

Studio Dragon (253450 KS)

Media/entertainment


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Rating	BUY (M)
Target price	W114,000 (U)
Current price (Mar 16)	W97,000
Upside potential	18%

Market cap (Wbn)	2,720
Shares outstanding	28,037,240
Avg daily T/O (2M, Wbn)	23
Avg daily volume (2M, shrs)	308,743
52-week high (won)	97,700
52-week low (won)	57,800
Foreign ownership (%)	1.1
Major shareholders (%)	
CJ E&M & others	75.7

Stock performance

(%)	1M	3M	12M
Absolute	22.0	62.5	0.0
Relative	15.7	40.2	0.0
Abs (US\$)	23.3	66.1	0.0

Star player in content market

1Q18 preview

- We estimate 1Q18 consolidated gross profit at W18.5bn (+10% YoY), OP at W15.0bn (+7% YoY), and NP at W11.9bn (-11% YoY). OP will likely miss consensus by about 10%. In 1Q18, base effect was strong on robust 1Q17 domestic distribution revenue (VOD) from mega-hit TV series "The Legend of the Blue Sea" and "Guardian: The Lonely and Great God" and recognition of their distribution revenue in Japan and SE Asia. However, we believe 1Q18 OP will grow YoY, as the firm will book most of **"A Korea Odyssey" distribution revenue from Netflix (about W10.0bn) in 1Q18. Moreover, it is likely to book about 40% of "Live" distribution revenue from Netflix in 1Q18.** Given that there is a one-week holdback condition for its overseas streaming service, Live's distribution revenue for the first seven episodes will likely be booked in 1Q18. Despite modest overseas distribution revenue, domestic distribution revenue will likely fall YoY. Live's average viewer rating on tvN was just 5.4%, far below The Legend of the Blue Sea and Guardian. Moreover, a major actor in "Cross" stepped down amid sexual assault allegations, resulting in sluggish domestic VOD revenue. This is why we believe 1Q18 OP will miss consensus.

Netflix and Chinese OTT providers

- We estimate the price of **A Korean Odyssey for Netflix at \$0.5mn per episode**, far higher than that of "Stranger" and "Man To Man," which aired in 2017. **We expect the prices of Studio Dragon's new drama series to continue rising.** In addition, "Mr. Sunshine," a drama series written by Kim Eun-suk ("Descendants of the Sun" and "Guardian"), is set to air via tvN in Jul 2018. Before it airs, SE Asian over-the-top (OTT) content providers (iflix, Viu, etc) and Japanese platforms, as well as Netflix will compete to buy Mr. Sunshine. Moreover, if Amazon Prime, which is increasing investment in global content, joins in, the price should rise sharply. Fiercer competition among foreign OTT content providers to buy Korean content, would raise Studio Dragon's negotiation power significantly. Moreover, **investors should note that drama series distribution to Chinese OTTs will likely resume in 2018.** State-owned outlet Beijing News ran a feature story about Korea drama series on Mar 2 and 9, 2018. We believe this is a sign that the ban on Korean cultural products will be lifted soon. **Investors should factor in the possibility that Chinese OTT content providers will purchase Mr. Sunshine and "Memories of the Kingdom."** Production of Memories of the Kingdom is likely to finish before it begins to air. Given that it is scheduled to air in 4Q18, tvN and a Chinese OTT content provider may air the drama series simultaneously. In 2019, a blockbuster overseas drama candidate is "The Asdal Chronicle." Song Joong-ki is in talks to star in the pre-produced historical drama.

Quarterly earnings

(Wbn)	1Q18E	% YoY	% QoQ	Consens	vs consens (%)
Sales	85	12.3	17.7	92	-7.6
OP	15	7.0	331.0	16	-9.3
Pre-tax net profit	16	18.1	826.4	17	-5.6
Net profit, CI	12	22.9	493.6	16	-24.3
OPM (%)	17.7	-0.8 %pt	+12.9 %pt	18.0	-0.3 %pt
NPM (%)	14.0	+1.2 %pt	+11.2 %pt	17.1	-3.1 %pt

Source: Yuanta Securities

Forecasts and valuations (K-IFRS, consolidated)

	2016A	2017E	2018E	2019E
FY ends Dec				
Sales	154	287	381	481
OP	17	33	73	116
Net profit, CI	8	24	58	92
P/E (x)	-	99.4	46.7	29.7
P/B (x)	-	7.3	6.3	5.2
EV/EBITDA	-	75.3	33.5	20.3
ROE (%)	12.0	9.4	14.6	19.3

Source: Yuanta Securities

Revise up target price

We maintain BUY and revise target price from W90,000 to W114,000, which implies a target P/E of 35x and 2019E EPS of W3,270.

We estimate 2019 OP at W116.0bn, assuming the number of new drama productions at 33 in 2019, average project margin at 25% (excluding distribution revenue from Netflix and Chinese OTT content providers), and distribution revenue from Netflix at W50.0bn and that from Chinese OTT providers at W30.0bn. Given that the company has 77 writers as of end-2017, it will have no problem in producing 33 new dramas in 2019.

Studio Dragon: earnings forecast													(Wbn)
	2017				2018				Full-year				
	1Q	2Q	3Q	4Q	1QE	2QE	3QE	4QE	2015	2016	2017	2018E	2019E
No of TV series produced	-	-	-	-	-	-	-	-	16	19	22	27	33
[Assumption]													
- Netflix distribution rev x	-	-	-	-	-	-	-	-	-	-	-	30.0	50.0
- Chinese OTT dis rev	-	-	-	-	-	-	-	-	-	-	-	10.0	30.0
Revenue	75.3	62.1	77.5	71.9	84.6	72.3	114.2	109.5	97.4	195.5	286.8	380.6	480.6
- Programming	26.3	24.1	41.8	39.0	36.4	-	-	-	54.8	87.8	131.2	161.1	196.8
- Distribution	36.5	26.3	23.3	25.7	36.2	-	-	-	39.0	75.4	111.8	177.2	217.2
- Others	12.5	11.6	12.4	7.2	12.0	-	-	-	3.6	32.3	43.7	42.3	66.5
Growth (YoY)	-	-	-	-	12%	16%	47%	52%	-6%	101%	47%	33%	26%
- Programming	-	-	-	-	38%	-	-	-	-6%	60%	49%	23%	22%
- Distribution	-	-	-	-	-1%	-	-	-	-3%	93%	48%	58%	23%
- Others	-	-	-	-	-4%	-	-	-	-25%	797%	35%	-3%	57%
Domestic distribution revenue	13.9	10.2	10.2	10.3	10.0	-	-	-	15.1	31.2	44.6	-	-
Overseas distribution revenue	22.6	16.1	13.1	15.4	26.2	-	-	-	23.9	44.2	67.2	-	-
COGS	58.6	49.9	66.8	64.4	66.2	58.6	87.8	80.0	91.1	168.3	239.7	292.6	346.6
COGS-to-sales (%)	78%	80%	86%	90%	78%	81%	77%	73%	94%	86%	84%	77%	72%
Gross profit	16.8	12.2	10.6	7.4	18.5	13.7	26.4	29.4	6.3	27.2	47.0	88.0	134.0
Gross margin	22%	20%	14%	10%	22%	19%	23%	27%	6%	14%	16%	23%	28%
SG&A expense	2.8	3.3	4.0	4.0	3.5	3.5	3.5	4.5	3.7	6.0	14.1	15.0	18.0
SG&A-to-sales (%)	4%	5%	5%	6%	4%	5%	3%	4%	4%	3%	5%	4%	4%
Operating profit	14.0	8.9	6.6	3.5	15.0	10.2	22.9	24.9	2.6	21.2	33.1	73.0	116.0
Operating margin	19%	14%	9%	5%	18%	14%	20%	23%	3%	11%	11%	19%	24%
Pre-tax profit	13.2	9.0	6.4	1.7	15.6	11.1	24.0	26.1	-	-	30.3	76.9	120.9
Pre-tax margin	18%	14%	8%	2%	18%	15%	21%	24%	-	-	11%	20%	25%
Net profit	13.4	2.8	5.7	2.0	11.9	8.4	18.2	19.8	-	-	23.8	58.3	91.7
Net margin (%)	18%	5%	7%	3%	14%	12%	16%	18%	-	-	8%	15%	19%
Growth (% YoY)													
Revenue	-	-	-	-	12%	16%	47%	52%	-6%	101%	47%	33%	26%
Operating profit	-	-	-	-	7%	15%	244%	619%	-38%	715%	56%	121%	59%
Net profit	-	-	-	-	-11%	200%	222%	890%	-	-	-	144%	57%

Note: Studio Dragon was split off from CJ E&M in May 2016; figures for 2016 include CJ E&M's drama production division earnings for January~April; pre-split-off earnings were supervised by KPMG Korea, Source: Yuanta Securities

Per-episode price of Korean TV series purchased by Netflix

Production	Title	Broadcaster	No of episodes	Aired	Per-episode price
Studio Dragon	Stranger	tvN	16	2017.06.10~2017.07.30	\$200,000
	A Korea Odyssey	tvN	20	2017.12.23~2018.03.04	\$500,000 (est)
Drama House	Man to Man	JTBC	16	2017.04.21~2017.06.10	\$350,000
FNC Add Culture	My Only Love Song (web drama)	-	20	-	\$75,000

Source: Media reports, Yuanta Securities

Sales price of hit Korean dramas to China over 2014~2017

Title	Broadcaster	Aired	Production	Per-episode price (\$'000)	Buyer
My Love from the Star	SBS	2013.12~2014.2	HB Entertainment	35	iQIYI
The Next Three Days	SBS	2014.3~2014.5	Goldthumb Pictures	50	Youku Tudou
Doctor Stranger	SBS	2014.5~2014.7	Aura Media	80	Youku Tudou
It's Okay, That's Love	SBS	2014.7~2014.9	GT Entertainment, CJ E&M	120	Youku Tudou
Fated to Love You	MBC	2014.7~2014.9	No.3 Pictures, Pageone Film	120	Sohu
My Lovely Girl	SBS	2014.9~2014.11	Acetory	200	Youku Tudou
Bad Guys: Reloaded	OCN	2014.10~2014.12	Urban Works	100	Youku Tudou
Pinocchio	SBS	2014.11~2015.1	IHQ	280	Youku Tudou
Hyde Jekyll, Me	SBS	2015.1~2015.3	KPJ, H E&M	100	Youku Tudou
The Producers	KBS2	2015.5~2015.6	Chorokbaem Media	200	Sohu
Descendants of the Sun	KBS2	2016.2~2016.4	NEW	250 + RS	iQIYI
Uncontrollably Fond	KBS2	2016.7~2016.9	Samhwa Networks, IHQ	250	Youku Tudou
Moon Lovers	SBS	2016.8~2016.11	Wind	400	Youku Tudou
While You Were Sleeping	SBS	2017.9~2017.11	IHQ	400	Tencent

Note: "While You Were Sleeping" has 32 episodes as SBS introduced premium commercials (PCM). The per-episode price above is 16-episode transferred.

Source: Media reports, Yuanta Securities

Studio Dragon: peer valuation of earnings and valuation

	Ticker	Unit	Mkt cap	2017E			2018E			2019E		
				Revenue	OP	NP	Revenue	OP	NP	Revenue	OP	NP
Studio Dragon	253450 KS	(Wbn)	2719.6	286.8	33.1	23.9	380.6	73.0	58.3	480.6	116.0	91.7
Jcontentree	036420 KS	(Wbn)	896.6	420.3	33.3	6.4	587.5	60.8	35.0	706.3	75.0	46.2
CJ E&M	130960 KS	(Wbn)	3582.7	1750.1	63.2	428.6	2028.2	132.7	140.5	2188.1	164.7	172.2
Netflix	NFLX US	(\$mn)	138,191	11,681	834	749	15,843	1,589	1,435	19,413	2,575	2,073
Hauce	300133 CH	(\$mn)	3,496	843	110	101	1,063	140	125	1,276	183	163
Huayi Brothers	300027 CH	(\$mn)	4,272	608	150	141	761	193	171	900	227	201
HualuBaina	300291 CH	(\$mn)	1,575	336	-	43	389	-	55	435	-	63
Zhejiang Talent	300426 CH	(\$mn)	1,298	214	48	35	266	71	70	335	95	93
New Culture	300336 CH	(\$mn)	960	211	51	46	302	74	65	375	92	76
				2017E			2018E			2019E		
				P/E	P/B	ROE	P/E	P/B	ROE	P/E	P/B	ROE
Studio Dragon		(x, %)		99.4	7.3	9.4	46.7	6.3	14.6	29.7	5.2	19.3
Jcontentree		(x, %)		83.8	3.1	5.0	25.6	4.3	18.4	19.4	3.5	20.0
CJ E&M		(x, %)		8.0	1.7	23.9	25.5	1.6	6.8	20.8	1.5	7.5
Netflix		(x, %)		188.7	40.8	17.7	103.6	30.1	26.0	65.3	21.6	28.0
Hauce		(x, %)		34.3	3.2	9.4	28.1	2.9	10.7	22.1	2.6	12.6
Huayi Brothers		(x, %)		31.6	2.7	9.4	25.9	2.5	10.0	23.4	2.2	10.8
HualuBaina		(x, %)		26.7	1.5	4.4	21.5	1.5	5.3	15.4	1.4	5.9
Zhejiang Talent		(x, %)		26.4	6.6	17.9	16.3	5.0	26.7	13.1	3.7	26.7
New Culture		(x, %)		19.6	2.0	9.7	14.9	1.8	12.0	12.5	1.5	12.8
Chinese peer avg		(x, %)		27.7	3.2	10.1	21.4	2.7	13.0	17.3	2.3	13.7

Note: Figures for Studio Dragon, Jcontentree, and CJ E&M are our estimates; those for Netflix and Chinese peers are consensus based.

Source: Bloomberg, Yuanta Securities

Studio Dragon (253450 KS) pro forma financial statements (K-IFRS, consolidated)

Statement of comprehensive income					
FY ends Dec (Wbn)	2016A	2017E	2018E	2019E	2020E
Sales	154	287	381	481	575
Cost of sales	133	240	293	347	414
Gross profit	22	47	88	134	161
SG&A	5	14	15	18	22
Operating profit	17	33	73	116	139
EBITDA	39	33	73	116	139
Non-op profit/loss	-6	-2	4	5	6
Forex gain/loss	0	0	0	0	0
Net interest income	-1	2	4	5	6
Equity-meth gain/loss	0	0	0	0	0
Other	-5	-4	0	0	0
Net prof before income tax	10	30	77	121	145
Income tax	2	6	19	29	35
Net profit from continuing ops	8	14	58	92	110
Net profit from discontinued ops	0	0	0	0	0
Net profit	8	24	58	92	110
NP for controlling interest	8	24	58	92	110
Total comprehensive income	8	8	58	92	110
Total comprehensive income, CI	8	0	0	0	0

Note: Operating profit calculation same as K-GAAP (sales - COGS - SG&A exp)

Statement of financial position					
FY ends Dec (Wbn)	2016A	2017E	2018E	2019E	2020E
Current assets	81	320	379	475	587
Cash & cash equivalents	12	264	313	401	506
Accts rec & other	39	17	26	33	40
Inventory	0	2	3	4	5
Non-current assets	161	170	170	170	170
Tangible assets	1	1	1	1	1
Investment in affiliates	0	0	0	0	0
Other non-current	2	2	2	2	2
Total assets	242	490	550	645	758
Current liabilities	84	109	110	114	116
Accts payable & other	20	25	26	30	32
ST financial liabilities	8	7	7	7	7
Liquid LT liabilities	0	20	20	20	20
Non-current liabilities	21	11	11	11	11
LT financial liabilities	0	0	0	0	0
Debentures	20	10	10	10	10
Total liabilities	106	120	121	125	127
Equity, controlling interest	136	370	429	520	631
Paid-in capital	11	14	14	14	14
Capital surplus	115	322	322	322	322
Retained earnings	8	32	91	182	292
Equity, non-controlling interest	0	0	0	0	0
Total equity	136	370	429	520	631
Net debt	16	-228	-277	-365	-470
Total debt	28	36	36	36	36

Cash flow statement					
FY ends Dec (Wbn)	2016A	2017E	2018E	2019E	2020E
Operating cash flow	-12	26	49	88	105
Net profit	8	8	58	92	110
Depreciation & amortization	0	0	0	0	0
Forex gain/loss	0	0	0	0	0
Affiliate invest gain/loss	0	0	0	0	0
Inc (dec) in net working cap	-46	18	-9	-4	-5
Other	25	0	0	0	0
Investing cash flow	-70	0	0	0	0
Investment	0	0	0	0	0
Inc in tangible assets	-1	0	0	0	0
Dec in tangible assets	0	0	0	0	0
Other	-68	0	0	0	0
Financing cash flow	93	210	0	0	0
Inc (dec) in ST fin liab	7	0	0	0	0
Inc (dec) in LT fin liab	20	0	0	0	0
Inc (dec) in equity	56	210	0	0	0
Cash dividend	0	0	0	0	0
Other	10	0	0	0	0
Other cash flow	0	28	0	0	0
Inc (dec) in cash & equivalents	12	264	49	88	105
Beginning cash & equivalents	0	0	264	313	401
Ending cash & equivalents	12	264	313	401	506
NOPLAT	17	33	73	116	139
FCF	-12	44	46	84	100

Note: CI = controlling interest

EPS, BPS, P/E and P/B are based on controlling interest

For valuation metrics such as P/E, historical figures are based on annual average prices and estimates, on current price

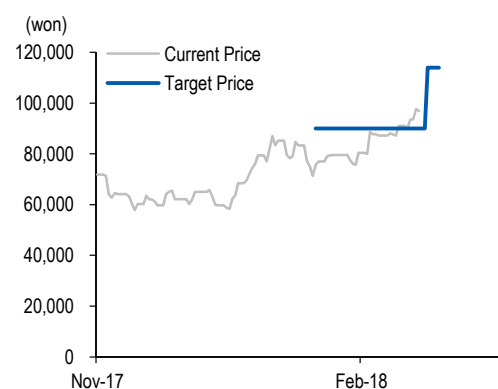
For ROA or ROE, assets and equity are averages of end-of-year figures for the given year and the year prior

Source: Yuenta Securities

Valuation					
FY ends Dec	2016A	2017E	2018E	2019E	2020E
EPS (won)	5,691	976	2,078	3,270	3,932
BPS (won)	61,763	13,212	15,289	18,559	22,491
EBITDA/shr (won)	27,127	1,349	2,604	4,137	4,965
SPS (won)	107,949	11,698	13,574	17,141	20,493
DPS (won)	0	0	0	0	0
P/E (x)	-	99.4	46.7	29.7	24.7
P/B (x)	-	7.3	6.3	5.2	4.3
EV/EBITDA (x)	-	75.3	33.5	20.3	16.2
P/S (x)	-	8.3	7.1	5.7	4.7

Key financial data					
FY ends Dec	2016A	2017E	2018E	2019E	2020E
Sales (% YoY)	0.0	85.7	32.7	26.3	19.6
Operating profit (%YoY)	na	98.9	120.7	58.9	20.0
Net profit, CI (%YoY)	na	193.9	143.4	57.4	20.3
Gross margin (%)	14.0	16.4	23.1	27.9	28.0
Operating margin (%)	10.8	11.5	19.2	24.1	24.2
Net margin, CI (%)	5.3	8.3	15.3	19.1	19.2
EBITDA margin (%)	25.1	11.5	19.2	24.1	24.2
ROIC (%)	21.8	23.6	51.8	77.6	89.6
ROA (%)	6.7	6.5	11.2	15.3	15.7
ROE (%)	12.0	9.4	14.6	19.3	19.2
Debt-to-equity (%)	77.8	32.4	28.3	24.0	20.2
Net debt-to-equity (%)	12.1	-61.5	-64.6	-70.1	-74.5
OP/financing cost (x)	19.5	0.0	0.0	0.0	0.0

Studio Dragon (253450 KS) ratings and target price history



Date	Rating	TP (won)	TP time frame	Difference (%)	
				vs avg price	vs high (low)
2018/03/19	BUY	114,000	1 yr		
2018/02/08	BUY	90,000	1 yr	-5.24	8.56
2017/11/24	BUY	60,000	1 yr	14.10	45.00

Note: Difference = (actual price* - target price) / target price x 100

* 1) The average price until the day target price was suggested

2) The highest (lowest) price until the day target price was suggested

Source: Yuanta Securities

Current distribution of Yuanta Securities Korea ratings

Rating	Share (%)
STRONG BUY	1.4
BUY	85.3
HOLD	13.3
SELL	0.0
Total	100.0

Note: As of Feb 15

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I/We, as the research analyst/analysts who prepared this research report, do hereby certify that the views expressed in this report accurately reflect my/our personal views about the subject securities discussed in this report.

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- **Stock ratings** include an Investment Rating (Strong Buy, Buy, Hold, Sell) based on the expected absolute return of a stock over the next 6 -12 months.
- - Strong Buy: Expected to return 30% or more
- - Buy: Expected to return between 10% and 30%
- - Hold: Expected to return between -10 and +10%
- - Sell: Expected to return -10% or less
- **Sector ratings** suggest 6 to 12 - month forward investment weighting of a given sector compared to its market capitalization weighting.
- - Overweight: Investment weighting is higher than the market capitalization weighting
- - Neutral: Investment weighting is equal to the market capitalization weighting
- - Underweight: Investment weighting is lower than the market capitalization weighting

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