

## DouYu International Holdings Limited - ADR (NASDAQ:DOYU)



**Champion Popular Investor  
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### Trading Statistics (USD)

<b>Market Cap (bb)</b>	3.61	<b>LTM EPS</b>	0.36	<b>Update Date</b>	28 Dec 2020
<b>Current Price</b>	11.26	<b>LTM P/E</b>	31.2	<b>Recommendation</b>	BUY
<b>52 Wk L - H</b>	6.11 - 17.85	<b>EV / EBITDA</b>	28.1	<b>Price Target</b>	NONE

### Business Description

DouYu is the second largest video game live streaming provider by revenues and market cap in China (behind Huya) and the largest in the world in number of users with 337 million users (as of December 2019). DouYu operates a similar business to Twitch (owned by Amazon) and is known as the Twitch of China. 37% of the company is owned by Tencent, which also owns 51% of Huya. Huya and DouYu are undergoing a merger of equals along with the video game streaming business of Tencent to form a behemoth (68% owned by Tencent), whereby the pro-forma company will own 80% of market share.

### Financial summary

	FY16	FY17	FY18	FY19	TTM
<b>Revenue (mm)</b>	114	286	531	1,038	1,347
<b>EBITDA (mm)</b>	-111	-90	-118	-6	88
<b>Margins</b>	-97.4%	-31.5%	-22.2%	-0.6%	6.5%
<b>Net Income (mm)</b>	-113	-93	-127	6	120
<b>Margins</b>	-99.1%	-32.5%	-23.9%	0.6%	8.9%

### Investment Thesis

#### Business Description:

DouYu operates a similar business to Twitch by enabling gamers to livestream while they are playing. Since Twitch and YouTube are banned in China, the market is really dominated by three main players, Huya, DouYu and Tencent video game streaming business. These three businesses are now going to merge.

Users can watch live streams for free but will need to be a paid user to live stream themselves. DouYu also makes money from ads with 91% of revenues coming from live streams in 2019 (vs 86% in 2018)

Both DouYu and Huya claim to be the market leader based on different metrics. If we look at revenues then Huya is bigger, although DouYu has more users and MAUs.

As of December 2019, DouYu had 337 million users with monthly MAUs of 165.8 million (vs 150.2 million for Huya) with 17.5 million paying users. Average MAUs in the third quarter of 2020 was 194.0 million.

DouYu also organizes tournaments and signs contracts with top streamers, which is different from what Twitch does in the West.

#### Catalyst:

China has the largest eSport market in the world with \$37.9 billion in revenues in 2018 (vs \$30.4 billion for the US) and is growing at 25% annually. As the market co-leader along with Huya, they are set to win from this trend even if the two companies don't merge.

However, we need to look at the merger and if there's opportunity for arbitrage.

The deal is an all stock one where each ADS of Douyu will be converted into 0.730 ADS of Huya. It is a merger of equals and the pro-forma company will have two co-CEOs (the current CEOs of each company). Tencent will own 68% of the new company. This deal is facing scrutiny from the Chinese Antitrust authorities.

On the day of the merger, both DouYu and Huya will each pay a special cash dividend of \$60 million and \$200 million respectively.

Right now the spread on the deal is 22.6% and since it is an all-stock deal, is dependent on the stock price of Huya.

### **Financial Analysis:**

The revenues of DouYu grew by 93% annually in the last 4 years. In 2019, the company had \$1.03 billion in revenues and in the TTM, this number grew to \$1.34 billion, an increase of 29.7% in just nine months. The live streaming revenues are contributing the most to this growth as the company is able to more than double its live streaming revenues every year.

DouYu only in 2018 had its first gross profit positive year and net income positive in 2019 at \$6 million. In the TTM the net income grew to \$120 million.

DouYu has a very good balance sheet with no debt at all and \$845 million in cash and cash equivalents after a very successful IPO last year raising \$775 million.

The total assets of DouYu are \$1.39 billion with \$1.25 billion in current assets. The total liabilities are \$306 million with \$297 million in current liabilities. The book value is \$1.08 billion.

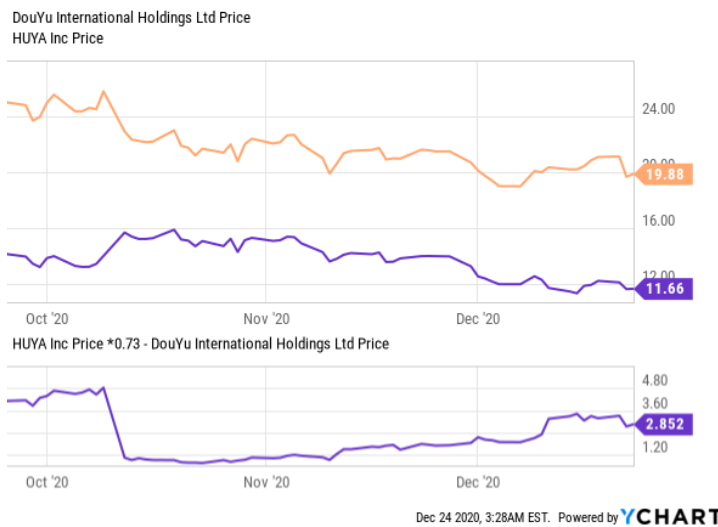
### **Valuation:**

We can already see that DouYu is a cheap stock with \$845 million in cash (and no debts) for a valuation of \$3.61 billion. The Net Current Asset Value of Benjamin Graham (Current Assets minus Total Liabilities) is \$948 million. For a fast growing technology company, this is cheap. Nevertheless, we can calculate the intrinsic value using the discounted owner's earning method.

From the cash flow statement, we can estimate about \$75 million in owner's earnings in 2019. In the TTM, the net income is about \$120 million, we cannot have the updated cash flow statements from the 10-Qs but we will estimate the owner's earnings at about \$150 million (that's conservative with a margin of safety). Let's give them an owner's earnings margin of 10%.

In the last 4 years, revenues grew by 93% annually, growing by 30% in the last 9 months. We will assume continuous revenue growth of 40% for the next 5 years, followed by 20% till year 15, then a terminal growth rate of 5% and use a discount rate of 15%.

Year	Revenues	Owner's Earnings	Discounted OE
2019	\$ 1,038	\$ 75	
<b>TTM</b>	\$ 1,347	\$ 150	
2021	\$ 1,886	\$ 189	\$ 164
2022	\$ 2,640	\$ 264	\$ 200
2023	\$ 3,696	\$ 370	\$ 243
2024	\$ 5,175	\$ 517	\$ 296
2025	\$ 7,244	\$ 724	\$ 360
<b>Terminal Value</b>			\$ 10,096
<b>Intrinsic Value</b>			\$ <b>11,359</b>



The uncertainty on this deal is high and that's why the stock price of Huya and consequently, DouYu are falling. But at the price at which DouYu is today, even without the deal, it is a good investment.

We are not going to look at an exit multiples table for this analysis since it is hard to predict what will happen to the stock of Huya in the coming year but the minimum amount of money we can make for the time being investing in DouYu is 22%. If the deal goes through (probability of 70%), then we're probably going to make more than 22%. However, if the deal doesn't go through, we will find ourselves with a deep value growth stock.

### Conclusion

I'll give a BUY rating on DouYu because either way this looks like a good investment. After the deal, we will need to assess Huya again to see if investing in it makes sense.