

Friday, 26 May 2023 | research report

Huuuge Games: buy (new)

HUG.PW; HUGP.WA | Gaming, Poland

A Cash Generating Machine

We initiate coverage of Huuuge with a buy recommendation and a target price of PLN 36.50 based on DCF analysis and relative valuation.

In 2022, Huuuge's two flagship games, *Huuuge Casino* and *Billionaire Casino*, had a combined 5th ranking among the world's top earning casino games (#11 HC, #26 BC). At the moment the Company observes a slower decline in paying casino game users, accompanied by rising revenues. In H2'22, Huuuge cut user acquisition spend to 16% of revenue from 30% in H1'22, and there is still a couple of percentage points to be shaved off. After a recent write-down of the Traffic Puzzle game, with no plans boost spend on new users or development of the title, we assume its revenues will diminish, with greater focus put on the casino titles.

Huuuge cut about 20% of its headcount in the first four months of 2023 by closing the Traffic Puzzle studio, cutting marketing jobs, and collective redundancies in Poland. With this, coupled with lower UA expenses and a streamlined OPEX, we expect Huuuge to generate higher profits this year, with adj. EBITDA at a projected USD 100m even assuming lower revenue.

Huuuge is poised to launch a share buyback in June, distributing at least USD 150m to its shareholders (ca. 30% of current market cap) out of the estimated ca. USD 250m cash currently on the books. In the long term, we expect the Company to maintain an OCF/EBITDA ratio of ca. 80-85%. That, combined with low CAPEX, may translate into a negative enterprise value in 2029, therefore we expect Huuuge to start making regular distributions to its shareholders in cash or buyback form in the next years.

Our base-case scenario for Huuuge Games assumes a decline in casino game revenues at an annual rate of ca. 5%, accompanied by cost savings led by further job cuts. As far as other games, their contributions seem to be rapidly fading away. Recently, Huuuge has created independent teams, called "Pods," tasked with creating new games (or, revenue streams). Huuuge has a rather unremarkable track record so far with new game development that, and so we do not include any potential new titles in our future earnings forecast. Nevertheless, even with our projected revenue decline below Newzoo's 4% growth forecast for the whole mobile gaming market, there is no downside in our valuation of HUG.

Moreover, Huuuge is trading at a 30-40% discount to the vast mobile peer group based on 2023-25 3Y trailing P/E and EV/EBITDA ratios. Having in mind that M&A deals in gaming sector in the last 12 months were done at ca. 3.8x EV/S, and ca. 11.1x EV/EBITDA (i.e. at least 20-30% premiums to market valuations), HUG's discount looks even higher – on our 2023-25 estimates, the shares are trading at 1.7x EV/S and 5.4x EV/EBITDA.

With a roster of casino games capable of strong cash generation, after scaling back payroll costs and setting up teams to seek new revenue streams, Huuuge is set to outperform with its low CAPEX needs and expected cash distribution to the shareholders.

(USD m)	2021	2022	2023E	2024E	2025E
revenue	373.7	318.6	276.6	253.1	238.3
adj. EBITDA	64.4	82.3	100.2	84.1	76.6
margin	17.2%	25.8%	36.2%	33.2%	32.2%
EBIT	44.6	38.6	84.8	71.7	63.9
adj. net profit	41.1	64.6	75.8	61.9	54.3
P/E	-	15.5	7.1	10.0	11.5
P/S	1.5	1.6	1.9	2.4	2.5
EV/EBITDA	7.2	5.8	4.1	5.7	6.4
FCFF/EV	-	14.1%	19.5%	13.1%	10.7%
SBB/DPS (PLN)	0.00	0.00	7.48	3.29	2.64
Yield	0.0%	0.0%	28.3%	12.4%	10.0%

current price*	PLN 26.45
target price	PLN 36.50
mCap	PLN 2,228m
free float	PLN 1,256m
ADTV (3M)	PLN 1.8m

*Price as of May 25, 2023, 5:00 PM

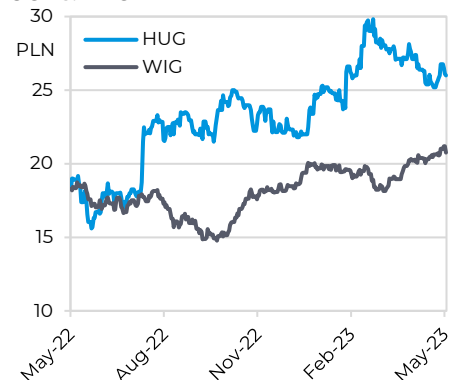
Ownership

Anton Gauffin	30.7%
The Raine Group	13.0%
Nationale-Nederlanden OFE	8.3%
NNLife OFE (f. MetLife OFE)	2.1%
Aegon OFE	1.0%
Uniqa OFE	0.8%
Aviva OFE	0.8%
Bankowy OFE	0.6%
Generali OFE	0.4%
others	42.3%

About Huuuge

Huuuge is a game developer and publisher. The Company creates free-to-play casual mobile games in which the players are able to chat, play and compete with one another in-game, and in real time (social aspect). Its most popular titles are *Huuuge Casino* and *Billionaire Casino*, which in 2022 ranked as the 11th and 26th top earning casino games worldwide. The two games between them accounted for ca. 90% of Huuuge's revenue in 2022. Huuuge employs ca. 360 people in Poland, ca. 50 in Israel, ca. 10 in the Netherlands, and ca. 30 in other locations.

HUG vs. WIG



name	target price		recommendation	
	new	old	new	old
Huuuge	36.50	-	buy	-

name	current price	target price	upside
	Huuuge	26.45	36.50

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List of abbreviations and ratios used by mBank:

EV (Enterprise Value) – Equity Value + Net Debt; **EBIT** – Earnings Before Interest and Taxes; **EBITDA** – EBIT + Depreciation & Amortisation; **Net Debt** – Borrowings + Debt Securities + Interest-Bearing Loans - Cash and Cash Equivalents; **P/E** (Price/Earnings) – Price Per Share Divided by Earnings Per Share; **P/CE** (Price to Cash Earnings) – Price Per Share Divided by Earnings + Depreciation & Amortisation; **P/B** (Price to Book Value) – Price Per Share Divided by Book Value Per Share; **P/CF** (Price to Cash Flow) – Price Divided by Cash Flow from Operations; **ROE** (Return on Equity) – Earnings Divided by Shareholders' Equity; **ROCE** (Return on Capital Employed) – EBIT x (Average Assets - Current Liabilities); **ROIC** (Return on Invested Capital) – EBIT x (1-Tax Rate) / (Average Equity + Minority Interest + Net Debt); **FCFF** (Free Cash Flow to Firm) – Cash Flow from Operations - CAPEX - Lease Payments; **FCFE** (Free Cash Flow to Equity) – Free Cash Flow to Firm - Net Interest Expense (incl. Debt + Leases)
EBITDA margin – EBITDA/Sales

OVERWEIGHT (OW) – a rating which indicates that we expect a stock to outperform the broad market
NEUTRAL (N) – a rating which indicates that we expect the stock to perform in line with the broad market
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HOLD – we expect that the rate of return from an investment will range from -5% to +5%
REDUCE – we expect that the rate of return from an investment will range from -5% to -15%
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NAV – valuation based on equity value, one of the most frequently used method in case of developing companies; the weak point of the method is that it does not factor in future changes in revenue/profits of a company.

mBank did not issue any recommendations for Huuuge in the 12 months prior to this publication.

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