BERNSTEIN
SOCIETE GENERALE GROUP

China Internet

Tencent Holdings Ltd

Rating

Outperform

Price Target

700.HK **780.00 HKD**



Robin Zhu
+852 2123 2659
robin.zhu@bernsteinsg.com



Charles Gou
+852 2123 2618
charles.gou@bernsteinsg.com



Min-Joo Kang
+852 2123 2644
minjoo.kang@bernsteinsg.com



Hyrum Caesar
+81 3 6777 6979
hyrum.caesar@bernsteinsg.com

Tencent: Two dots make a line? Quick thoughts on hy3

Hy3 officially released. On July 6, Tencent announced the official release of its Hy3 model. 10 weeks removed from the preview release, the updated model (still 295bn parameters, 21bn active) delivered meaningful improvements across key performance metrics. The benchmark slate Tencent published pointed to a model that delivered GLM-5.1 tier reasoning capabilities across tool call stability, hallucination control (12.5% to 5.4%), and multi-turn retention (MRCR 42.9% vs. 75.1%)… while deprioritising heavy-duty coding and general reasoning. The use of GQA also leaves room for improvement, for example by incorporating KV cache compression techniques like MLA or DSA.

A step in the right direction. Hy3 is not frontier, but GLM-5.1 level output across capabilities Tencent needs to build agentic services across its ecosystems is a credible step forward. We argued a couple of months ago that the significance of Hy3 was that it was the first act of Tencent's new AI team, and that having a credible pre-training, RL, and eval stack was as important for Tencent as headline parameter counts. The improvements made in the final Hy3 release felt confirmatory of that view. The benchmark results Tencent published also puts Hy3 clearly ahead of Minimax's M3 model. We still think a next iteration of Tencent's model (hopefully featuring a new pre-train) by late 2026 or early 2027 represents a sensible base case for the next step forward.

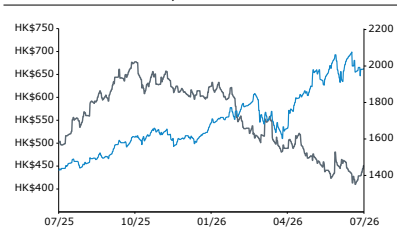
The capex debate is what it is, token spend fears feel overdone. Internet analysts globally have spent the past year watching their companies become more asset-heavy. Tencent has guided for capex to rise sequentially over the course of 2026, with associated implications for D&A costs. Where we think the bear case for Tencent's AI efforts has become overly punitive relates to token spend. Chatbot conversations typically consume hundreds of tokens, while agentic transactions require tens of thousands. Said differently, Tencent's token consumption only goes parabolic if agentic transaction volume and GMV take off. A time lag is likely between engagement and monetisation growth, but history suggests the latter is a matter of when not if.

Close Date	6 Jul 2026
700.HK Close Price (HKD)	452.00
Price Target (HKD)	780.00
Upside/(Downside)	73%
52-Week Range	683.00/411.00
ASIAX	1,979.72
FYE	Dec
Div Yield	1.2%
Market Cap (HKD) (B)	4,109.69
EV (HKD) (B)	3,587.55

Performance	YTD	1M	6M	12M
Absolute (%)	(24.5)	(0.3)	(27.6)	(10.0)
ASIAX (%)	21.1	0.2	16.2	38.4
Relative (%)	(45.6)	(0.5)	(43.8)	(48.4)

Source: Bloomberg, Bernstein estimates and analysis.

Price Performance, 1YR



Adjusted EPS	F25A	F26E	F27E
700.HK (CNY)	28.09	30.00	34.91

Financials	F25A	F26E	F27E	CAGR
Revenues (M)	751,766	828,757	917,101	--
Gross Profit (M)	422,593	480,299	536,643	--
Operating Earnings (M)	280,656	295,913	333,253	--
Net Earnings (M)	259,626	274,800	316,569	--

Valuation Metrics	F25A	F26E	F27E
Adjusted P/E (x)	13.9	13.1	11.2
EV/Sales (x)	4.1	3.7	3.4
EV/EBIT (x)	11.3	10.6	9.2

*Values shown in billions;Source: Bloomberg, Bernstein estimates and analysis.

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Consumer AI monetization - the US vs. China. Agentic commerce hype came and went quickly in the US. In contrast with the US, where Tiktok spent years trying to train consumers to click on shopping links, every kind of transactional intent already exists within China's Internet platforms. For Tencent, we expect the agentic AI roll-out to happen gradually, and expect monetisation to come via merchants (e.g. by gating access to and charging for agentic AI traffic) rather than consumers (see Doubao paying user ratios hovering around… zero). Merchants subscribing to the new agentic AI service get more traffic, more AI tools, more connectivity with different parts of Weixin… while those that don't get less of each.

Solving the harder problem? In our minds, the main conflict inherent to Tencent's AI efforts is the following. The company's extensively (and expensively) retooled AI team appears now to have made real progress realigning model training infra, but for a variety of reasons does not appear to get access to Weixin data. Meanwhile, our understanding is that the upcoming Weixin AI agent was built by the Weixin team independently of the former group. We assume this impasse will eventually be resolved through executive action… but why that hasn't already happened is probably a fair question for Tencent management.

INVESTMENT IMPLICATIONS

We rate Tencent Outperform (PT HK$780).

BERNSTEIN TICKER TABLE

			6 Jul 2026		TTM		Adjusted EPS			Adjusted P/E (x)		
			Closing	Price	Rel.							
Ticker	Rating	Cur	Price	Target	Perf.	Cur	2025A	2026E	2027E	2025A	2026E	2027E
700.HK (Tencent)	O	HKD	452.00	780.00	(48.4)%	CNY	28.09	30.00	34.91	13.9	13.1	11.2
ASIAX			1,979.72									

O - Outperform, M - Market-Perform, U - Underperform, NR - Not Rated, CS - Coverage Suspended

Source: Bloomberg, Bernstein estimates and analysis.

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Tencent Holdings Ltd

We value Tencent at HK$780 per share, on a 20x FY+1 (i.e. Quarters 5-8) PE multiple.

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Tencent Holdings Ltd

The main downside risks associated with Tencent include macroeconomic risks (e.g. credit, retail consumption), fluctuations in user engagement with its platforms, gaming and advertising demand competition with rival internet platforms, and regulatory risks – for example related to China's anti-monopoly regulations.

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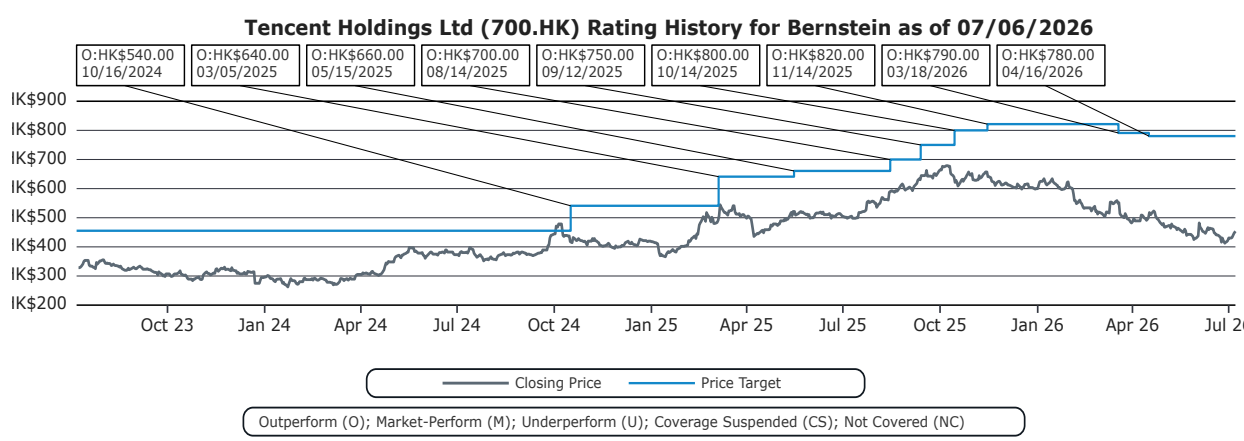
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Market-Perform (Bernstein Brand) Neutral (Autonomous Brand)	HOLD	35.8%	16.2%
Underperform	SELL	13.1%	13.6%

* These figures represent the percentage of companies within each equity rating category for which affiliates of Bernstein have provided investment banking services within the previous 12 months.
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