

G5 Entertainment

Quarter Update – Q4'15



Share Price	37.9 SEK
Market Capitalisation	333.5 mSEK
Target Price	48.8 SEK

Last updated on the 02/03/2016

G5 Entertainment develops and sells casual games for different platforms. The company acts as both developer and publisher of their own games as well as actively working with third-party licenses. The company now focuses on Free-To-Play (FTP) games, where players buy virtual goods within the game rather than the old revenue model of unlockables where games are pre-paid.

Strong growth trajectory

In the fourth quarter of the year, G5 Entertainment achieved record for the year quarterly revenue of SEK 101.3 M, 23% YoY. This added up to a record-breaking year with revenue ending at SEK 384 million, and a net profit for the year of SEK 15 million.

The market remains equally competitive, but we believe that G5 possesses significant expertise in monetising its games and it can maintain its strong positions. The global mobile gaming market is expected to grow rapidly in 2016 and without a doubt this will benefit companies such as G5 Entertainment.

Overall, we believe the business is in a strong upward spiral and it will continue to outperform the market in 2016. Therefore, we maintain our 'Strong Buy' recommendation with target price of SEK 48.8 per share.

Company	G5 Entertainment
Ticker	G5EN.STO
Currency	SEK
Industry	Mobile gaming
# of shares	8,800,000
Share price	37.9
Target price	48.8
Risk	Medium
Recommendation	Strong Buy

SHARE PRICE PERFORMANCE



NEXT EVENT

May 5, 2016: Q1'15 Release

CONTACT ANALYSTS

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SEK (Thousand)	2013	2014	2015	2016e	2017e	2018e
Revenue	100,007	182,117	384,369	495,836	604,920	701,707
EBITDA	(11,826)	9,014	19,788	41,610	64,493	76,762
EPS	-1.34	0.77	1.74	3.65	5.65	6.72
EBITDA margin	-12%	5%	5%	8%	11%	11%
NIBD/EBITDA	N/A	N/A	N/A	N/A	N/A	N/A
EV/Sales	2.44	1.34	0.64	0.49	0.40	0.35
EV/EBITDA	(20.67)	27.12	12.36	5.88	3.79	3.19
ROIC	-13%	7%	13%	21%	25%	23%

See disclosures at the end of this report.

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Investment Summary

Strong business model and good margins

Revenue growth in Q4 was lower than some of the previous quarter, but nevertheless the company managed to surpass the SEK 100 million mark. The slowdown in growth rate was mainly due to temporary factors such as slower performance of some of the older F2P games, and the fact that the company did not release new games until late in the year. However, the market outlook remains strong.

We expect 2016 to be another record-breaking year. The company demonstrates strong ability to make profit and quite likely it will use the extra profit to fuel future growth. User Acquisition (UA) expenditure has been reduced to 16% of revenue, but given the extra cash and good performance in Q1, the company might increase this. 2015 proved that G5's business model is extremely strong and the company managed to outperform most of the market by a combination of excellent games portfolio and tactical user acquisition. Given the fact that the company has acquired much new knowledge and improved its analytics/monetization processes, there is no reason not to expect solid results in 2016.

Solid pipeline for 2016

G5 has released a number of games towards the end of the year, most of which will be marketed and monetized starting from the first quarter of the year. The company is focused on utilizing its existing IP and developing F2P games – something that has proven to bring solid profit.

G5 reports that it has a number of games lined up for 2016 and it will be releasing its games on all currently used gaming platforms. Additionally, the company informs that a number of G5's games will be coming to Facebook. Given the recent trends, establishing Facebook presence might be a very timely move for G5, as other gaming companies have been performing particularly well on the platform.

Valuation: Still one of the fastest growing companies in Sweden

G5 remains one of the fastest growing companies in Sweden, beating most expectations. Despite what seemed like a slowdown in the beginning of 2015, the company performed very well during the year and did not interrupt its growth.

Right now, it is all about marketing. The company has a clear opportunity to become one of the world's leading mobile games developers and for this purpose G5 will re-invest much of its profits. The company's financial position remains extremely strong with SEK 33.9 M of cash at the end 2015.

Much of what has been invested in 2015 will continue to fuel growth in 2016 and 2017. The strategy has worked out very well and we expect that the company will continue to maintain its strong momentum. Given the company's strong ability to grow, while balancing its expenditure, we believe that it is one of the most overlooked companies in Sweden.

Our DCF analysis shows a fair share price of 48.8 per share, even with conservative estimates, which reveals a significant upside potential for its shares.

Q4 Review

Revenue for the last quarter of the year was SEK 101.3 M (82.2), 23% increase YoY, while EBIT increased by 256% YoY and ended at SEK 8.4 M (2.4). The increased EBIT also resulted in higher net result for the period of SEK 9.6 M (3.3). Thus, the company demonstrated its profit-making ability, even though growth was slower than earlier in the year. The lower growth was mainly due to the fact that the company did not release new games until late in the year, as well as suboptimal performance of some of the old games.

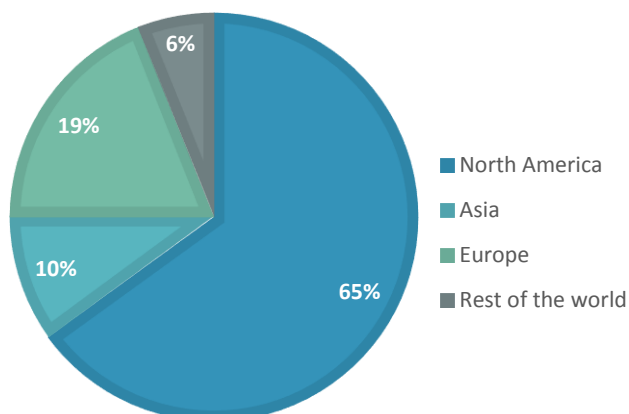
Sales and marketing expenses during the quarter were SEK 18.5 M, including SEK 16.5 M spent on user acquisition. Thus, user acquisition expenses represent 16% of total revenue, compared to 19% at the end of 2014. The reduction in user acquisition expenses happened after a slower than expected first quarter of the year. Going forward, we expect that UA spent will remain 16% for the first quarter, but later in the year the company might use more of its extra profits and reinvest it in user acquisition. This has proven a strong strategy and UA has fueled much of the growth we have seen in 2015.

R&D expenses also increased in the last quarter to SEK 14.5 M, a 45% YoY, which we believe to be a sign that the company is working to expand its product portfolio and improve its analytics/development platforms.

MSEK	Q4'15	Q4'14
Net turnover	101,277	82,152
Gross profit	49,240	39,747
R&D expenses	-14,535	-10,010
Sales & Marketing	-18,531	-15,654
General expenses	-7,949	-11,120
Pre-tax profit	8,386	2,394
Taxes	1,173	861
Net profit	9,560	3,255
EPS	1.09	0.37

The divisional breakdown of revenue shows that nearly 2/3 is derived from North America, followed by distant Europe with 19%. Together North America and Europe define almost 85% of total revenues. At the moment, the US gaming market is in a strong position, so it is likely that the importance of this market will increase even further.

REVENUE BY GEOGRAPHICAL REGION



Q1 Expectations

Going forward, we expect a strong first quarter of the year. We project a growth of 7.8%, which is higher than what was achieved in Q4'15. However, depending on the number of games G5 releases and relative game performance, the company is capable of achieving a double-digit growth. In fact, G5 released a number of games towards the end of Q4, which can fuel growth in Q1:

- Mahjong Journey, already released on iOS and Amazon, was also released on Google Play.
- Supermarket Mania Journey was released on Apple App Store for iPad.
- Special Enquiry Detail, was also released on Apple App Store for iPad.

We also expect a marginal increase in sales & marketing expenses as the company will try to promote those games, plus any new games that it may releases in Q1. Overall, we expect EBIT to be higher in Q1, compared to Q4, but the net result and EPS might be lower due to the positive effect of taxes in Q4.

MSEK	Q1'16	Q4'15
Net turnover	109,177	101,277
Gross profit	53,081	49,240
R&D expenses	-14,942	-14,535
Sales & Marketing	-19,254	-18,531
General expenses	-8,028	-7,949
Pre-tax profit	10,103	8,386
Taxes	-2,021	1,173
Net profit	8,082	9,560
EPS	0.92	1.09

2016 Expectations

We expect that 2016 will be an equally successful year for G5 and the company will continue to grow. We project revenue growth rate of 29%, which will result in SEK 495 million in revenue and expect EBIT to double in the upcoming year. We also believe that given a good start of the year, the company might increase its UA costs to 19% of revenue and thus project an increase in overall expenses. Other expenses will increase marginally with the exception of R&D, where the company will invest in the development of new games.

Even despite the projected increase in expenses, the company is a position to double its income and reach profit of SEK 30 million. Whether this happens will depend on how the company's strategy will develop throughout the year. If game performance is strong, G5 will likely invest the extra cash either in user acquisition or in further game releases and improvement of its analytics/marketing processes.

The company is in a strong position to grow and become a premier game developer/publisher. While we expect the first half of the year to be largely similar to 2015, G5 might make changes in its strategy in 2H 2016 with the purpose of growing its future potential. Of course, the market remains highly competitive and dynamic and we do not expect any unnecessary risks to be undertaken.

ESTIMATES

Profit and loss

SEK (Thousand)	2013	2014	2015	2016	2017	2018
Revenue	100,007	182,117	384,369	495,836	604,920	701,707
Production Cost	(78,925)	(102,091)	(201,094)	(252,876)	(308,509)	(357,871)
	-79%	-56%	-52%			
Gross Profit	21,082	80,026	183,275	242,960	296,411	343,836
General Expenses	(34,342)	(69,584)	(160,690)	(199,256)	(229,144)	(263,516)
Other Operating Income	2,046	1,803	2,549	2,569	2,588	2,608
Other Operating Expense	(612)	(3,231)	(5,346)	(4,663)	(5,362)	(6,167)
Operating Result Before Financial Results	(11,826)	9,014	19,788	41,610	64,493	76,762
Financial Income	85	249	38	129	135	142
Financial Expense	(301)	(646)	(48)	(50)	(53)	(56)
Operating Result After Financial Results	(12,042)	8,617	19,778	41,688	64,575	76,849
Taxes	378	(1,804)	(4,448)	(9,588)	(14,852)	(17,675)
	3%	21%				
Net Result	(11,664)	6,813	15,330	32,100	49,723	59,173

Balance Sheet

SEK (Thousand)	2013	2014	2015	2016	2017	2018
FIXED ASSETS						
Intangible fixed assets						
Capitalized development costs	48,299	71,680	94,269	99,925	105,921	112,276
Goodwill	2,318	2,302	2,293	2,293	2,293	2,293
	50,617	73,982	96,562	102,218	108,214	114,569
Tangible Fixed Assets						
Equipment	1,929	2,892	4,634	6,465	9,020	12,585
Deferred Tax	2,105	1,025	2,310	2,310	2,310	2,310
	4,034	3,917	6,944	8,775	11,330	14,895
Total fixed assets	54,651	77,899	103,506	110,993	119,544	129,464
Current assets						
Account receivable	7,156	7,569	9,881	10,868	13,259	15,380
Tax receivable	4,437	0	175	177	180	182
Other receivables	6,915	7,327	3,952	4,268	4,610	4,978
Developer Royalty Advance	0	0	0	0	0	0
Prepaid expenses and accrued income	10,916	21,536	25,197	35,276	49,386	69,141
Cash at bank	27,433	32,864	33,870	55,522	88,038	123,277
Total Current assets	56,857	69,296	73,075	106,111	155,472	212,958
TOTAL ASSETS	111,508	147,195	176,581	217,104	275,016	342,422
Equity						
Share capital	880	880	880	880	880	880
Other capital contribution	54,032	54,032	54,032	54,032	54,032	54,032
Other reserves	22	8,575	8,575	8,575	8,575	8,575
Retained Earnings	34,058	40,871	59,858	91,958	141,680	200,854
Total shareholders' equity	88,992	104,358	123,345	155,445	205,167	264,341
Non-current liabilities						
Deferred tax	0	0	0	0	0	0
Current liabilities						
Account payable	7,478	12,893	12,320	16,627	20,286	23,531
Other liabilities	464	1,593	1,225	1,372	1,537	1,721
Tax liabilities	6,505	2,326	6,438	7,082	7,790	8,569
Accrued expenses	8,069	26,025	33,253	36,578	40,236	44,260
Total current liabilities	22,516	42,837	53,236	61,660	69,848	78,081
TOTAL EQUITY AND LIABILITIES	111,508	147,195	176,581	217,104	275,016	342,422

VALUATION

DCF Valuation

Scenario	Fair value	Probability
Base	49.83	50%
Worst	35.57	25%
Best	60.06	25%
Weighted Fair Value per share	48.82	

WACC Calculation	
Debt to Equity Ratio	0.00%
Cost of Equity	10.50%
Cost of Debt	4.27%
WACC	10.50%

SEK (Thousand)	2013	2014	2015	2016	2017	2018
Sales	100,007	182,117	384,369	495,836	604,920	701,707
EBITDA	(11,826)	9,014	19,788	41,610	64,493	76,762
EPS	-1.34	0.77	1.74	3.65	5.65	6.72
DPS	N/A	N/A	N/A	N/A	N/A	N/A
Share Outstanding	8,711	8,800	8,800	8,800	8,800	8,800
Sales Growth	24%	82%	111%	29%	22%	16%
EBITDA margin	-12%	5%	5%	8%	11%	11%
NIBD/EBITDA	N/A	N/A	N/A	N/A	N/A	N/A
Debt/Equity	0%	0%	0%	0%	0%	0%
EV/Sales	2.44	1.34	0.64	0.49	0.40	0.35
EV/EBITDA	(20.67)	27.12	12.36	5.88	3.79	3.19
ROIC	-13%	7%	13%	21%	25%	23%
ROA	-10%	5%	9%	15%	18%	17%
ROE	-13%	7%	12%	21%	24%	22%

Top Shareholders

Figure 3.0: Top 15 shareholders as of 31/12/2014

	Name	# shares	% ownership
1	Försäkringsaktiebolaget Avanza Pension	812,676	9,23%
2	Rite Internet Ventures Holding AB	677,447	7,70%
3	Wide Development Limited	616,000	7,00%
4	Proxima LTD	570,000	6,48%
5	Swedbank Robur Ny Teknik	550,000	6,25%
6	Purple Wolf Limited	530,000	6,02%
7	Nordnet Pensionsförsäkring AB	478,445	5,44%
8	Tommy Svensk	403,000	4,58%
9	ABG Sundal Collier ASA	249,818	2,84%
10	Peter Lindell	143,673	1,63%
11	Mattias Ståhlgren	142,000	1,61%
12	Robur Försäkring AB	107,742	1,22%
13	Old Mutual International IOM LTD	100,750	1,14%
14	Altraplan Bermuda Limited	99 33	1,13%
15	Daniel Eriksson	90 00	1,03%
	Top 15	5,381,551	61.15%
	Other	3,418,449	38.85%
	Total	8,800,000	100.00%

G5 Entertainment



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