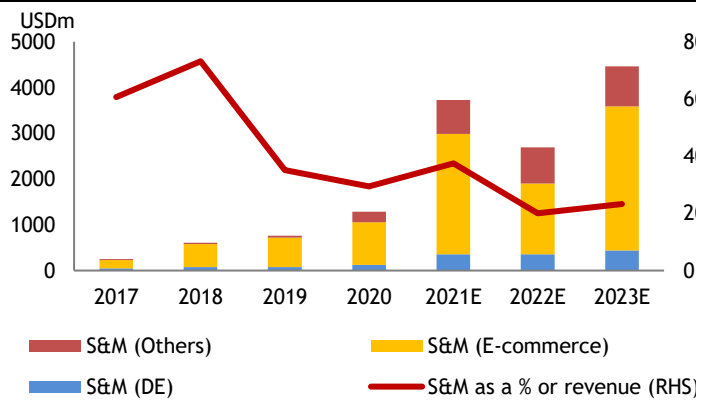
Source: Company, Maybank IBG Research

Fig 3: Shopee GMV. Revenue and take rate



Source: Company, Maybank IBG Research

Fig 4: Sales & marketing expenses



Source: Company, Maybank IBG Research

Fig 5: Forecast changes

USDm	FY22			FY23		
	New	Old	change	New	Old	change
DE bookings	3,074	3,030	1%	3,834	3,513	9%
E-commerce GAAP revenue	8,539	9,052	-6%	12,824	12,626	2%
Revenue	13,461	13,330	1%	19,190	18,279	5%
Gross profit	4,653	4,178	11%	6,550	5,922	11%
EBITDA	(1,475)	(1,699)	-13%	(12)	(481)	-98%
PATMI	(2,513)	(2,489)	1%	(1,420)	(1,449)	-2%

Source: Maybank IBG Research

Fig 6: 1Q22 summary

Items (USDm)	1Q22	1Q21	4Q21	YoY	QoQ	FY21E	1Q22 vs FYE
Digital entertainment bookings	803	1,114	1,149	-28%	-30%	3,030	26
E-commerce GMV	17,400	12,598	18,200	38%	-4%	99,345	18
E-commerce GAAP revenue	1,516	922	1,595	64%	-5%	9,052	17
Service revenue							
Digital entertainment (revenue)	1,135	781	1,415	45%	-20%	2,957	38
E-commerce and other services (revenue)	1,500	772	1,483	94%	1%	8,178	18
Sales of goods	265	210	324	26%	-18%	2,196	12
Total revenues	2,900	1,764	3,222	64%	-10%	13,330	22
Total costs of revenues	(1,730)	(1,118)	(1,911)	55%	-10%	(9,152)	19
Gross profit	1,170	645	1,311	81%	-11%	4,178	28
Net income/(loss) after minority	(580)	(423)	(618)	37%	-6%	(2,489)	23

Source: Company, Maybank IBG Research

Fig 7: SOTP

Business	Methodology	Multiple	Item	Value (USDm)	Value of business (USDm)	Note
Digital entertainment	EV/EBIT	15.0	FY22E EV/EBIT	2,032	30,478	15% discount to global peers on account of Free Fire concentration and FY22 slowdown
E-commerce	EV/Sales	3.0	FY23E EV/S	12,824	38,473	In line with MELI
Digital financial services	EV/TPV	0.1	FY23E EV/TPV	50,535	5,053	
				FY22E net cash (USDm)	7,224	
				Equity value (USDm)	81,228	
				Number of shares (m)	578.93	
				Value per share (USD)	140	

Source: Maybank IBG Research

Fig 8: Peer comps

Company	BBG Code	Price (LC)	Mcap USDm	P/E (x)			EPS CAGR	EV /EBIT (x)		EV/S (x)	
				FY1	FY2	FY3		FY1	FY2	FY1	FY2
Digital entertainment											
Tencent	700 HK	350.00	428,571	22.4	18.8	16.2	-9%	18.2	15.3	5.0	4.4
Krafton	259960 KS	241,000	9,209	15.9	14.5	13.8	15%	9.1	7.8	3.6	3.2
Electronic Arts Take Two Interactive	EA US TTWO US	127.39 110.11	35,825 12,713	17.6 22.2	15.5 18.9	13.7 13.3	9% 18%	13.5 17.0	11.7 12.9	4.4 3.0	4.1 2.5
Netease	NTES US	93.25	62,546	20.8	17.8	15.9	8%	18.9	15.2	3.4	3.0
Zynga	ZNGA US	7.92	9,007	23.7	19.0	15.8	31%	14.1	12.3	3.3	3.0
NCSOFT	036570 KS	420,500	7,188	15.5	13.2	11.7	26%	12.0	9.8	2.6	2.3
Netmarble	251270 KS	73,800	4,939	20.7	16.3	15.4	19%	26.3	20.3	2.3	2.1
Nexon	3659 JP	2,934	20,471	24.5	20.1	18.9	6%	17.5	12.8	6.6	5.6
Bandai Namco	7832 JP	8,744	15,040	22.0	20.0	18.6	4%	13.7	12.3	1.9	1.8
Average				21.8	18.4	16.0	-3%	17.6	14.7	4.6	4.1
E-commerce											
Alibaba	BABA US	86.48	232,021	12.1	11.4	10.0	-5%	21.1	13.3	1.8	1.6
JD.com	JD US	51.53	68,122	29.1	18.7	14.5	28%	49.4	20.3	0.4	0.3
Meituan	3690 HK	163.50	114,672	-	143.7	42.4	-193%	NA	136.1	3.4	2.6
Pinduoduo	PDD US	37.84	47,844	23.7	15.8	13.1	NM	NA	NA	2.9	2.4
VIPSHOP	VIPS US	8.14	4,707	6.5	6.0	5.5	2%	3.0	1.9	0.3	0.3
Amazon.com	AMZN US	2,216	1,127,431	116.6	40.3	24.9	11%	56.2	30.5	2.1	1.8
eBay	EBAY US	45.09	25,243	11.3	10.1	9.2	7%	11.1	10.3	2.6	2.5
Shopify	SHOP US	360	41,104	289.4	158.5	82.3	-12%	372.0	173.4	7.0	5.3
MercadoLibre	MELI US	788	39,688	117.4	65.2	39.7	NM	71.7	42.7	3.9	3.0
Rakuten	4755 JP	802	9,841	-	-	31.4	NM	-7.2	-157.7	0.7	0.6
Bukalapak	BUKA IJ	272	1,918	-	-	264.2	NM	-6.4	-11.0	9.8	6.8
Baozun	BZUN US	7.82	442	18.7	9.5	7.0	NM	4.7	2.0	0.3	0.3
Average				97.3	44.7	25.1	-8%	58.5	37.5	2.3	1.9
Payments and fintechs											
Visa	V US	197.81	325,540	27.6	23.6	20.1	18%	22.2	19.3	11.3	10.0
Mastercard	MA US	329.73	318,163	31.4	26.0	21.1	23%	26.6	21.7	14.3	12.2
Paypal	PYPL US	77.65	89,922	19.7	15.9	12.9	9%	15.3	12.2	3.2	2.7
Square	SQ US	79.70	41,349	94.7	49.2	34.3	11%	-81.0	-304.2	2.3	1.9
Average				31.8	25.0	20.4	19%	17.7	2.2	11.1	9.7

Source: Bloomberg, FactSet, Maybank IBG Research

FYE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
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)	29.1	17.0	8.1	9.1	7.4
P/NTA (x)	29.1	17.1	8.1	9.2	7.5
Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0
FCF yield (%)	0.2	nm	nm	nm	3.1
EV/EBITDA (x)	nm	nm	nm	nm	20.9
EV/EBIT (x)	nm	nm	nm	nm	56.0

INCOME STATEMENT (USD m)

Revenue	4,375.7	9,955.2	13,461.3	19,190.4	24,105.6
EBITDA	(1,122.6)	(1,304.4)	(1,475.1)	(11.8)	1,929.9
Depreciation	(180.8)	(278.7)	(557.1)	(859.6)	(1,208.3)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	(1,303.3)	(1,583.1)	(2,032.2)	(871.4)	721.6
Net interest income / (exp)	(123.4)	(102.9)	(163.0)	(185.6)	(217.1)
Associates & JV	0.7	5.0	5.0	5.0	5.0
Exceptionals	0.0	0.0	0.0	0.0	0.0
Other pretax income	(56.5)	(29.5)	0.0	0.0	0.0
Pretax profit	(1,482.5)	(1,710.4)	(2,190.3)	(1,052.0)	509.5
Income tax	(141.6)	(332.9)	(321.6)	(366.9)	(441.2)
Minorities	6.1	(1.4)	(1.4)	(1.4)	(1.4)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	(1,618.1)	(2,044.7)	(2,513.3)	(1,420.3)	66.9
Core net profit	(1,618.1)	(2,044.7)	(2,513.3)	(1,420.3)	66.9

BALANCE SHEET (USD m)

Cash & Short Term Investments	7,026.1	10,799.4	9,036.1	8,565.3	10,050.4
Accounts receivable	363.0	388.3	516.3	736.1	924.6
Inventory	64.2	117.5	143.3	231.5	300.0
Property, Plant & Equip (net)	386.4	1,030.0	1,480.2	1,978.9	2,231.9
Intangible assets	39.8	52.5	67.5	82.5	97.5
Investment in Associates & JVs	0.0	0.0	0.0	0.0	0.0
Other assets	2,576.2	6,368.3	6,472.9	6,915.6	7,254.9
Total assets	10,455.7	18,756.0	17,716.3	18,509.9	20,859.3
ST interest bearing debt	0.0	100.0	100.0	100.0	100.0
Accounts payable	121.6	213.6	224.3	291.1	339.9
LT interest bearing debt	1,840.4	3,475.7	3,814.0	3,534.2	2,500.0
Other liabilities	5,073.0	7,542.0	7,890.0	9,438.0	11,410.0
Total Liabilities	7,035.4	11,331.6	12,028.8	13,362.8	14,349.6
Shareholders Equity	3,382.9	7,398.7	5,663.1	5,124.2	6,488.3
Minority Interest	37.3	25.7	24.3	22.9	21.5
Total shareholder equity	3,420.2	7,424.4	5,687.4	5,147.1	6,509.7
Total liabilities and equity	10,455.7	18,756.0	17,716.3	18,509.9	20,859.3

CASH FLOW (USD m)

Pretax profit	(1,482.5)	(1,710.4)	(2,190.3)	(1,052.0)	509.5
Depreciation & amortisation	180.8	278.7	557.1	859.6	1,208.3
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	0.0
Change in working capital	1,525.9	1,276.2	61.3	528.0	656.6
Cash taxes paid	0.0	0.0	0.0	0.0	0.0
Other operating cash flow	331.5	364.2	835.8	517.1	539.2
Cash flow from operations	555.6	208.6	(736.0)	852.7	2,913.5
Capex	(336.3)	(722.2)	(1,076.9)	(1,343.3)	(1,446.3)
Free cash flow	219.3	(513.5)	(1,812.9)	(490.6)	1,467.2
Dividends paid	0.0	0.0	0.0	0.0	0.0
Equity raised / (purchased)	2,970.2	4,050.1	0.0	0.0	0.0
Change in Debt	1,110.8	2,960.3	0.0	0.0	0.0
Other invest/financing cash flow	(374.8)	445.9	(2,690.4)	277.5	122.9
Effect of exch rate changes	0.0	0.0	0.0	0.0	0.0
Net cash flow	3,621.2	3,843.0	(1,801.8)	na	na

FYE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Key Ratios					
Growth ratios (%)					
Revenue growth	101.1	127.5	35.2	42.6	25.6
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	8.0
EBIT margin	nm	nm	nm	nm	3.0
Pretax profit margin	nm	nm	nm	nm	2.1
Payout ratio	0.0	0.0	0.0	0.0	0.0
DuPont analysis					
Net profit margin (%)	nm	nm	nm	nm	0.3
Revenue/Assets (x)	0.4	0.5	0.8	1.0	1.2
Assets/Equity (x)	3.1	2.5	3.1	3.6	3.2
ROAE (%)	na	na	na	na	na
ROAA (%)	(20.6)	(14.0)	(13.8)	(7.8)	0.3
Liquidity & Efficiency					
Cash conversion cycle	16.7	9.0	8.5	9.7	11.2
Days receivable outstanding	22.6	13.6	12.1	11.7	12.4
Days inventory outstanding	5.4	5.4	5.3	5.3	6.3
Days payables outstanding	11.4	10.0	8.9	7.3	7.4
Dividend cover (x)	nm	nm	nm	nm	nm
Current ratio (x)	1.9	2.1	1.8	1.5	1.4
Leverage & Expense Analysis					
Asset/Liability (x)	1.5	1.7	1.5	1.4	1.5
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	3.3
Debt/EBITDA (x)	nm	nm	nm	nm	1.3
Capex/revenue (%)	7.7	7.3	8.0	7.0	6.0
Net debt/ (net cash)	(5,185.7)	(7,223.7)	(5,122.0)	(4,931.1)	(7,450.4)

Source: Company; Maybank IBG Research

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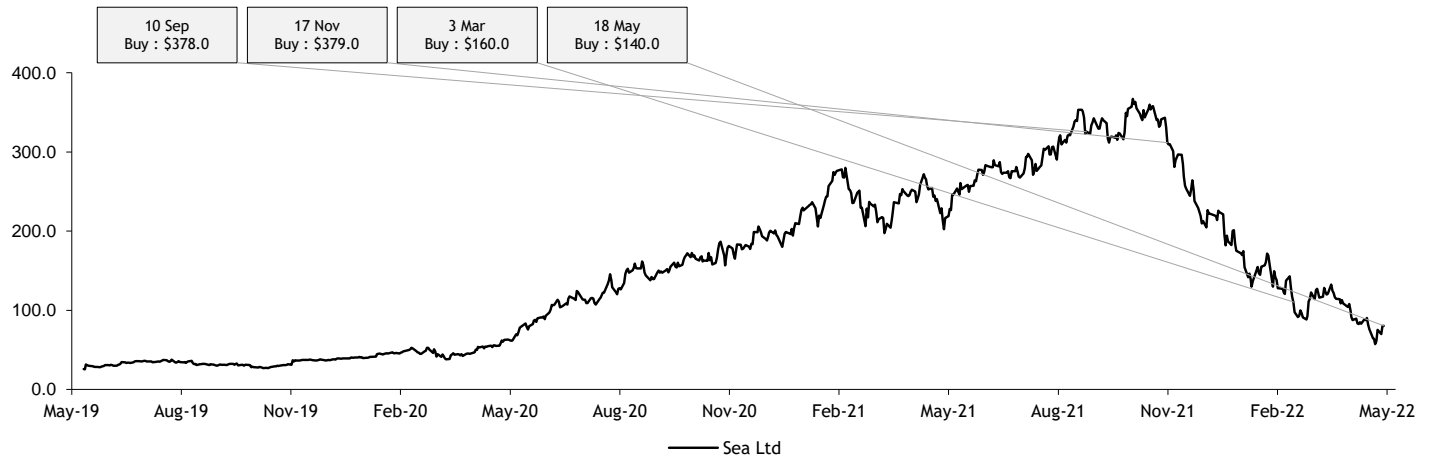
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