BRYAN, GARNIER & CO

FOCUS
TMT CONFERENCE

16th March 2016

TMT

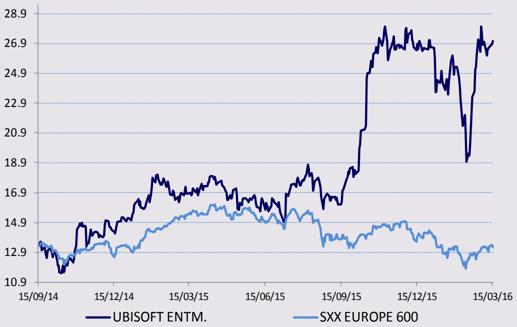
Ubisoft

Play again or end of the independent game?

Fair Value EUR34 (price EUR27.07) **BUY**

Bloomberg	UBI.FP
Reuters	UBIP.PA
12-month High / Low (EUR)	28.1 / 14.9
Market capitalisation (EURm)	3,010
Enterprise Value (BG estimates EURm)	3,065
Avg. 6m daily volume ('000 shares)	406.9
Free Float	88.5%
3y EPS CAGR	22.7%
Gearing (03/15)	-20%
Dividend yield (03/16e)	NM

YE March	03/15	03/16e	03/17e	03/18e
Revenue (EURm)	1,464	1,365	1,706	1,877
EBITA EURm)	161.1	138.0	218.0	289.9
Op.Margin (%)	11.0	10.1	12.8	15.4
Diluted EPS (EUR)	0.91	0.73	1.25	1.68
EV/Sales	1.92x	2.25x	1.67x	1.41x
EV/EBITDA	4.3x	5.2x	3.9x	3.1x
EV/EBITA	17.5x	22.2x	13.1x	9.2x
P/E	29.7x	36.9x	21.7x	16.1x
ROCE	12.7	8.0	13.8	18.5



During meetings with Ubisoft's management (CFO and IR) at our TMT conference, half of the time was spent discussing the company on a stand-alone basis, and the other half on Vivendi's entry into the share capital with the direct and indirect implications. Ubisoft again stated that its FY 2018/19 financial targets are based on cautious assumptions and that it intends to remain independent in the interests of all of its shareholders. We maintain our Buy rating and FV of EUR34 (our FV is a minimum price in the case of takeover bid).

- **Ubisoft is currently one of the main video game publishers worldwide.** It boasts three of the Top 4 biggest-ever new IPs in this demanding industry (in our view, thanks to its in-house development strategy in particular). The group is benefiting from the disappearance of some of its competitors and from its improvement towards digital. Following its latest successful release, *Tom Clancy's The Division*, **the group is demonstrating that it is one of the few players able to operate big online games** (high-quality games, with strong online infrastructure and services). This is a **major point to prepare for the group's future and make its FY 2018/19 targets credible** (digital is its main operating leverage, and notably digital contents).

- **Our meetings with Ubisoft have strengthened our view on the current fiscal year**, namely that thanks to *Far Cry Primal* and above all *The Division*, **the group could even meet its previous FY15/16 guidance** (the recent profit warning reducing sales from EUR1,465m to ~1,360m and non-IFRS EBIT from >=EUR200m to ~EUR150m). In addition, **we predict that *The Division* could be the first Ubisoft game in history to reach the 15m unit threshold on a 12-month basis.**

- **Regarding Vivendi,** management said that it did not need Vivendi to continue to grow, and that managing talents in the video game industry is quite different from managing pure creative people in the media world. **We reiterate that a public offer on Ubisoft has to be friendly** and that **it is essential that the CEO remains at the head of the gaming division** (for Vivendi not to take any risk of acquiring an empty shell).

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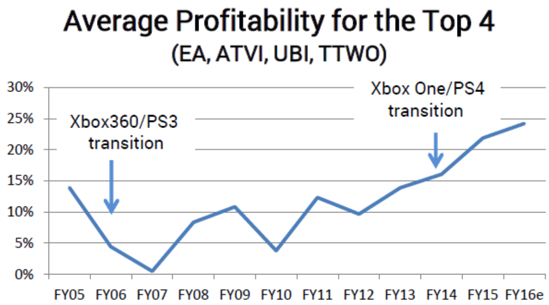
Ubisoft: Key Focuses from BG's TMT Conference

1. One Chart



Sources: based on Ubisoft consensus and Thomson One.

- The video game sector is historically highly correlated to the console cycle. **However, it has transformed into a more recurring and profitable industry.** Indeed, during the last console cycle transition (Xbox One and PS4 releases at end-2013), video game publishers were particularly resilient in terms of profitability compared to the previous cycles (they even improved their margins Y/Y). **This was mainly the result of the sector consolidation** (Atari, THQ, Konami, Namco Bandai, Capcom, Square Enix have either disappeared or are almost out of the market) **and the growing transition towards digital** (gamers are increasingly comfortable with downloading games, all the more so with the highly connected home consoles). According to management, **a digital game generates around EUR6-8 in incremental EBIT compared to a packaged game**.

- Ubisoft is lagging behind its competitors in digital contents but is in line with the industry average regarding digital distribution. **The clear operating leverage in digital therefore stems from digital contents** as they are even more profitable than their most profitable games (80-100% in EBIT margin, on our estimates). **That's why Ubisoft intends to launch more strong multi-player titles** (these include more digital live services).

- As a reminder, **Ubisoft's plan out to 2018/19 plan** (EUR2.2bn in sales, 20% in non-IFRS EBIT margin and ~EUR300m in FCF) **is based on a gross margin of more than 80% via 1/ the release of around five AAA games generating a cumulative 40m units** (stemming only from existing franchises, and taking into account quantities that they have all already reached), **and 2/ the digital segment** (45% of its FY18/19 sales vs. 30% in FY15/16: 28% in digital distribution vs. 21% and 17% in player recurring investment vs. 9%). **We expect the vast majority of the EBIT margin improvement from 11% in FY15/16 to 20% in FY18/19 to come from gross margin** and ~2% from other P&L costs reductions (R&D, marketing and SG&A).

2. One Sentence

"We do not need Vivendi to succeed in the video game industry"

- **Asked at our TMT conference about Vivendi's entry into Ubisoft's share capital, management said that it did not need Vivendi to continue to grow** (in this respect, the overwhelming success of *The Division* is a good demonstration). As a reminder, Ubisoft boasts three of the Top 4 biggest-ever new IP launches in the video game industry (*Watch Dogs*, *Assassin's Creed* and *The Division*) and two of the Top 3 over the current cycle (*Watch Dogs* and *The Division*).

- **In Ubisoft's view, if ever Vivendi were to enter the Board of Directors** (next September at the AGM)**, this would only serve the interests of Vivendi shareholders and not those of Ubisoft**. Management added that **managing talents in the video game industry is quite different from managing pure creative people in the world of advertising, TV, cinema…** Indeed, developers are creative people but with a strong technology focus. In this respect, we agree with the group, especially in a sector like this where corporate culture is strong. **We believe that if Ubisoft were to be acquired by Vivendi, it would be essential to keep the current CEO** (Yves Guillemot) **at the head of the video game division** because he would guarantee that star developers would remain in place (i.e. that Vivendi would not risk acquiring an empty shell).

3. One Figure

15m

- During our TMT conference, **Ubisoft's management stated that there is no reason why a Ubisoft game could not reach 15m units at some time in the future, during its first year on the market** (whether it is *Assassin's Creed*, *Watch_Dogs*, *Far Cry* or *The Division*). **In this respect, we believe that *Tom Clancy's The Division* could be a historical first** (after having already sold through more copies in its first 24 hours than any previous title in the company history and having registered the biggest first 5 days ever for a new video game franchise with USD330m generated worldwide i.e. 4.5/5.5m units).

- **The group is now able to operate big online games**, i.e. to attract a large community of players with high-quality games (re. the good ratings given to *The Division* a few days ago by key media outlets), accompanied with one of the best live operations currently on the market (in terms of servers and the technology behind these services: e.g. *The Division* surpassed 1.2m peak concurrent users over its first weekend). **In our view, this is a major point in making the group's FY18/19 targets credible.** Moreover, note that **the group is conquering new territories such as Russia, Brazil, and some Asian countries.** For instance, if China, Taiwan and Hong Kong were put together, this would be Ubisoft's number 8 geographical area in terms of players for the last episodes of *Assassin's Creed* and *Rainbow Six*.

- **We particularly appreciate Ubisoft's strategy: 1/** its in-house development, which generates significant operating leverage on its main IPs (its major AAA games are the most profitable: margin of 55%+ above the breakeven point); **2/** its digital development (organically and through small targeted acquisitions); and **3/** its entertainment vision (well above the video game segment: merchandising, films, TV-series, books, the theme park… to broaden its gamer base).

4. How does the Conference impact our Investment Case

- **Our meetings with Ubisoft have strengthened our view on the current fiscal year (at end-March 2016)**, namely that thanks to *Far Cry Primal* (23th February) and above all *The Division* (8th March), **the group could even meet its previous FY15/16 guidance** (the recent PW reducing sales from EUR1,465m to ~1,360m and non-IFRS EBIT from >=EUR200m to ~EUR150m).

Simulation for *Far Cry Primal* and *The Division* on Q4 and FY15/16 (vs. last guid. and previous guid.)

2015/16	Q4		FY	
	Minimum	Maximum	Minimum	Maximum
Cumulated sell-in units for *Far Cry Primal* and *The Division* (m)	14	17	14	17
Revenue outperformance vs. last guidance	+7%	+30%	+3%	+13%
Average outperformance vs. previous guidance (before the PW)	+0.7%		+0.2%	

Sources: Bryan, Garnier & Co ests.

- **Beyond the current fiscal year, we maintain our scenario.** We believe that **Vivendi's entry into the Guillemot galaxy is bound to continue.** It now owns 15.66% of Ubisoft's share capital with ~13.90%e of voting rights (our FV of EUR34 for Ubisoft values the entire 2013-19e cycle), and 29.86% of Gameloft's capital with 26.63% of voting rights (it has launched a hostile takeover bid, raised from EUR6 to EUR7.2, whereas our FV of EUR6.7 was a minimum price). In our view, Vivendi's bid for Gameloft intends to force Ubisoft into discussions and convince the Guillemot family that there are synergies to be unlocked and that they can be partners. We reiterate our view that a **public offer on Ubisoft must be friendly** and that the **current CEO must remain at the head of the gaming division**. To succeed, **Vivendi has to be generous** (both for Gameloft and Ubisoft as they are run by the same family) **if it really wants to add a 5th pillar to its French media group**. Vivendi's net cash position of EUR6bn should help to reach an agreement, even if it could take some time.

Next Catalysts

- **FY 2015/16 earnings results:** the week of the 9th May

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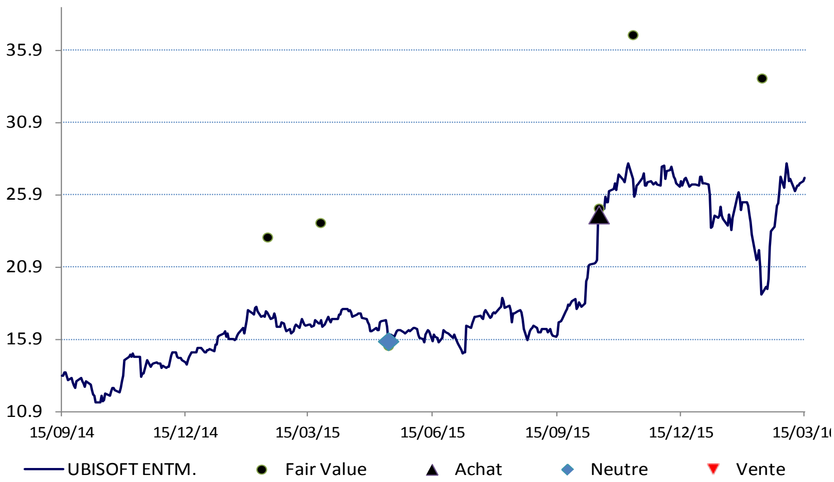
Price Chart and Rating History

Ubisoft



Ratings		
Date	**Ratings**	**Price**
15/10/15	BUY	EUR21.385
13/05/15	NEUTRAL	EUR15.8
09/09/14	BUY	EUR13

Target Price	
Date	**Target price**
12/02/16	EUR34
09/11/15	EUR37
15/10/15	EUR25
13/05/15	EUR15.5
24/03/15	EUR24
13/02/15	EUR23
09/09/14	EUR21

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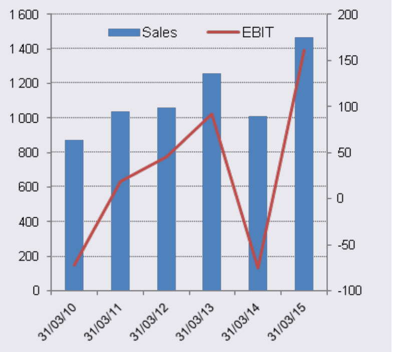
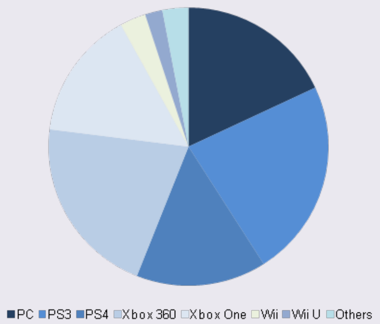


FY 2014/15e sales



Company description

Publisher, developer and distributor of video games, mainly positioned on consoles and PCs

Simplified Profit & Loss Account (EURm)	31/03/13	31/03/14	31/03/15	31/03/16e	31/03/17e	31/03/18e
Revenues	1,256	1,007	1,464	1,365	1,706	1,877
Change (%)	*18.4%*	*-19.8%*	*45.3%*	*-6.7%*	*25.0%*	*10.0%*
Ifl change (%)	*13.5%*	*-16.9%*	*41.6%*	*-9.8%*	*25.0%*	*10.0%*
EBITDA	458	309	650	585	730	853
EBIT	87.9	(97.9)	139	134	218	290
EBIT adjusted	92.2	(75.3)	161	138	218	290
Change (%)	*102%*	*-182%*	*-314%*	*-14.4%*	*58.0%*	*32.9%*
Financial results	4.0	10.3	0.71	(10.0)	(5.0)	(4.0)
Pre-Tax profits	91.9	(87.6)	140	124	213	286
Tax	(27.1)	22.1	(53.1)	(43.7)	(72.0)	(95.3)
Profits from associates	0.01	0.0	0.0	0.0	0.0	0.0
Minority interests	0.0	0.0	0.0	0.0	0.0	0.0
Net profit	64.8	(65.5)	87.0	80.8	141	191
Restated net profit	61.1	(59.0)	103	83.1	141	191
Change (%)	*127%*	*-197%*	*-275%*	*-19.4%*	*69.7%*	*35.1%*
Cash Flow Statement (EURm)						
Operating cash flows	415	285	648	543	665	766
Change in working capital	(24.6)	(37.2)	28.4	(208)	133	(8.2)
Capex, net	(400)	(454)	(478)	(568)	(581)	(563)
Financial investments, net	(9.7)	(28.6)	0.0	0.0	0.0	0.0
Dividends	0.0	0.0	0.0	0.0	0.0	0.0
Other	34.8	49.6	13.7	0.0	0.0	0.0
Net debt	(104)	14.8	(198)	54.7	(163)	(357)
Free Cash flow	(9.4)	(206)	199	(232)	217	194
Balance Sheet (EURm)						
Net fixed assets	740	794	783	909	966	954
Investments	4.3	3.6	4.2	4.2	4.2	4.2
Deffered tax assets	0.0	0.0	0.0	0.0	0.0	0.0
Cash & equivalents	238	238	657	95.9	313	508
current assets	54.4	94.7	42.3	248	123	135
Other assets	222	210	266	248	311	342
Total assets	1,257	1,339	1,752	1,505	1,716	1,942
L & ST Debt	133	253	459	151	151	151
Provisions	8.7	8.0	12.9	12.9	12.9	12.9
Deffered tax liabilities	0.0	0.0	0.0	0.0	0.0	0.0
Others liabilities	277	268	301	281	351	387
Shareholders' equity	838	810	979	1,060	1,201	1,392
Total Liabilities	1,257	1,339	1,752	1,505	1,716	1,942
Capital employed	734	825	782	1,115	1,039	1,035
Ratios						
Operating margin	7.34	(7.48)	11.01	10.11	12.78	15.44
Tax rate	29.47	25.21	37.90	35.08	33.80	33.34
Net margin	5.16	(6.51)	5.94	5.92	8.26	10.15
ROE (after tax)	7.73	(8.09)	8.88	7.62	11.74	13.69
ROCE (after tax)	8.81	(6.79)	12.66	7.97	13.78	18.51
Gearing	(12.47)	1.83	(20.19)	5.16	(13.53)	(25.64)
Pay out ratio	0.0	0.0	0.0	0.0	0.0	0.0
Number of shares, diluted	97,316	107,343	113,298	113,262	113,262	113,262
Data per Share (EUR)						
EPS	0.68	(0.62)	0.81	0.73	1.27	1.71
Restated EPS	0.63	(0.55)	0.91	0.73	1.25	1.68
% change	*123%*	*-188%*	*-266%*	*-19.4%*	*69.7%*	*35.1%*
BVPS	8.61	7.55	8.65	9.36	10.61	12.29
Operating cash flows	4.26	2.66	5.72	4.80	5.87	6.76
FCF	(0.10)	(1.92)	1.76	(2.05)	1.92	1.72
Net dividend	0.0	0.0	0.0	0.0	0.0	0.0

Source: Company Data; Bryan, Garnier & Co ests.

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SELL	Negative opinion for a stock where we expect an unfavourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential downside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.

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BUY ratings 64.4%   NEUTRAL ratings 28.1%   SELL ratings 7.4%

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