Media and Games Invest

Sector: Technology

The whole is greater than the sum of its parts

MGI Q2'21 results were well above our expectations. The organic growth came in at 36% in the quarter, above management's expectations. The Media segment is firing on all cylinders, and we do not believe that the share price has fully appreciated this, especially considering the high flying valuations of ad tech companies in the U.S.

Media powerhouse — building network effects and scale

The Media segment is becoming a real powerhouse, especially post the acquisition of Smaato. Verve Group. MGI's Media segment became one of the leading omnichannel exchanges worldwide and a top 10 mobile exchange through the acquisition. MGI has had an outspoken goal to increase the adjusted EBITDA margin in the Media segment to 15-20%. It is already on track to do this as the margin reached 16% in Q2'21. The Smaato acquisition will only accelerate this as Smaato has an adjusted EBITDA margin of ~33%. We believe MGI is building competitive advantages and powerful network effects through its vertical integration and scale.

Beating our high expectations and raised guidance

Q2'21 and H1'21 came in well above our high expectations, and as we stipulated in our Initiation of Coverage back in March 2021, the Media segment delivered strong organic growth and margin expansion. Games achieved organic growth despite having challenging comparables, and KingsIsle is also firing on all cylinders, growing faster than our internal expectations. We have raised our guidance following the strong performance, the acquisition of Smaato and MGI's own raised guidance.

M&A: Firepower & Pipeline

We estimate the potential M&A firepower to EUR ~305m, not accounting for equity raises. MGI thus has a lot of room for M&A, and the pipeline is well-filled with several interesting targets in sight. The Smaato acquisition highlights MGI's competency in M&A: Smaato was acquired at very low multiples and is a high-quality company. There was no bidding process and MGI's reach and network enabled them to acquire Smaato at a bargain.

+40% upside potential

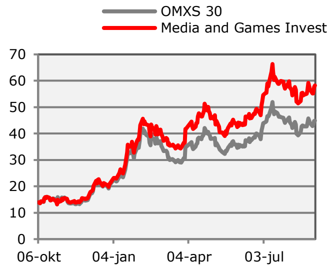
Redeye sees over a 40% upside potential in MGI from current levels. It can be argued the Media segment alone is worth SEK ~60 per share and that the Games segment is worth roughly SEK ~30 per share. Indicating a value of MGI north of SEK 90 per share based on our SOTP-valuation. We raise our Base Case to SEK 85 per share, indicating a upside potential north of 40%, supported by a SOTP and a DCF-valuation.

KEY FINANCIALS (EURm)	2018	2019	2020	2021E	2022E	2023E
Net sales	45	84	140	244	307	364
EBITDA	11	16	27	64	87	108
EBIT	3	5	11	37	56	76
EPS (adj.)	0.0	0.0	0.1	0.2	0.3	0.3
EV/Sales	0.0	0.9	5.8	3.3	2.7	2.2
EV/EBITDA	0.0	18.0	27.5	12.2	9.1	7.3
EV/EBIT	0.0	18.0	61.5	22.2	14.6	10.7
P/E	0.0	0.0	49.4	24	17	15

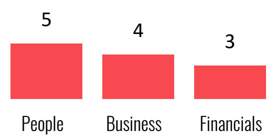
FAIR VALUE RANGE

BEAR	**BASE**	BULL
45	**85**	110

VERSUS OMXS30



REDEYE RATING



KEY STATS

Ticker	M8G
Market	First North
Share Price (SEK)	59.4
Market Cap (SEK)	8290
Net Debt 21E (MSEK)	150
Free Float	58%
Avg. daily volume ('000)	

ANALYSTS

Danesh Zare

danesh.dare@redeye.se

Tomas Otterbeck

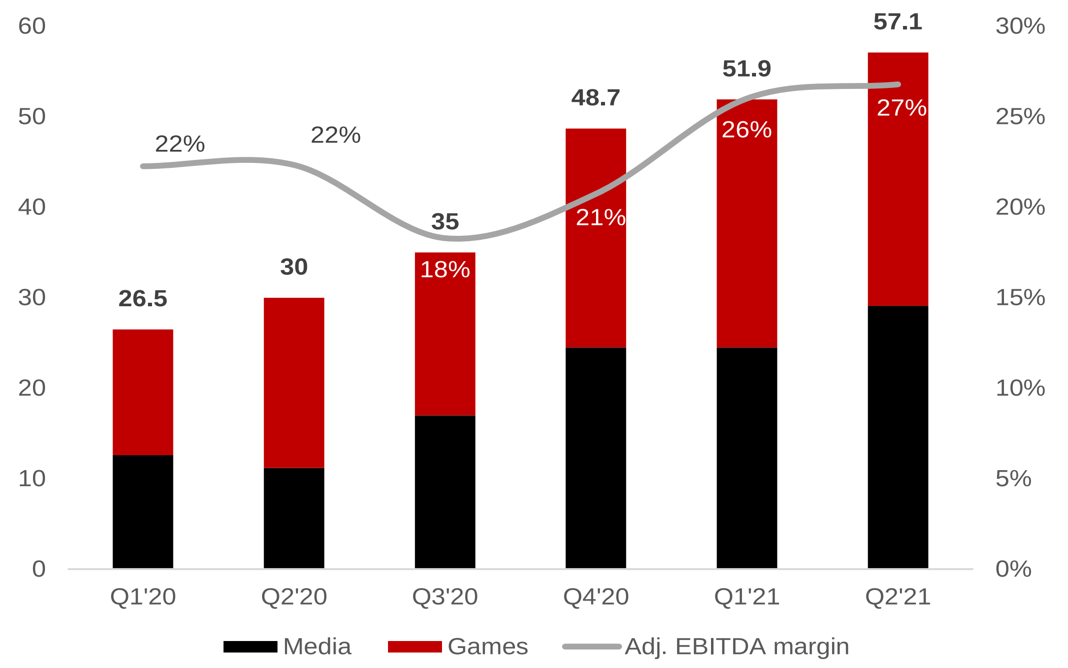
tomas.otterbeck@redeye.se

The whole is greater than the sum of its parts

Q2'21 and H1'21

MGI followed through with a strong quarter in Q2'21. A particularly impressive quarter for the Media segment, while Games had challenging comparables due to the pandemic last year. Revenues in Q2'21 amounted to EUR 57.1m (30), growing 90% year-over-year. The growth was mainly driven by unlocked revenue synergies within the group and recent M&A transactions, with KingsIsle contributing the most. Adjusted EBITDA amounted to EUR 15.3 (6.7) and grew even faster at an increase of 127% year-over-year. The sharp increase in profitability is mainly attributable to a strong showing from KingsIsle in combination with overall economies of scale. A large part of MGI's cost base is fixed to a degree. Personnel costs did not increase at the same rate as revenues did, for example. The adjusted EBITDA margin amounted to 27% in the quarter, up from 22% a year ago.

Net revenues & adj. EBITDA margin, Q1'20-Q1'21, EURm



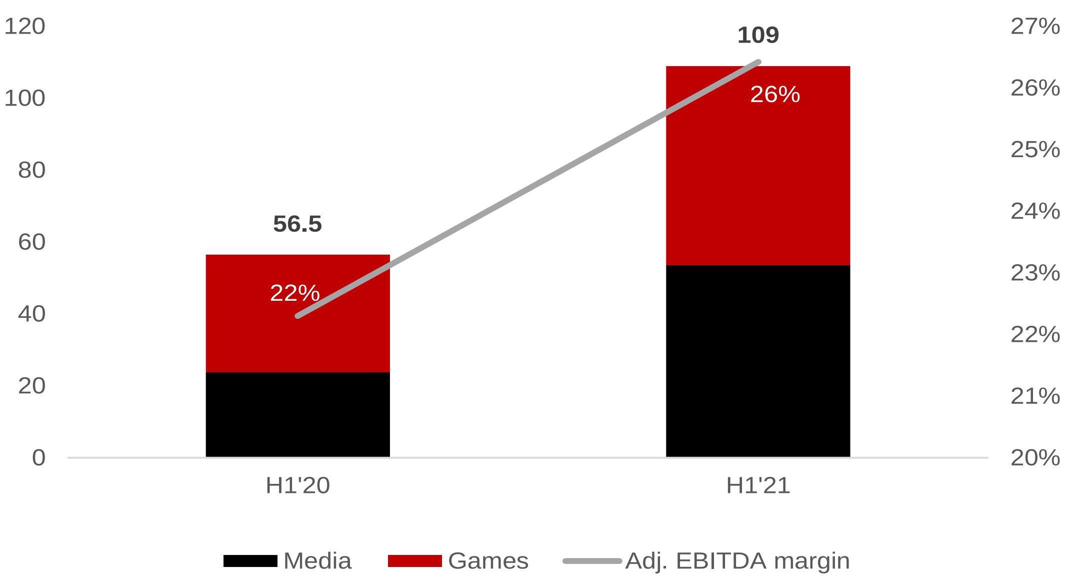
Source: Redeye Research

Media accounted for 51% of revenues in the quarter, while Games accounted for the rest. Media revenues grew 159% year-over-year and amounted to EUR 29.1m (11.2), while adjusted EBITDA amounted to EUR 4.7m (1.0), growing 370%, corresponding to an adjusted EBITDA margin of 16%, up five percentage points from a year ago. MGI's outspoken goal of increasing the adjusted EBITDA margin within the Media segment to 15-20% is thus already achieved. The acquisition of Smaato will be very accretive to the Media segment's bottom line as Smaato has an adjusted EBITDA margin of ~33%. Games revenues amounted to EUR 28m (18.8) and increased 49% year-over-year. Adjusted EBITDA within Games amounted to EUR 10.6m (5.5), corresponding to a growth of 93% and a margin of 38% (29%).

MGI managed to grow faster than its underlying markets, and we were particularly impressed by MGI's ability to achieve organic growth of 36% in the quarter. Albeit 26% organic growth came from the Media segment, which had softer comparables as advertiser's budgets were withdrawn during Q2'20. However, this highlights the benefit of having both Media and Gaming in-house as it acts as a natural hedge of sorts. Games stood for 10% of the organic growth, which is strong against the backdrop of last year's substantial influx of users to its games, which created quite challenging comparables. The organic growth was well ahead of management's expectations. MGI accredits organic growth within games to content updates, game launches and in-game ad revenues, and customer growth based on strong synergies with the media segment.

Revenues in H1'21 grew 93% compared to H1'20 and amounted to EUR 109m (56.5). At the same time, the adjusted EBITDA margin expanded five percentage points and amounted to 26% in H1'21. MGI keeps firing on all cylinders and is, again and again, reaffirming our positive outlook for the Company.

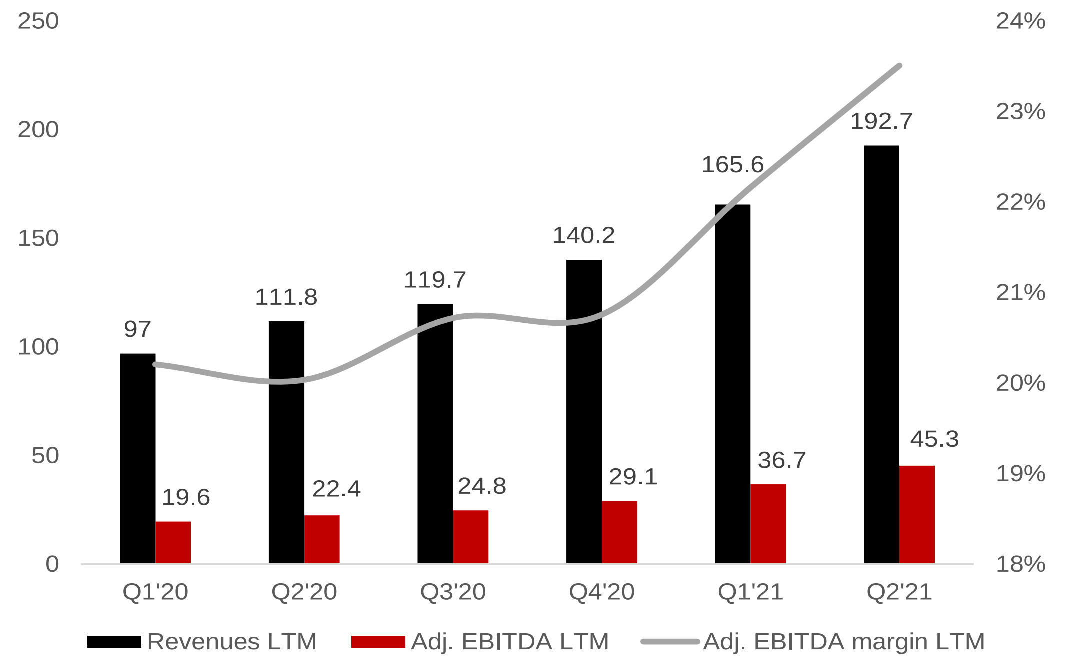
Net revenues & adj. EBITDA margin, H1'20-H1'21, EURm



Source: Redeye Research

LTM net revenues amounted to EUR ~193m, and adjusted EBITDA amounted to EUR ~45m, corresponding to an adj. EBITDA margin of ~24%.

Net revenues LTM & adj. EBITDA LTM, Q1'20-Q2'21, EURm



Source: Redeye Research

The Media segment has become an absolute powerhouse

The media segment has become a real powerhouse following the acquisitions in recent years. 85% of the revenues within Verve Group come from SaaS accounts, and Verve has a 95% retention rate of its SaaS accounts that generate over USD 100k per month. SaaS accounts grew 21% year-over-year in Q2’21. The SaaS revenues stem from platform fees and revenue share on the programmatic platforms. 75% of revenues come from platform revenue share, 10% come from platform fees, and the rest comes from individual bookings (flat cost-per-mille).

Acquisition of Smaato

MGI announced on July 13 that it is acquiring Smaato for an EV of EUR 140m, corresponding to a low multiple of 10.7x 2021E EBITDA and 6.8x 2022E EBITDA. This is a seemingly very low price point, especially when considering that Smaato’s organic growth is expected to reach 20% in 2021E. Ad tech peers trade at significantly more elevated EV/EBITDA multiples in the range of 20-40x 2021E EBITDA. We believe the acquisition to be highly value-accretive as Smaato is very profitable with an EBITDA margin of ~33%. Smaato is expected to increase MGI’s revenues by EUR 39m and EBITDA by EUR 13m in 2021E. Smaato will be consolidated from September 1, 2021.

Smaato had over 173 publishers on its platform with over USD 100k in gross revenue in 2020, up from 96 in 2019. Then retention rate within this cohort was 99% in Q1’21. The average gross revenue for its top 30 publishers in 2020 amounted to EUR 1.7m.

The acquisition seems to be an excellent addition to MGI’s Media segment due to several factors:

- MGI will become one of the leading omnichannel exchanges worldwide and a top 10 mobile exchange through the acquisition.
- Smaato adds significant capabilities on both the demand and the supply side, and we see a lot of potential for cross-selling.
    - On the supply side, MGI’s global reach amounted to 1.4 billion users before the Smaato acquisition. The combined entity is expected to increase the user reach by 30% to roughly 1.8-2.0 billion users. Smaato also contributes with a footprint in Asia, something that MGI lacked in the past.
    - The demand side is strengthened by the addition of over a hundred partners that Smaato has established a relationship with on the demand side. This should drive synergies through cross-selling, as MGI did not have an existing relationship with many of these partners.

- Smaato adds a lot of vertical integration within the Media segment by adding to its open exchange, SSP, and first-party data (SDK) capabilities. Before the acquisition, MGI had no real position on the web and mobile web supply side, which is now added and is as such also enabling further synergies with especially the still web-focused gaming side.

The value chain and vertical integration

MGI is vertically integrating within its value chain, especially within the Media segment, as seen in the matrix below. MGI offers a full-stack advertising technology platform that keeps growing both organically and through acquisitions. MGI is currently active throughout the whole ad-tech value chain.

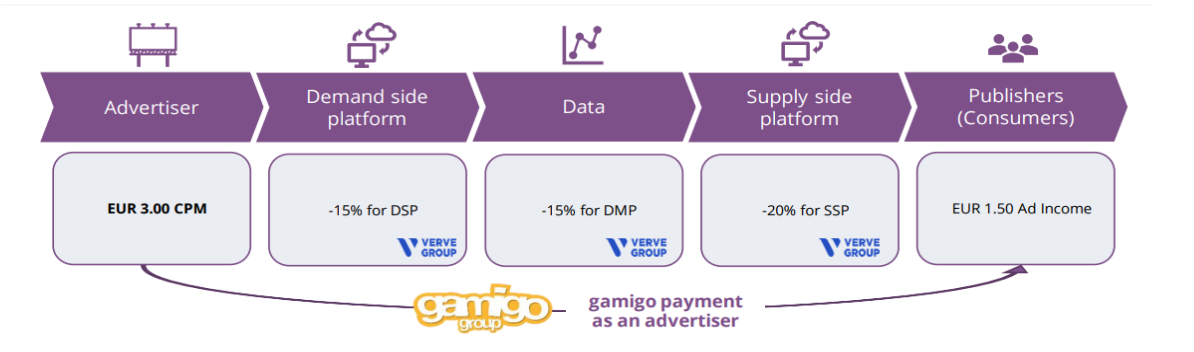
Differentiators vs. competitors

Topic	Description	MGI	Magnite	theTradeDesk	ironSource	PubMatic	APPLOVIN
Transparency/ Open Standards	Transparency in sourcing, pricing and operations, contrary to "walled gardens"	✓	✓	✓		✓	
Open Source Projects	Being open to the ecosystem and active participants in building open-source tech.	✓	✓	✓		✓	
DSP (Demand Side Platform)	Allows advertisers to programmatically manage multiple ad and data exchange accounts through a single interface.	✓		✓	✓		✓
DMP (Data Manage-ment Platform)	Platform where companies can identify audience segments, targeting, and ad campaigns.	✓					✓
SSP (Supply Side Platform)	Technology platform enabling web publishers & DOOH media owners to manage and offer advertising inventory	✓	✓		✓	✓	✓
Full Stack	Portfolio of products that are seamlessly integrated, driving end-end control and cost efficiencies to marketers.	✓			✓		✓
Mobile	Advertising on mobile devices such as smartphones or tablets	✓		✓	✓		✓
Web	Internet based advertising	✓	✓	✓		✓	
CTV (Connected TV) / **OTT** (Over-the-top)	Connected TV (Smart TVs and connected streaming devices) / Over-the-top (Distribution of video content via internet)	✓	✓	✓		✓	
O&O Owned and Operated Ad Tech	Access to a valuable pool of first-party data from users in an ecosystem of owned and operated media (games)	✓			✓		✓

Source: MGI Capital Markets Day, August 2021

Verve Group vertical integration means it is a part of the whole value chain of the programmatic platform; the demand-side platform (DSP), the data-management platform (DMP), and the supply-side platform (SSP). The programmatic platform is mostly monetized via revenue share, as can be seen in the diagram below. DSPs and DMPs typically have a take rate of 15%, while SSPs take 20%. What makes MGI truly vertically integrated is the synergies achieved via having its Games segment. Gamigo can act as both an advertiser and publisher, meaning the margin (which is quite significant) stays in-house.

MGI Ad tech value chain



Source: MGI Capital Markets Day, August 2021

The benefits include:

- Margin from ad buying stays in-house
- Efficient user acquisition (UA) for the Games segment, up to 50% cost savings for UA using internal Media segment (Verve Group). Increased ROI for user acquisition spend because of the use of first-party data. 89% of Gamigo's user acquisition came through its own media channels, increasing profitability.
- Gamigo's in-game ad inventory can be sold to advertisers
- Margin from ad selling stays in-house

Network effects through scale and reach

We believe that MGI is building powerful competitive advantages through network effects around its Media segment through its consolidation of businesses and vertical integration. The ad tech platform becomes more powerful and competitive the more advertisers (demand-side) and publishers (supply-side) are onboarded. More advertisers increase the attractiveness for publishers and vice versa. Thus, we think scale is critical, and we like that MGI is consolidating its media assets into one powerful platform in Verve Group.

Financial forecasts

MGI financial forecast 2021E

MGI unveiled its 2021E financial forecast post the Smaato acquisition, and it expects revenues of between EUR 234-254m and adjusted EBITDA of EUR 65-70m, corresponding to an adj. EBITDA margin of 28%. MGI predicted revenues of EUR 220-240m and adjusted EBITDA of EUR 60-65m in its initial guidance, excluding Smaato.

The EBITDA margin is in line with its previously announced mid-term financial targets (25-30% EBITDA margin), which were prudent. The revenue growth, however, is well above the target of 25-30% revenue CAGR. The guidance implicates a revenue growth of 67-81% year-over-year.

Proforma financials 2021E

We estimate the proforma financials 2021E for MGI by basing it on MGI's initial financial forecast, excluding Smaato. We have then added the full-year Smaato financial guidance communicated by MGI on top of that. The proforma financials below should not be compared to MGI's current guidance as the proforma contains Smaato's full-year guidance. MGI's updated financial forecast only includes one quarter from Smaato as it will be consolidated from September 01, 2021.

MGI proforma financials 2021E

EURm	MGI initial guidance	Smaato guidance	Proforma
Revenue	220-240	39	259-279
Adjusted EBITDA	60-65	13	73-78

Source: Redeye Research

Detailed financial forecast

We have outlined our detailed financial forecasts for 2021-23E below.

Media and Games Invest: Financial forecast '19-'23E									
EURm	2019	2020	Q1'21	Q2'21	Q3'21E	Q4'21E	2021E	2022E	2023E
Net revenues									
Total:	**83.9**	**140.2**	**51.9**	**57.1**	**61.2**	**74.8**	**244.0**	**307.4**	**364.4**
Adj. EBITDA									
Total:	**18.1**	**29.1**	**13.5**	**15.3**	**17.0**	**21.2**	**67.00**	**89.80**	**112.0**
EBITDA									
Total:	15.5	26.5	12.1	14.5	16	21.2	63.8	86.8	108.0
D&A exkl. PPA	(10.5)	(15.5)	(4.2)	(4.2)	(4.2)	(4.2)	(16.8)	(21.0)	(23.0)
Adj. EBIT									
Total:	**10.5**	**17.5**	**9.3**	**11.1**	**12.8**	**17.0**	**50.2**	**68.8**	**89.0**
PPA amortization	na	na	(2.6)	(2.6)	(2.6)	(2.6)	(10.3)	(10.0)	(9.5)
EBIT	5.0	11.0	5.3	7.8	9.2	14.4	36.7	55.8	75.5

Source: Redeye Research

Financial position - M&A firepower

The midpoint of the proforma financials in 2021E suggests that MGI's adjusted EBITDA will amount to EUR 75m. Net debt will amount to roughly EUR 150m after the cash out for the Smaato acquisition and the new bond framework. So the net leverage ratio will stand at roughly 2x adjusted EBITDA on a proforma basis. MGI targets a net leverage ratio of 2-3x, meaning it could potentially raise another EUR 75m in cash before hitting the ceiling of 3x. MGI's cash and cash equivalents will amount to roughly EUR 230m after the cash-out for Smaato and including the revolving credit facility (RCF) of EUR 30m. The total M&A firepower could therefore reach approximately EUR 305m, not taking equity into consideration. MGI is no stranger to equity raises, so we believe more significant future acquisitions would be made by using a mix of equity, debt, and cash.

M&A pipeline

The M&A pipeline is well filled, and MGI communicated its most promising takeover targets in conjunction with its Capital Markets Day (CMD) on August 21. MGI deems that part of the M&A targets in the diagram below are somewhat likely to be signed within the next six months.

Media and Games Invest: M&A pipeline			
Acquisition target	**Description**	**Revenues (EURm)**	**Profitability**
Mobile MMO publisher & developer	Own and licensed IP's	90-110	Profitable
Demand side platform (DSP)	Own IP	6-8	Profitable
Supply side platform (SSP)	Own IP	20-30	Profitable
Mobile casual and mid core games publisher	Own and licensed IP's	20-30	Profitable
Mobile MMO publisher & developer	Own IP	5-10	Profitable

Source: Redeye Research

Peer Valuation

Peer valuation

		EV/Sales			EV/EBITDA			Sales CAGR	EBIT CAGR	EBIT margin		
Company	**EV (MSEK)**	**2021E**	**2022E**	**2023E**	**2021E**	**2022E**	**2023E**	**20-23E**	**20-23E**	**2021E**	**2022E**	**2023E**
Nordics												
Embracer Group	92 189	5.5x	4.6x	4.2x	11.8x	9.9x	8.7x	35%	384%	30%	30%	29%
Paradox Interactive	19 972	11.1x	8.4x	7.7x	18.8x	13.4x	11.8x	11%	8%	33%	36%	37%
EG7	3 618	1.9x	1.7x	1.3x	6.9x	4.5x	3.1x	68%	N/A	19%	29%	34%
Remedy	5 121	11.1x	10.5x	7.6x	30.7x	30.4x	15.0x	17%	22%	34%	30%	36%
Stillfront	26 256	6.3x	5.6x	5.1x	17.6x	14.4x	12.8x	19%	24%	27%	30%	31%
G5 Entertainment	3 883	2.8x	2.4x	2.1x	10.0x	7.6x	6.3x	11%	31%	18%	22%	24%
Thunderful	4 647	1.2x	1.2x	1.2x	9.7x	8.3x	7.9x	4%	24%	9%	11%	12%
Median	**5 121**	**5.5x**	**4.6x**	**4.2x**	**11.8x**	**9.9x**	**8.7x**	**17%**	**24%**	**27%**	**30%**	**31%**
Mobile/Casual												
Zynga	84 966	3.4x	3.0x	2.8x	14.7x	12.3x	11.0x	16%	N/A	21%	22%	23%
Ten Square	8 135	5.0x	4.5x	4.0x	16.8x	14.6x	14.3x	14%	20%	32%	34%	35%
Com2us	5 445	1.3x	1.0x	0.9x	7.6x	4.8x	4.1x	15%	14%	16%	21%	22%
Rovio	3 832	1.4x	1.3x	1.2x	9.1x	8.0x	7.4x	3%	-2%	12%	14%	15%
Roblox	394 282	17.8x	14.5x	12.1x	65.6x	57.2x	44.7x	55%	N/A	21%	19%	21%
Playtika	105 628	4.6x	4.3x	4.0x	11.8x	10.9x	10.7x	6%	23%	29%	29%	29%
MTG	14 652	2.3x	1.7x	1.5x	15.4x	8.8x	7.5x	27%	120%	6%	12%	14%
Median	**14 652**	**3.4x**	**3.0x**	**2.8x**	**14.7x**	**10.9x**	**10.7x**	**15%**	**20%**	**21%**	**21%**	**22%**
Ad tech												
Magnite	43 564	10.8x	8.4x	6.9x	34.1x	25.4x	19.2x	40%	N/A	-7%	7%	9%
Applovin	253 784	10.7x	8.6x	7.1x	40.8x	29.9x	23.2x	38%	218%	9%	14%	17%
The Trade Desk	328 845	32.8x	25.4x	19.9x	84.9x	67.6x	51.3x	29%	45%	20%	22%	24%
PubMatic	12 853	7.2x	5.8x	4.7x	22.2x	18.8x	14.8x	26%	15%	16%	14%	16%
Viant	6 839	5.7x	4.6x	3.8x	26.0x	21.1x	14.8x	6%	20%	14%	14%	19%
Iron Source	83 472	18.8x	14.2x	10.7x	55.3x	43.1x	31.3x	37%	45%	21%	24%	27%
Median	**63 518**	**10.7x**	**8.5x**	**7.0x**	**37.4x**	**27.7x**	**21.2x**	**33%**	**45%**	**15%**	**14%**	**18%**
Peer Group median	**14 652**	**4.4x**	**3.8x**	**3.5x**	**14.7x**	**10.9x**	**10.7x**	**17%**	**24%**	**21%**	**21%**	**22%**
Media and Games Invest	**8 290**	**3.3x**	**2.7x**	**2.2x**	**12x**	**9x**	**7x**	**37%**	**90%**	**15%**	**18%**	**21%**

Source: Factset *Redeye Research

We divide our peer-valuation table into three peer groups: Nordic Gaming, Mobile/Casual, and Media/ad tech to better reflect the differences in valuation across the different segments. Media and Games Invest appears undervalued when looking at peers, albeit it is hard to find a direct peer. Valuation multiples are affected by expected growth, margins, the risk profile of the company, and return on capital (higher returns on capital suggests higher competitive advantages).

Nordic gaming companies are valued higher than international gaming companies on EV to sales ratios due to them being smaller and growing faster. Nordic investors have recently also started to appreciate gaming companies quite a lot, driving up multiples. We find this group to be the best peer group for MGI as it is listed on the First North stock exchange and is growing in line with this peer group. Although most of the Nordic Gaming peer group companies are mostly selling fully paid games, except for G5, Stillfront, and EG7, which have a lot of live services games similar to MGI.

Mobile/Casual gaming companies typically enjoy lower margins as the competition within the mobile gaming market is higher, and barriers to entry are lower. Therefore, mobile gaming companies are typically valued lower, despite the mobile gaming market growing faster than the gaming market overall. We do not find this peer group to indicate MGI's valuation, as only 6% of MGI's revenues are derived from mobile games. However, almost all of MGI's revenues are derived from free-to-play games, which is true for most mobile game companies. But MGI is focused on the MMOGs market, which has a very loyal player base and requires less investment into UAC.

As mentioned previously, the Nordic peer group is the closest to MGI since MGI is listed on a Swedish stock exchange, is growing faster, and is entering a phase of margin expansion.

Advertising technology (ad tech) companies are typically valued higher than gaming companies, and the media peer group is valued at a median of 13x sales in 2021E, compared to PC/Console gaming companies that are valued at a median of roughly 10-12x 2021E sales and 25-40x 2021E EBITDA with a median of 36x 2021E EBITDA. MGI's Media segment is growing fast while still being profitable in contrast to many of the ad tech companies within our peer group. MGI's Media segment is on track to increase its adjusted EBITDA margin, reaching ~21% in 2022E.

Closing the gap

Currently, MGI seems to trade at a considerable discount to peers, roughly ~30-40% discount to Nordic gaming peers based on EV/Sales multiples. In fact, we argue MGI should trade at a premium to the gaming companies as approximately 50% of MGI's revenues are derived from advertising, mostly from ad tech business models (over 88% from programmatic marketplaces). MGI only trades at 3.3x sales in 2021e while growing faster than the median of our peer groups. Looking at EV/EBITDA tells the same story: MGI is valued below peers while growing faster and, to a large extent, being an ad tech company, which typically enjoys much higher valuation multiples than gaming companies.

A catalyst for closing the gap will be the integration of the Smaato acquisition in 2022. And finally, we think the market has not yet fully appreciated the growing media segment and the synergies that the company enjoys by combining its media and gaming divisions. We believe the share price will close the gap when the network effects and the scalability effects within the Media segment become apparent. We believe the market will finally start valuing MGI closer to that of a Media company.

SOTP

We believe a sum-of-the-parts valuation is the most accurate way to value MGI due to the vastly different valuations within the two different segments that MGI is active within. Ad tech companies are currently valued at much higher multiples than gaming companies, and we believe that MGI's current valuation does not reflect the underlying value of its Media segment. We believe that just the Media segment alone justifies the current share price of SEK ~59.4 per share, as our SOTP-valuation implies that the Media segment could be worth SEK ~60 per share.

We believe the Media segment will account for roughly 53% of revenues in 2022E. The adjusted EBITDA margin within Media will amount to 21%, resulting in an adjusted EBITDA of EUR ~34m. We estimate that adjusted EBITDA in games will amount to EUR ~56m. Our ad tech peer table supports the Media EV/EBITDA multiple of 32x (the median of the ad tech peer group is 37x). We apply an EV/EBITDA multiple of 10x for the Games segment, in line with Nordic gaming peers. We keep our assumption quite conservative and value MGI slightly below peers even if MGI's sales and EBIT CAGR are higher than our peer groups. We discount the 2022E EBITDA back to today and apply a valuation multiple to this. Given our conservative estimates, we still derive a value of approximately SEK ~60 per share for the Media segment and SEK ~30 per share for the Games segment, after adding back the net debt of EUR ~150m. The SOTP-valuation supports a value of SEK ~90 per share for MGI, in line with our DCF valuation.

Media and Games Invest SOTP valuation 2022E (EURm)		EBITDA 2022E	EV/EBITDA	EV	EV/share
Media		34.2	32x	1095.0	7.3
Games		55.6	10x	555.8	3.7
Total:		**89.8**	**18.4**	**1650.8**	**11.0**
WACC	**9%**				
Discount factor	**0.89**				
Discounted	**1476**				**9.9**
Net debt	**150**				**1.0**
Equity Value	**1326**				**8.9**

Source: Redeye Research

DCF

We use a WACC of 9% across our three scenarios. MGI has an extensive track record of value accretive acquisitions. However, M&A is hard to estimate, and we maintain a conservative view of valuing MGI based on its current operations. Future M&A is cherry on top and provides nice optionality to the upside.

Bear Case 45 SEK

Sales '23: SEK 3345m
Sales CAGR '23-'31: 4%
Terminal growth: 2%
Avg. EBIT-m '23-'31: 18%
Terminal EBIT-m: 15%

Base Case 85 SEK

Sales '23: SEK 3956m
Sales CAGR '23-'31: 6%
Terminal growth: 2%
Avg. EBIT-m '23-'31: 23%
Terminal EBIT-m: 20%

Bull Case 110 SEK

Sales '23: SEK 4170m
Sales CAGR '23-'31: 7%
Terminal growth: 2%
Avg. EBIT-m '23-'31: 27%
Terminal EBIT-m: 25%

Investment case

An entrepreneur with skin in the game

The CEO and founder Remco Westermann have a lot at stake as he owns 33% of the Company's capital. The whole management team's incentives are aligned with the shareholders as they own large amounts of phantom stock and regular shares, which we view as very positive as it indicates that all of them have a long-term view. The CFO Paul Echt and board member Tobias Weitzel acquired a considerable number of shares in MGI during Q1 21.

MMOGs - Loyal player base

MGI is focused on the MMOG market, which is a market with higher barriers to entry due to the high initial development cost and recurring costs associated with MMOGs. MMOGs tend to have a very long lifespan, and the player base typically shows a high degree of stickiness, in contrast to casual games where "easy come, easy go" applies. It is not unusual for revenues from MMOGs to be generated from players that have been active for over five years, which lowers the operational risk of the Company as revenues are stable.

Games and Media synergies

User Acquisition (UA) is an important piece of the gaming puzzle, and the media segment has a natural fit with the gaming segment. UA is 200% more efficient through synergies as the UA cost (UAC) is lower, and the advertising-income is higher when it is done in-house. There are clear cost and data advantages gained via synergies. Data on important metrics are valuable for evaluating M&A targets when improving and monetizing current games in the portfolio and advertising within games. MGI has a lot of data and know-how from both segments.

Growth platform - Buy, Integrate, and Improve

MGI has a platform to grow from, which enables a low-risk business model. Acquired games have already been developed, and the bulk of the costs are behind them. The risk is lower since the game is already developed and has been proven in the market. MGI achieves a very high return on investment as it can integrate and improve these games via its platform and UA capabilities, leading to efficiency gains, economies of scale, and improved profitability for its portfolio of games.

Diversified and stable income streams

MGI's income streams are highly diversified, with income from both the games and media segments. MGI has a broad games portfolio and is not "hit-driven," and the concentration risk is low, as the largest game represents less than 25% of total revenues. MGI has over 30 MMOGs (Massive Multiplayer Online Games) and over five thousand casual games in its portfolio that are played by over five million active players. The game's revenues are very stable and predictable in nature as the games have a very long lifetime, lowering the overall risk profile as a gaming company.

A growing market with structural tailwinds

The gaming industry is the largest entertainment industry in the world today. Over 2.7 billion people play games, and the market is expected to grow with a CAGR of 8% between 2020 and 2023, and the total market is expected to surpass USD 159bn in 2020. It is eventually forecasted to exceed USD 200bn by the end of 2023. Mobile gaming is the largest gaming segment and is expected to grow the fastest. The opportunity is huge, and the gaming market is very fragmented with a vast amount of independent developers. MGI has recognized this and has carved out a niche in the market.

Catalysts

M&A

There are a lot of gaming companies that have an outspoken M&A strategy, and competition for gaming studios is high, with big players like Tencent, Microsoft, Amazon, Google, Embracer, Stillfront, EG7, and others all looking to consolidate the gaming market. There is a lot of competition in the M&A market for larger companies, but Media and Games Invest is focusing on the smaller A and AA segments of the market where there is less competition. Indeed, the companies mentioned previously are all eyeing much bigger game companies. In the near term, the focus will lie on acquiring gaming companies, but they also have and will acquire media companies. Value-accretive acquisitions through a business model that has been proven via their extensive track record. MGI's management is acutely aware of the risks and opportunities surrounding the gaming and media industries and is financially incentivized to continue the value-accretive journey. Future M&A is not included in our estimates nor valuation and thus provides nice optionality on the upside.

Integration and improvement of KingsIsle Entertainment and Smaato

The latest acquisition by MGI was a transformative one as the group EBITDA increase 63% and revenues increase 20% on a pro forma basis. MGI can unlock synergies and increase the profitability of the already profitable games Wizard101 and Pirate101. There is a lot of optionalities in porting the games to other platforms and in internationalizing the games as they only are available in NA and EU at the moment. Redeye is of the opinion that the markets have not fully priced in the acquisition. Perhaps due to "seeing is believing," and we, therefore, think that upcoming earnings reports with consolidated financials will be a catalyst.

Increased valuation on the capital markets

The share price has increased sharply (by over 220%) since the parallel listing on the First North stock exchange in October 2020, enabling MGI to tap into the equity markets to raise capital. This was evident from the acquisition of KingsIsle Entertainment, as MGI raised EUR 25m from a directed share issue. A higher share price means less dilution, and MGI previously has felt that its shares were too undervalued for equity issuance. This opens up more opportunities as the Company can acquire larger companies if they want.

Organic growth opportunities

There are a lot of opportunities for organic growth via cross-platform as MGI can launch many of the IPs in the current games portfolio on other platforms such as console and mobile. The bulk of the revenues are coming from NA and EU today. Thus, another growth opportunity is to internationalize and localize current games into other markets. MGI is currently porting its most successful game, Trove, to Switch. It is also launching Trove in South Korea, driving organic growth in 2021.

Internally developed games

One natural step for the Company is to start developing completely new games internally as it becomes larger. The revenue potential could be large if MGI can develop a sequel or a game based on a new IP. The risks are higher when developing games in-house. However, MGI has communicated that it does not expect to start developing games based on new IPs in the coming years.

Counter-thesis

Biting off more than they can chew

KingsIsle Entertainment is MGI's largest acquisition to date. The acquisition is transformative but also increases the risk. Larger acquisitions might prove to be the norm rather than the exception. It could prove to be risky if MGI acquires significant assets and overestimates said asset's lifetime value, albeit we view this risk as low, as MGI has acquired many companies in the past, with great success.

Concentration risks

Roughly 25 percent of total game revenues are expected to be derived from Wizard101. The concentration risk is, therefore, higher post-acquisition. Before the acquisition, the largest contributor to gaming revenue was Trove, making up roughly 18% of total game revenues in Q3 20. Albeit the concentration is higher, it is still quite low considering the group's total revenues, as Wizard101 only accounts for roughly 15% of total group revenues.

Spread to thinly

The Company acquires companies, and instead of having them act completely decentralized, the business model is to integrate and improve companies. This requires a lot of management attention and resources. Mergers are being carried out in many different countries, and this presents a lot of different challenges specific to certain markets. Regional differences in consumer behavior, different business models, competitive landscapes, and regulations are some examples of challenges that might arise.

Conflict of interest

MGI often markets direct competitors through its media segment. Trust is important, and the data that MGI receives from this must not be shared with the gaming segment. Separation of the business segments is very important. There are risks concerning customer relationships connected to this issue if the trust would somehow be tarnished. However, MGI keeps the media and games segments at arms lengths because of this, and the risk of this happening is low.

Privacy concerns

Privacy initiatives like GDPR and the coming update to Apple's iOS 14 are a threat to online advertisers. Targeted ads rely on the collection of user data in order to have high precision. Thankfully, MGI has a lot of first-party data and is also working on a technology called Verve Edge, which will solve many of the problems concerning privacy issues. Contextual targeting is also set to benefit due to the coming changes, and advertising within games provides quite a nice avenue for contextual ads.

Summary Redeye Rating

The rating consists of three valuation keys, each constituting an overall assessment of several factors that are rated on a scale of 0 to 1 points. The maximum score for a valuation key is 5 points.

People: 5

The management team is excellent as their track record speaks for itself. Over 30 companies have been acquired by the management team, and their acquisition has overall been very value-accretive. And all of them own a significant number of shares and are incentivized to do what is best for shareholders. The CEO and founder Remco Westermann own a vast amount of the company's capital (33%), and he has been with the company from the start. The launch of the ESOP will help retain key people within the management team, and our overall view of the management team is very positive.

Business: 4

The synergies that MGI obtains between its media and gaming divisions result in operational excellence. Revenues and adj. EBITDA has compounded at impressive rates, and we believe there is much more to come. The fit between the media and gaming segments is obvious, and the media division has grown into a real programmatic powerhouse. We expect continued growth and margin expansion in the future on the back of the recent acquisition, efficiencies, high degree of stickiness within its user base, and high growth within its media division.

Financials: 3

MGI has a history of a strong return on investment, revenue growth, and return on equity. The company has not been that profitable in the past but has recently become very profitable on an EBITDA level. We expect margin expansion on an EBIT and EBITDA level starting in 2021. The outlook for the programmatic advertising and the gaming markets is very positive, and we strongly believe MGI will benefit from this.

Redeye Rating and Background Definitions

Company Quality

Company Quality is based on a set of quality checks across three categories; PEOPLE, BUSINESS, FINANCE. These are the building blocks that enable a company to deliver sustained operational outperformance and attractive long-term earnings growth.

Each category is grouped into multiple sub-categories assessed by five checks. These are based on widely accepted and tested investment criteria and used by demonstrably successful investors and investment firms. Each sub-category may also include a complementary check that provides additional information to assist with investment decision-making.

If a check is successful, it is assigned a score of one point; the total successful checks are added to give a score for each sub-category. The overall score for a category is the average of all sub-category scores, based on a scale that ranges from 0 to 5 rounded up to the nearest whole number. The overall score for each category is then used to generate the size of the bar in the Company Quality graphic.

People

At the end of the day, people drive profits. Not numbers. Understanding the motivations of people behind a business is a significant part of understanding the long-term drive of the company. It all comes down to doing business with people you trust, or at least avoiding dealing with people of questionable character.

The People rating is based on quantitative scores in seven categories:

- Passion, Execution, Capital Allocation, Communication, Compensation, Ownership, and Board.

Business

If you don't understand the competitive environment and don't have a clear sense of how the business will engage customers, create value and consistently deliver that value at a profit, you won't succeed as an investor. Knowing the business model inside out will provide you some level of certainty and reduce the risk when you buy a stock.

The Business rating is based on quantitative scores grouped into five sub-categories:

- Business Scalability, Market Structure, Value Proposition, Economic Moat, and Operational Risks.

Financials

Investing is part art, part science. Financial ratios make up most of the science. Ratios are used to evaluate the financial soundness of a business. Also, these ratios are key factors that will impact a company's financial performance and valuation. However, you only need a few to determine whether a company is financially strong or weak.

The Financial rating is based on quantitative scores that are grouped into five separate categories:

- Earnings Power, Profit Margin, Growth Rate, Financial Health, and Earnings Quality.

Redeye Equity Research team

Management

Björn Fahlén
bjorn.fahlen@redeye.se

Håkan Östling
hakan.ostling@redeye.se

Technology Team

Jonas Amnesten
jonas.amnesten@redeye.se

Henrik Alveskog
henrik.alveskog@redeye.se

Fredrik Nilsson
fredrik.nilsson@redeye.se

Tomas Otterbeck
tomas.otterbeck@redeye.se

Oskar Vilhelmsson
oskar.vilhelmsson@redeye.se

Viktor Westman
viktor.westman@redeye.se

Forbes Goldman
forbes.goldman@redeye.se

Mark Siöstedt
mark.siostedt@redeye.se

Danesh Zare
danesh.zare@redeye.se

Mattias Ehrenborg
mattias.ehrenborg@redeye.se

Editorial

Mark Siöstedt
mark.siostedt@redeye.se

Joel Karlsson
joel.karlsson@redeye.se

Life Science Team

Gergana Almquist
gergana.almquist@redeye.se

Oscar Bergman
oscar.bergman@redeye.se

Anders Hedlund
anders.hedlund@redeye.se

Ludvig Svensson
ludvig.svensson@redeye.se

Niklas Elmhammer
niklas.elmhammer@redeye.se

Mats Hyttinge
mats.hyttinge@redeye.se

Filip Einarsson
filip.einarsson@redeye.se

Fredrik Thor
fredrik.thor@redeye.se

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Redeye Rating (2021-09-07)

Rating	People	Business	Financials
5p	23	18	3
3p - 4p	96	79	39
0p - 2p	6	28	83
Company N	125	125	125

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CONFLICT OF INTERESTS

Danesh Zare. owns shares in the company : Yes

Tomas Otterbeck. owns shares in the company : Yes

Redeye performs/have performed services for the Company and receives/have received compensation from the Company in connection with this.