

Tencent (700 HK)

FUNDAMENTAL VIEW ¹

As of 07 Jan 2025

- We maintain our Outperform recommendation on Tencent post its decent 3Q24 results; Revenues remained resilient on a pick of its gaming/social networking segment; EBITDA margin was higher on a better revenue mix, monetization and cost efficiencies; cash flow notably improved and Total debt/EBITDA trended lower despite the increased shareholder rewards. We expect the company's debt metrics to further improve in FY25. We continue viewing Tencent \$ bonds as core holdings in China and Asia IG credits; we like its 30,31 for investors looking to add duration as it offers a 15-20 bp of spread pick up against US A Tech and China SOEs. We prefer Tencent over Baidu/JD, which are rated 1-3 notches lower but trade only marginally wider/tighter.

RISKS & CATALYSTS

As of 07 Jan 2025

- While Chinese regulators have adopted a more friendly stance towards tech companies, any regulatory clampdowns abroad and domestically (e.g. antitrust rules, data security, personal information protection laws) may affect Tencent's business. Tencent's gaming, music streaming, and online payment units are among those that have come under regulatory scrutiny in the past.
- Tencent uses variable interest entities (VIEs) to circumvent China's restrictions on foreign ownership of Internet Content Providers, which poses regulatory risks. Specifically, VIE transactions involving "change in control" will be subject to antitrust regulatory processes.
- US-China tension may escalate under the new Trump Administration, including additional chip sanctions, which may result in higher volatility. Failing to secure a stable supply of advanced AI chips and/or find domestic alternatives could weigh on the long-term AI development of Tencent against international peers.

CREDIT QUALITY SCORE (CQS) ²

As of 13 Jan 2025

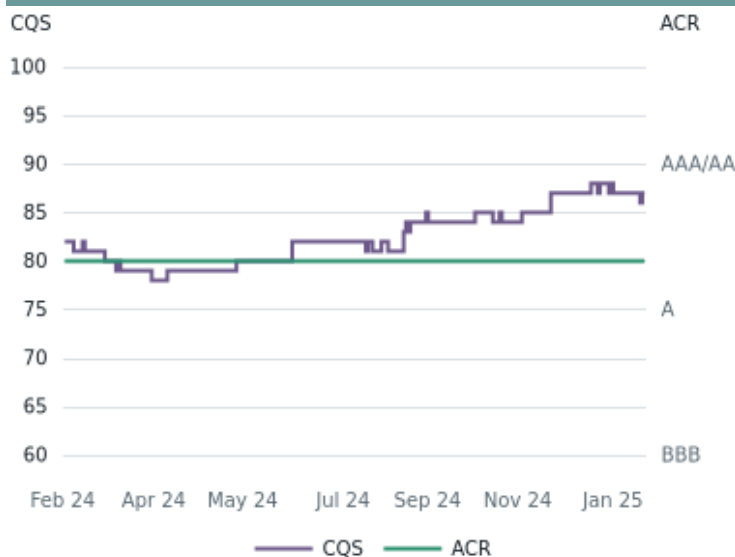
CURRENT CQS

87

CQS OUTLOOK ³

NEGATIVE STABLE POSITIVE

HISTORICAL RATINGS: AVERAGE AGENCY RATING (ACR) ⁴ VS CQS



KEY METRICS

As of 07 Jan 2025

RMB BN	FY20	FY21	FY22	FY23	LTM 3Q24
Debt to Book Cap	25.2%	27.0%	31.4%	29.8%	26.3%
Net Debt to Book Cap	4.0%	6.0%	8.5%	1.0%	0.5%
Debt/Total Equity	33.7%	36.9%	45.9%	42.5%	35.7%
Debt/Total Assets	19.7%	20.1%	22.8%	23.5%	20.3%
Gross Leverage	1.4x	1.7x	1.9x	1.6x	1.3x
Net Leverage	0.2x	0.4x	0.5x	0.1x	0.0x
Interest Coverage	24.8x	24.7x	19.0x	19.9x	22.2x
EBITDA Margin	38.3%	34.9%	34.3%	38.9%	41.9%

Year-end: 31 December.

BUSINESS DESCRIPTION

As of 07 Jan 2025

- Founded in November 1998, Tencent is a leading provider of Internet value added services in China. Since its establishment, Tencent has ventured into instant messaging, social networking, online payments, digital entertainment, and PC and smartphone gaming. Most recently, it has also forayed into high-tech areas such as artificial intelligence, and cloud computing.
- Tencent's leading Internet platforms in China include Weixin/WeChat (online messaging), QQ Instant Messenger (online messaging), Tencent Games (gaming), Tencent Video/Weixin Video Accounts (video platforms), WeChat Pay (payments), and Tencent Cloud. The combined monthly average users (MAU) of Weixin and Wechat reached 1.38 bn as of 30 Sep 2024.
- In 3Q24, 49% of revenues came from Value Added Services (which consist of Domestic Games, International Games, and Social Networks), 32% came from FinTech and Business Services (e.g. commercial payments and cloud), 18% from Online Advertising and 1% from Others.
- Tencent is currently primarily listed on the Hong Kong Stock Exchange, with a market capitalization of HKD 3.9 tn as of 10 Dec 2024.

GLOSSARY

- The Fundamental View** is our current assessment of credit quality and our expectation of how credit quality will trend over the next year or longer.
 - The Credit Quality Score (CQS)** is a number between 5 and 100. It is a medium-term credit score for corporates and financial institutions that utilizes a combination of sector fundamental scores and equity market signals. Values of CQS above 50 generally indicate investment grade credit quality.
 - The Credit Quality Score (CQS) Outlook** is the near-term (3 month) outlook for the CQS, based on its trend, volatility and distance from the adjacent CQS risk bucket.
 - The Agency Composite Rating (ACR)** is the average senior unsecured rating from one or more major rating agencies.
- Quantitative scores provided by CreditSights Analytics, LLC. Scores are shown are for the lesser of (1) 2 years and (2) date of CreditSights inception of quantitative coverage.

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