

# 11 bit Studios - Hold

Target Price: PLN 391.20 | Close as of 26/08/2020: PLN 488.00

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## 2Q'20 adj. figures slightly below our forecast

11 bit studios posted its 2Q'20 figures with following highlights:

- Revenues of PLN 19.7mn vs. PLN 18.2mn expected by us
- EBIT of PLN 9.1mn vs. PLN 6.5mn expected by us (positive impact of PLN 4mn linked to the incentive scheme recognition change)
- Net income of PLN 10.5mn vs. PLN 5.5mn expected, linked to the change in incentive scheme recognition and the decision of IP Box implementation
- **When our official net income forecast of PLN 5.5mn would be increased by no incentive scheme costs and IP Box recognition, we would be looking for the 2Q'20 bottom line of PLN 12.6mn, hence, reported bottom line in 16.5% below our estimates**
- Low effective tax rate in 1H'20 of 6.3%
- OCF of PLN 4.6mn vs. PLN 4.3mn year ago
- Net cash position of PLN 82.7mn vs. PLN 83mn in the previous quarter
- Capitalized development costs of PLN 18.8mn vs. PLN 14.3mn at the end of 1Q'20
- Off balance sheet liabilities of PLN 21.7mn vs. PLN 22.9mn in the previous quarter

Standalone, IFRS (PLN, mn)	Reported			Expected		Reported	
	2Q20	2Q19	y/y	Erste Group	Consensus	Erste Group	vs. Consensus
Revenues	19.7	16.6	19%	18.2	19.6	8.2%	0.5%
EBITDA	11.6	4.4	163%	8.9	11.5	30.4%	1.1%
EBIT	9.1	2.9	211%	6.5	9.2	40.5%	-0.5%
Net income	10.5	2.0	431%	5.5	8.9	90.6%	18.0%
EBITDA margin	58.8%	26.5%		48.8%	58.5%		
EBIT margin	46.3%	17.7%		35.7%	46.8%		
Net income margin	53.2%	11.9%		30.2%	45.3%		

Source: Company Data, PAP, Erste Group Research

## OPINION: SLIGHTLY NEGATIVE

**Second quarter figures of 11 bit studios came in below expectations, both on the operating and bottom line level, despite headline figures suggesting solid performance. That is mainly due to the fact, that the company will no longer recognize non-cash incentive scheme cost, which however was assumed in our estimates (originally, it should be recognize**

until the end of 2Q'20, but according to the company's calculations, it was fully recognize until the end of 2019. Hence, 2020 shouldn't be affected by the incentive scheme costs). If we assume that incentive scheme program cost was not included in our estimates, our EBIT forecast would amount to PLN 10.6mn vs. PLN 9.1mn reported by the company. Despite higher than expected revenues, operating profit is below our adj. expectations, which is primarily linked to higher than anticipated services cost and PLN 0.9mn donation to fight COVID-19. Net income came in at PLN 10.5mn with negative tax of PLN 1.7mn. When compared to our adjusted net income forecast of PLN 12.6mn, reported net income is down by 16.5% vs. our estimates (our official forecast of PLN 5.5mn increased by no incentive scheme cost and IP Box recognition). Nevertheless, PLN 0.9mn donation should be seen also as a one-off cost, which decreasing the scale of underperformance to 10.1% on the bottom line level. **Taking all of that into account, we are looking for rather slightly negative market reaction, despite the headline figures being in line with market expectations.**

The company announced that the publishing segment was responsible for c. 30% of sales in 1H'20 vs. 24% in 1Q'20, which suggest that the publishing revenues accounted for c. 40% of sales in the 2Q'20, above our expectations of 28%. In our quarterly forecast, we were looking for Children of Morta and Moonlighter sales of c. PLN 5.2mn, while based on the publishing segment share in the total sales; revenues from both titles came in at c. PLN 7.9mn. Company revealed some sales data about its key titles. Frostpunk sales since the release is currently close to PLN 110mn, Moonlighter sold in more than 1mn copies, while This War of Mine revenues are already above PLN 100mn. Conversion of Frostpunk players to season pass amounted to approx. 15%.

As a result of higher than anticipated publishing revenues, royalties costs came in at PLN 3.9mn vs. PLN 3.4mn expected by us, which led to higher than anticipated services costs of PLN 6.6mn vs. PLN 5.4mn in our forecast. Second reason of the underperformance on the operation level is PLN 0.9mn donation on COVID-19, which however should be seen as a one-off.

In line with a yesterday's announcement, 11 bit studios recognized IP Box for the 1H'20, which led to the required correction of the first quarter tax rate and negative effective tax rate in 2Q as a result. In the first quarter of the year, effective tax rate came in at 6.3%, which is a very solid figure compared to 7-9% on average reported by peers.

OCF came in at 4.6mn vs. PLN 4.3mn year ago, while net cash position increased to PLN 84mn vs. PLN 58mn year ago. The company revealed its off balance sheet liabilities amounted to PLN 21.7mn vs. PLN 22.9mn in the previous quarter. In the cash flow from investment activities, the company revealed it has granted its employees with PLN 4.1mn loan.

Finally, the company said that approx. 30 people are working currently on Project 8, while Eleanor project team is close to 20 people. As we already mentioned in dedicated flash note, we suspect Eleanor project is basically a Frostpunk 2, as the company should carry on with its successful franchise. Total employment at the end of June amounted to 148 people.

P & L (PLN m)	2Q19	3Q19	4Q19	1Q20	2Q20	YoY	QoQ	6M'19	6M'20	YoY
<b>Revenues</b>	<b>16.6</b>	<b>18.9</b>	<b>22.0</b>	<b>30.5</b>	<b>19.7</b>	<b>19%</b>	<b>-35%</b>	<b>30.8</b>	<b>50.3</b>	<b>63%</b>
Am&Dep	1.5	1.5	1.8	2.4	2.5	68%	4%	3.0	4.8	59%
Rawmaterials	0.1	0.1	0.1	0.1	0.1	-39%	-16%	0.2	0.2	-20%
Services	8.6	9.2	5.2	7.0	6.6	-23%	-5%	11.9	13.6	14%
Employee benefits	2.9	3.2	2.9	3.5	0.3	-89%	-91%	6.2	3.8	-39%
Taxes & charges	0.1	0.1	0.1	0.1	0.1	42%	26%	0.1	0.2	37%
Other expenses	0.6	0.2	1.1	0.4	1.0	77%	180%	0.7	1.3	90%
<b>Operating profit (loss)</b>	<b>2.9</b>	<b>4.6</b>	<b>10.7</b>	<b>17.2</b>	<b>9.1</b>	<b>211%</b>	<b>-47%</b>	<b>8.6</b>	<b>26.3</b>	<b>206%</b>
Financial revenues	0.1	0.4	0.4	1.4	-0.5	-430%	-135%	0.5	0.9	84%
Financial expenses	0.1	0.1	-0.1	0.8	-0.2	-333%	-123%	0.2	0.6	197%
Extraordinary gains/loss	0.0	0.0	0.0	0.0	0.0			0.0	0.0	
Profit (loss) before tax	3.0	4.9	11.2	17.8	8.8	194%	-50%	8.9	26.6	200%
Income tax	1.0	1.3	-0.6	3.3	-1.7	-263%	-150%	2.6	1.7	-35%
<b>Net profit (loss)</b>	<b>2.0</b>	<b>3.6</b>	<b>11.8</b>	<b>14.4</b>	<b>10.5</b>	<b>431%</b>	<b>-27%</b>	<b>6.3</b>	<b>24.9</b>	<b>294%</b>
Am&Dep	1.5	1.5	1.8	2.4	2.5	68%	4%	3.0	4.8	59%
<b>EBITDA</b>	<b>4.4</b>	<b>6.1</b>	<b>12.5</b>	<b>19.5</b>	<b>11.6</b>	<b>163%</b>	<b>-41%</b>	<b>11.6</b>	<b>31.2</b>	<b>168%</b>
Tax rate	34.2%	27.0%	-5.1%	18.8%	-19.0%			29%	6%	
EBITDA margin	26.5%	32.4%	57.0%	64.0%	58.8%			38%	62%	
EBIT margin	17.7%	24.3%	48.7%	56.3%	46.3%			28%	52%	
Net profit margin	11.9%	19.1%	53.6%	47.3%	53.2%			21%	50%	
<b>Main BS &amp; CF items</b>	<b>2Q19</b>	<b>3Q19</b>	<b>4Q19</b>	<b>1Q20</b>	<b>2Q20</b>	<b>YoY</b>	<b>QoQ</b>	<b>6M'19</b>	<b>6M'20</b>	<b>YoY</b>
OCF	4.3	16.7	5.0	24.3	4.6	6%	-81%	19.9	28.9	45%
FCF	1.7	13.1	-0.6	12.6	1.3	-26%	-90%	14.6	13.9	-5%
Total Assets	126.6	138.8	155.7	171.2	176.4					
Net debt (cash)	-58.0	-70.9	-70.5	-83.0	-83.7					
Equity	0.0	0.0	119.7	0.0	0.0					

Source: Company Data, Erste Group Research

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