

## 11 bit studios

### Too many questions, too many risk factors

We cut our financial estimates for 11 bit studios, following weaker than expected release of The Invincible, surprising reveal of Indika (we expected large scope game with at least solid commercial potential, in our view, Indika doesn't meet any of these criteria) and below expectations performance of games, which we thought, had higher volume potential compared to Frostpunk 2. For example, **Cities: Skylines II**, as despite having **200k followers** on a release date (FP2 has currently 110k, we expect c. 130-150k on launch at the end of 2Q'24), the game sold in approx. **1.1mn unit within the first 5 months, what may imply 12M sales at c. 1.5-1.7mn i.e. below our 2.1mn forecast for FP2** (performance of CSII may be explained by weak reviews, however, it still cooling down our optimism). Recent launch of **Starfield** is a similar case, as **despite >400k followers on launch day, the game sold in c. 1.9mn copies within the first 6M which may lead to 12M sales at c. 2.4-2.7mn** – still rather not inspiring number vs. followers group. Additionally, we found that recent sequels like HF2, ARK2, or mentioned CSII are selling only slightly better than prequels – we now expect 48M sales volume of FP2 to come 26% above the first edition. Such sales performance is, in our view, linked to increasing **difficulty of today's gaming market**. Based on the newest data we found, since the beginning of 2023, there was just **31/16 releases of paid games that exceeded 1/2mn sales volume**, out of more than 15k games that were published on the Steam platform. While we remains optimistic in front of planned launch (mainly due to >2mn wishlist, and quality approach of 11 bit), recent development of the market / competitors justifies a **more cautious approach**, we believe.

Regarding the publishing division, we perceive the release of The Invincible as well as the reveal of Indika as disappointing, what **question the existence of the publishing business in its current form**.

Based on our estimates, 11 bit should deliver **net income of PLN 158/117mn in 2024/25**, a **P/E ratio of 9/12x**, incl. the release of P8 in '25, about which **we know nothing**. Later, profits are expected to decline **well below PLN 100mn level**. Despite attractive near term multiples, in the eye of highlighted risks, **uncertainty regarding P8**, growing **cost of development**, and the incomprehensible level of **involvement of the key management** which recently sold shares before the premieres, we slashed our recommendation to **Sell and TP to PLN 525.0/sh**.

PLN mn	2021	2022	2023e	2024e	2025e	2026e
Revenues	70.4	74.3	49.1	331.2	307.1	187.5
Adj. EBITDA	42.3	28.8	8.3	240.8	194.9	127.3
Growth %	-14%	-32%	-71%	2795%	-19%	-35%
Free cash flow	12.1	-13.7	-47.0	159.6	119.1	57.2
Growth %	53%	n/a	n/a	-439%	-25%	-52%
Net income	28.7	22.9	-4.1	158.0	116.8	72.3
DPS	0.0	0.0	0.0	0.0	19.9	14.7
DY	0.0%	0.0%	0.0%	0.0%	3.5%	2.6%
P/E	43.7	54.5	-1198.8	8.7	11.8	18.7
EV/EBITDA	30.8	46.1	165.2	5.0	5.9	8.8

Source: Company, Pekao Equity Research

**SELL** (Buy previously)

Target price

**PLN 525.0**

Upside to TP

**-6.6%**

Price on 04 March 2024

PLN 562.0

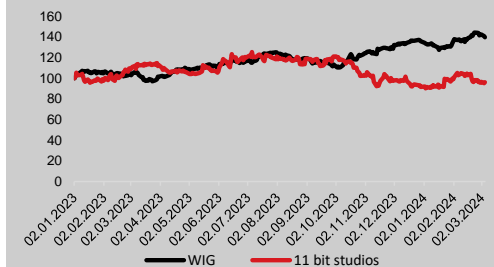
**ESG rating**

**B**

Final ESG score

**1.16**

Relative share price performance vs. WIG



#### UPCOMING EVENTS

4Q'23 report	April, 18
1Q'24 report	May, 23

#### STOCK DATA

Reuters/Bloomberg	11B.WA/11B.PW
Free float (%)	71.5
Market capitalization (PLN mn)	1,330
No. of shares in issue (mn)	2.4

Shareholders	TFI Allianz 9.51%
	G. Miechowski 6.97%
	Esaliens TFI 6.38%

Niniejszy raport stanowi skrót raportu przekazanego wcześniej klientom profesjonalnym i uprawnionym kontrahentom usługi sporządzania analiz inwestycyjnych BM Pekao w języku angielskim, a jego treść dostępna jest w aplikacji eTrader. Data pierwszej publikacji materiału: 07.03.2024 g. 07:00 Wyjaśnienie terminologii fachowej stosowanej w opracowaniu znajduje w zastrzeżeniach prawnych na końcu dokumentu.

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## Valuation

We carried out SOTP analysis to present intrinsic value of particular franchises, which together makes up the company's valuation. All cash flows and operating costs are discounted to present value, final valuation is adjusted by net debt/cash hold by the company and presented as a 12M target price per share. In addition we present a peer comparison and DCF model. Our target price is equally based on SOTP and DCF model.

### Key assumptions

- Risk free rate of 5.3%, Beta of 1.0, Equity Risk Premium of 6.0%
- 3.0% growth used in terminal
- TV FCFF calculated as an average 2024-29 FCFF
- USD/PLN of 4.0 in 2024 and thereafter, EUR/PLN of 4.40
- SOTP WACC of 10.5%
- EBIT adjusted for the non-cash incentive scheme cost
- Diluted number of shares used to calculate TP
- FP2 release expected by us in 2Q'24 with 4Y sales of 3.8mn copies
- The Alters premiere expected by us in 2Q'24, 4Y sales volume of 2.3mn
- Project 8 expected by us in 3Q'25 with 4Y sales of 2.8mn copies
- Other adjustments of PLN 1mn – market value of 11b's stake in Starward Industries
- ESG Rating: B – WACC risk premium impact (% of RFR) = - 7.5%

Based on our model value of particular franchises coupled with unassigned costs and PLN 33mn of net cash (as of the end of 2023e), translates into **SOTP valuation of 11 bit studios of PLN 1,155mn or PLN 522.2/sh.**

### Peer comparison

Company name	Ticker	P/E			EV/EBITDA		
		2024e	2025e	2026e	2024e	2025e	2026e
Electronic Arts Inc	EA US	18.6	16.6	14.7	13.8	12.7	11.2
Ubisoft Entertainment	UBI FP	11.5	10.1	8.3	3.7	3.3	3.6
Take-Two Interactive Software	TTWO US	24.2	16.7	15.8	22.1	15.9	19.4
Konami	9766 JT	23.1	21.6	21.6	11.8	11.0	11.0
Capcom	9697 JT	26.1	24.0	25.4	19.7	18.4	17.6
Tencent	700 HK	13.7	12.1	10.7	10.4	9.3	8.1
Square Enix	9684 JT	18.6	19.6	17.9	8.5	8.8	7.9
Paradox Interactive	PDX SS	26.8	21.5	19.1	10.0	9.4	9.0
Embracer Group	EMBRACB SS	4.8	4.1	3.9	3.4	3.1	3.3
Team17	TM17 LN	11.0	10.5	10.5	7.2	6.7	6.8
Nintendo	7974 JT	26.0	23.9	21.0	19.2	17.2	14.9
Bandai Namco	7832 JT	19.4	17.5	17.9	9.9	9.2	9.1
CD Projekt	CDR PW	35.3	54.3	93.6	20.1	29.5	44.9
Creepy Jar	CRJ PW	28.7	8.4	12.5	24.0	4.6	7.2
People Can Fly	PCF PW	n/a	9.8	10.2	35.0	4.8	2.6
PlayWay	PLW PW	13.4	13.2	12.1	9.5	9.4	8.7
<b>Median</b>		<b>19.4</b>	<b>16.7</b>	<b>15.3</b>	<b>11.1</b>	<b>9.4</b>	<b>8.9</b>
37 Interactive	002555 CH	11.2	10.0	4.0	9.2	8.1	7.0
Nexon	3659 JT	17.7	15.3	15.2	9.5	8.3	8.4
Playtika	PLTK US	10.4	9.8	9.9	5.5	5.2	4.4
Netmarble Corp	251270 KS	109.0	54.5	n/a	25.0	21.4	n/a
Huuuge	HUGE PW	6.7	7.3	7.8	2.8	2.3	1.6
Ten Square Games	TEN PW	7.5	7.7	7.8	4.9	5.2	5.4
<b>Median - mobile gaming only</b>		<b>10.8</b>	<b>9.9</b>	<b>7.8</b>	<b>7.3</b>	<b>6.7</b>	<b>5.4</b>
<b>Median total</b>		<b>18.6</b>	<b>14.2</b>	<b>12.5</b>	<b>10.0</b>	<b>9.0</b>	<b>8.1</b>
<b>11 bit studios</b>		<b>8.7</b>	<b>11.8</b>	<b>18.7</b>	<b>5.0</b>	<b>5.9</b>	<b>8.8</b>
<i>Premium/discount vs. Median</i>		<i>-53%</i>	<i>-17%</i>	<i>49%</i>	<i>-49%</i>	<i>-35%</i>	<i>9%</i>
<b>Implied value p.s. PLN</b>		<b>1200.4</b>	<b>684.2</b>	<b>378.1</b>	<b>1041.1</b>	<b>808.9</b>	<b>527.9</b>

Source: Bloomberg, Pekao Equity Research

**WACC calculation**

	2024e	2025e	2026e	2027e	2028e	2029e	Terminal Year
Risk free rate	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	4.0%
Equity risk premium	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	5.0%
ESG discount/premium	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%	-0.3%
Beta	1.0	1.0	1.0	1.0	1.0	1.0	1.0
<b>Cost of equity</b>	<b>10.9%</b>	<b>10.9%</b>	<b>10.9%</b>	<b>10.9%</b>	<b>10.9%</b>	<b>10.9%</b>	<b>8.7%</b>
Cost of debt	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	6.0%
<b>After-tax cost of debt</b>	<b>6.6%</b>	<b>6.6%</b>	<b>6.6%</b>	<b>6.6%</b>	<b>6.6%</b>	<b>6.6%</b>	<b>5.5%</b>
Equity weight	100%	100%	100%	100%	100%	100%	100%
<b>WACC</b>	<b>10.9%</b>	<b>10.9%</b>	<b>10.9%</b>	<b>10.9%</b>	<b>10.9%</b>	<b>10.9%</b>	<b>8.7%</b>

**DCF valuation**

(PLN mn)	2024e	2025e	2026e	2027e	2028e	2029e	Terminal Year
Revenues	331.2	307.1	187.5	152.2	122.7	346.1	
EBIT (excl. non cash incentive scheme cost)	176.2	130.3	78.3	50.7	17.1	157.5	
Taxes on EBIT	-15.9	-11.7	-7.0	-4.6	-1.5	-14.2	
<b>NOPAT</b>	<b>160.3</b>	<b>118.6</b>	<b>71.2</b>	<b>46.1</b>	<b>15.5</b>	<b>143.3</b>	
Depreciation and assets write-offs	64.6	64.6	49.0	39.1	37.5	69.6	
Change in NWC	2.0	0.2	1.1	0.3	0.3	-2.1	
Capital expenditures	-64.0	-65.0	-66.0	-67.0	-68.0	-69.0	2024-29 avg.
<b>FCFF</b>	<b>158.9</b>	<b>117.9</b>	<b>53.1</b>	<b>17.9</b>	<b>-15.2</b>	<b>146.0</b>	<b>82.2</b>
<i>Terminal value growth</i>							3.0%
Terminal value							1 484.6
<i>Discount factor</i>	0.90	0.81	0.73	0.66	0.60	0.54	0.49
Discounted free cash flow - Dec 31 2023	143.3	95.9	38.9	11.8	-9.1	78.5	774.7
<b>Enterprise value - Dec 31 2023</b>	<b>1 134.0</b>						
Minorities	0.0						
Net debt	-33.2						
Other adjustments	1.4						
<b>Equity value - Dec 31 2023</b>	<b>1 168.7</b>						
Number of shares (mn)	2.5						
<b>12M target price per share (PLN)</b>	<b>527.9</b>						
Share price as of March 4th (PLN)	562.0						
<i>Upside/Downside vs. current price</i>	-6.1%						

Revenues growth	6%	-7%	-39%	-19%	-19%	182%	n/a
EBIT margin	53.2%	42.4%	41.8%	33.3%	13.9%	45.5%	n/a
Tax rate	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%
Capex/revenues	19.3%	21.2%	35.2%	44.0%	55.4%	19.9%	n/a
Capex/depreciation	99.0%	100.6%	134.7%	171.5%	181.3%	99.1%	n/a

**Sensitivity of 12M target price per share to Terminal value growth & WACC**

	1.5%	2.0%	2.5%	3.0%	3.5%	4.0%	4.5%
<b>527.9</b>							
<b>7.0%</b>	535.3	573.0	619.1	676.6	750.6	849.3	987.4
<b>8.0%</b>	480.4	507.2	538.9	576.9	623.4	681.5	756.1
<b>8.7%</b>	451.0	472.8	498.1	<b>527.9</b>	563.4	606.5	659.8
<b>9.7%</b>	417.7	434.5	453.6	475.7	501.2	531.3	567.1
<b>10.7%</b>	391.6	405.0	420.0	437.0	456.3	478.6	504.4

**Sensitivity of 12M target price per share to Forstpunk 2 12M sales volume & USD/PLN**

	1.52	1.72	1.92	2.12	2.32	2.52	2.72
<b>527.9</b>							
<b>4.60</b>	515.8	576.3	636.7	697.2	757.7	818.1	878.6
<b>4.30</b>	442.1	498.9	555.7	612.5	669.4	726.2	783.0
<b>4.00</b>	368.5	421.6	474.8	<b>527.9</b>	581.0	634.2	687.3
<b>3.70</b>	294.8	344.3	393.8	443.2	492.7	542.2	591.7
<b>3.40</b>	221.1	267.0	312.8	358.6	404.4	450.2	496.0

Source: Pekao Equity Research

P&L (PLN mn)	2021	2022	2023e	2024e	2025e	2026e
<b>Revenues</b>	<b>70</b>	<b>74</b>	<b>49</b>	<b>331</b>	<b>307</b>	<b>187</b>
<b>Operating costs</b>	<b>39</b>	<b>49</b>	<b>45</b>	<b>153</b>	<b>175</b>	<b>107</b>
Other Operating Income/Cost	-2	-5	-3	-5	-5	-5
<b>EBITDA</b>	<b>39</b>	<b>26</b>	<b>5</b>	<b>238</b>	<b>192</b>	<b>124</b>
<b>EBITDA recurring</b>	<b>42</b>	<b>29</b>	<b>8</b>	<b>241</b>	<b>195</b>	<b>127</b>
<b>EBIT</b>	<b>30</b>	<b>20</b>	<b>1</b>	<b>173</b>	<b>127</b>	<b>75</b>
Financial Income/(Cost)	2	8	-6	0	2	5
<b>Pretax Profit</b>	<b>32</b>	<b>27</b>	<b>-5</b>	<b>174</b>	<b>129</b>	<b>80</b>
Income Tax	3	4	-1	15	12	8
<b>Net Income</b>	<b>29</b>	<b>23</b>	<b>-4</b>	<b>158</b>	<b>117</b>	<b>72</b>
<b>EPS (PLN)</b>	<b>11.51</b>	<b>9.14</b>	<b>-1.65</b>	<b>63.09</b>	<b>46.61</b>	<b>28.87</b>
Balance Sheet (PLN mn)	2021	2022	2023e	2024e	2025e	2026e
<b>Total Current Assets</b>	<b>129</b>	<b>102</b>	<b>50</b>	<b>245</b>	<b>313</b>	<b>318</b>
Cash and Equivalents	107	87	39	198	269	290
Other Current Assets	21	14	11	47	44	29
<b>Total Fixed Assets</b>	<b>91</b>	<b>143</b>	<b>200</b>	<b>200</b>	<b>200</b>	<b>217</b>
Tangible Assets	26	25	26	26	27	28
Other Fixed Assets	65	118	175	173	173	189
<b>Total Assets</b>	<b>220</b>	<b>244</b>	<b>251</b>	<b>445</b>	<b>513</b>	<b>535</b>
<b>Stockholders` Equity</b>	<b>197</b>	<b>225</b>	<b>223</b>	<b>384</b>	<b>457</b>	<b>497</b>
<b>Long Term Liabilities</b>	<b>9</b>	<b>9</b>	<b>8</b>	<b>7</b>	<b>6</b>	<b>5</b>
Long -Term Debt	8	6	5	4	3	2
Other Long - Term liabilities	1	3	3	3	3	3
<b>Short Term Liabilities</b>	<b>13</b>	<b>10</b>	<b>19</b>	<b>53</b>	<b>49</b>	<b>33</b>
Short -Term Debt	1	1	1	1	1	1
Other Current Liabilities	12	9	17	51	48	32
<b>Total Equity &amp; Liabilities</b>	<b>220</b>	<b>244</b>	<b>251</b>	<b>445</b>	<b>513</b>	<b>535</b>
Net debt	-99	-80	-33	-193	-265	-287
Cash Flow (PLN m)	2021	2022	2023e	2024e	2025e	2026e
Net Profit	29	23	-4	158	117	72
Depreciation and Amortisation	9	6	4	65	65	49
Other (incl. WC)	3	4	15	1	3	2
<b>Operating Cash Flows</b>	<b>41</b>	<b>33</b>	<b>15</b>	<b>224</b>	<b>184</b>	<b>123</b>
Capital Expenditures	-29	-47	-62	-64	-65	-66
Other	-9	18	0	0	0	0
<b>Cash Flows from Investing Activities</b>	<b>-37</b>	<b>-29</b>	<b>-62</b>	<b>-64</b>	<b>-65</b>	<b>-66</b>
Dividends paid	0	0	0	0	-47	-35
Other	-1	0	-1	-1	-1	-1
<b>Cash Flows from Financing Activities</b>	<b>-1</b>	<b>0</b>	<b>-1</b>	<b>-1</b>	<b>-48</b>	<b>-36</b>
Change in Cash	3	4	-48	159	71	21
<b>Cash at the end of period</b>	<b>107</b>	<b>87</b>	<b>39</b>	<b>198</b>	<b>269</b>	<b>290</b>
DPS (PLN)	0.00	0.00	0.00	0.00	19.92	14.72
Y/Y growth ratios						
Revenues	-20%	6%	-34%	575%	-7%	-39%
EBITDA	-24%	-34%	-79%	4335%	-19%	-35%
EBIT	-26%	-33%	-95%	17992%	-27%	-41%
Net profit	-23%	-20%	-118%	-3927%	-26%	-38%
EPS	73%	79%	-18%	-3827%	74%	62%
Margins						
<b>EBITDA</b>	<b>55.3%</b>	<b>34.8%</b>	<b>10.9%</b>	<b>71.8%</b>	<b>62.5%</b>	<b>66.3%</b>
EBIT Margin	42.7%	26.9%	2.0%	52.3%	41.5%	40.2%
Net Margin	40.8%	30.8%	-8.4%	47.7%	38.0%	38.6%
<b>ROE</b>	<b>14.5%</b>	<b>10.2%</b>	<b>-1.8%</b>	<b>41.1%</b>	<b>25.6%</b>	<b>14.6%</b>
Balance Sheet Ratios						
BVPS (PLN)	79.2	89.6	89.2	153.4	182.3	198.4
Net debt/EBITDA	-2.3	-2.8	-4.0	-0.8	-1.4	-2.3
Bank Debt/Equity	4.5%	3.4%	3.0%	1.5%	1.0%	0.7%

Source: Pekao Equity Research



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AB S.A. 3; Alior 3; Allegro 3; Astarta S.A. 3; Asseco Poland 3, 4; CCC 3; CD Projekt 3, 4; Cyfrowy Polsat 3, 4; Dino Polska 3; ENEA 3; ENERGA 3; GPW 3, 4; JSW 3; KGHM 3; LPP 3; Lotos 3; LW Bogdanka 4; mBank 4; Mercator 3; Orange Polska 3, 4; PGE 3; PGNiG 3, 4; PKN Orlen 3; PKO BP 3; PKP Cargo 4; Play 3; Santander Bank Polska 3; Tauron PE 3; Stalprodukt S.A. 3; WP Holding 4;

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Analyst	Position	Financial instrument	Number of instruments	Exposure (long/short)	Average transactions price	Transactions dates
Emil Popławski	Analyst	11 bit studios	0	n/a	n/a	n/a

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### **METHODS USED TO FORMULATE OUR RECOMMENDATIONS:**

Our company valuations are based on two valuation methods selected from among the following: discount model, multiples-based model or asset-based valuation method.

**Discount models** are characterized by simultaneous and comprehensive consideration of key determinants of intrinsic value, e.g. operating cash flow, capex, cost of capital (WACC). They are theoretically appealing and provide a direct computation of intrinsic value. However, discount model valuations are highly sensitive to changes in assumptions, particularly the risk free rate and terminal growth rate. Moreover, projections cannot be stated with certainty; unforeseen future events can cause income or earnings projections to be invalid.

**Multiples-based models** are based on the analysis of the valuation multipliers of a given company in relation to other similar companies in the industry. Among strengths of multiplier models we can highlight their simplicity, as they are easy to compute as well as to understand. Moreover, only the key statistics for investors are chosen for valuation. On the other hand, multiples are based on historic data or near-term forecasts. Valuations based on multiples will therefore fail to capture differences in projected performance over the longer term. Finally, it may be problematic to select a suitable peer group.

**Asset-based models** can be used even if a company has a brief record of earnings or its future existence is uncertain. However, it may be challenging to determine market value of some assets, particularly intangibles. Additionally, asset-based models do not take into account future changes in financial results, nor do they include non-balance sheet items, such as know-how.

Valuation models are dependent on macroeconomic factors, such as interest rates, exchange rates, raw materials, and on assumptions about the economy. Furthermore, market sentiment affects the valuation of companies. The valuation is also based on expectations that might change rapidly and without notice, depending on developments specific to individual industries. Our recommendations and target prices derived from the models might therefore change accordingly.

The investment ratings generally relate to a 12-month horizon. They are, however, also subject to market conditions and can only represent a snapshot. The ratings may in fact be achieved more quickly or slowly than expected, or need to be revised upward or downward. In the tables and charts throughout this report, we designate the years with an "E" to denote that the figures presented are forecasts and estimates.

### **Definition of ratings used in our publications:**

We currently use a three-tier recommendation system for the stocks in our formal coverage: Buy, Hold, or Sell (see definitions below):

A **Buy** is applied when the expected total return over the next twelve months is higher than 15%.

A **Hold** is applied when the expected total return over the next twelve months is within the range of 0% to 15%.

A **Sell** is applied when the stock's expected total return over the next twelve months is negative.

We employ three further categorizations for stocks in our coverage:



**Restricted:** A rating and/or financial forecasts and/or target price is not disclosed owing to compliance or other regulatory considerations such as blackout period or conflict of interest.

**Coverage in transition:** Due to changes in the research team, the disclosure of a stock's rating and/or target price and/or financial information are temporarily suspended. The stock remains in the research universe and disclosures of relevant information will be resumed in due course.

**Under review:** A rating and/or financial forecasts and/or target price is at the moment under revision of an analyst and the previous rating and/or financial forecasts and/or target price should not be relied on.

**Not rated:** We do not issue company-specific recommendations and we do not plan to issue them in the foreseeable future.