

# Studio Dragon (253450 KS)

## Media/entertainment



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Rating	<b>BUY (M)</b>
Target price	<b>W114,000 (M)</b>
Current price (Aug 8)	<b>W96,000</b>
Upside potential	<b>19%</b>

Market cap (Wbn)	2,692
Shares outstanding	28,037,240
Avg daily T/O (2M, Wbn)	23
Avg daily volume (2M, shrs)	217,112
52-week high (won)	119,800
52-week low (won)	57,800
Foreign ownership (%)	2.8
Major shareholders (%)	
CJ E&M Corporation & others	75.7

### Stock performance

(%)	1M	3M	12M
Absolute	(11.6)	20.6	0.0
Relative	(8.8)	27.3	0.0
Abs (US\$)	(11.9)	15.9	0.0

## Long-term content blue chip investment

### 2Q18 review

- Studio Dragon reported consolidated 2Q18 sales of W74.3bn (+20% YoY), OP of W7.3bn (-21% YoY), and NP (controlling interest) of W8.9bn (-8% YoY), with OP missing consensus by about 20%. The YoY drop in OP is attributable to base effect from solid overseas sales of "Stranger" in 2Q17, and CoGS growth, which outpaced TV drama sales growth. In detail, programming revenue rose 41% YoY to W34.1bn and distribution revenue 9% YoY to W28.8bn, while other revenue fell 2% YoY to W11.4bn. 1) The sharp rise in programming revenue indicates a higher number of productions and higher average production cost. 2) Domestic distribution revenue rose 21% YoY to W12.3bn, decent even after we factor in the increase in the number of series produced YoY. The company's productions are gaining more influence, as shown by the improvement in its average viewership from 2.7% in 2Q17 to 4.2% in 2Q18 (+1.5%p). 3) **Overseas sales were stagnant at W16.5bn (+2% YoY) due to base effect from sales of "Stranger" to Netflix in 2Q17. In 2Q18, no Netflix sales were booked, and thus, overseas sales growth was slow and operating leverage lacking.** 4) Meanwhile, the firm booked financial gains of W3.4bn, up W3.1bn YoY, which we attribute mostly to a higher KRW/USD and resultant FX translation gains.

### Content blue chip for long-term investment

- We reiterate BUY and our target price of W114,000, implying a 2019E P/E of 34.5x. **The firm stands to benefit most from the resumption of TV drama sales to Chinese OTT firms and Amazon Prime's entry into the Korean market.** In addition, it has the biggest and best content creator pool in Korea. This enables it to produce original series for global OTT service providers and remake Korean hit series overseas (joint-productions with global media companies) as well as for its captive channels. This is why we believe Studio Dragon is a blue chip investors should have in their portfolios as a long-term play. We expect 2H18 OP to 295% YoY to W39.9bn for the following reasons. 1) 3Q18 OP will likely surge 220% YoY to W21.3bn thanks to "Mr. Sunshine," a 2018 blockbuster drama from prominent screen writer, Kim Eun-sook. Netflix is estimated to have paid at least W28.7bn (about W30.0bn in terms of estimated sales price), boosting operating leverage. 2) We estimate 4Q18 OP at W18.6bn (+436% YoY) even if we exclude sales to Chinese OTT players. In addition to "Memories of Alhambra" written by Song Jae-jeong, **"Boyfriend," starring Song Hye-kyo and Park Bo-gum, has been added to the 4Q18 line-up. It will air on tvN in Nov 2018, boosting expectations for 4Q18 earnings.** The production cost for the new series is said to be double the usual cost for a TV drama, and thanks to the popularity of actress Song Hye-kyo, Boyfriend will likely be priced highly in the overseas market.

### Quarterly earnings

(Wbn)	2Q18E	% YoY	% QoQ	Consens	vs consens (%)
Sales	74	19.6	-7.0	68	8.5
OP	7	-17.6	-31.3	9	-21.0
Pre-tax net profit	11	23.0	2.1	10	16.3
Net profit, CI	9	35.8	13.0	10	-8.0
OPM (%)	9.9	-4.4 %pt	-3.4 %pt	13.5	-3.6 %pt
NPM (%)	12.0	+1.5 %pt	+2.2 %pt	14.1	-2.1 %pt

Source: Yuanta Securities

### Forecasts and valuations (K-IFRS, consolidated)

	2016A	2017A	2018E	2019E
FY ends Dec				
Sales	154	287	367	457
OP	17	33	58	120
Net profit, CI	8	24	48	92
P/E (x)	-	60.3	56.7	29.1
P/B (x)	-	4.8	6.5	5.3
EV/EBITDA	-	21.4	23.4	15.6
ROE (%)	12.0	9.5	12.1	20.0

Source: Yuanta Securities

## Studio Dragon: earnings forecast

(Wbn)

	2017				2018				Full-year				
	1Q	2Q	3Q	4Q	1Q	2QP	3QE	4QE	2015	2016	2017	2018E	2019E
No of TV series produced	-	-	-	-	-	-	-	-	16	19	22	27	33
<b>Revenue</b>	75.3	62.1	77.5	71.9	79.9	74.3	120.7	91.8	97.4	195.5	286.8	366.6	457.2
- Programming	26.3	24.1	41.8	39.0	40.7	34.1	55.1	50.7	54.8	87.8	131.2	180.6	231.7
- Distribution	36.5	26.3	23.3	25.7	32.1	28.8	49.2	28.8	39.0	75.4	111.8	138.9	171.6
- Others	12.5	11.6	12.4	7.2	7.1	11.4	16.4	12.3	3.6	32.3	43.7	47.2	53.9
Growth (% YoY)	-	-	-	-	6	20	56	28	-6	101	47	28	25
- Programming	-	-	-	-	54	41	32	30	-6	60	49	38	28
- Distribution	-	-	-	-	-12	9	111	12	-3	93	48	24	24
- Others	-	-	-	-	-43	-2	32	72	-25	797	35	8	14
Domestic distribution revenue	13.9	10.2	10.2	10.3	9.4	12.3	-	-	15.1	31.2	44.6	-	-
Overseas distribution revenue	22.6	16.1	13.1	15.4	22.7	16.5	-	-	23.9	44.2	67.2	-	-
COGS	58.6	49.9	66.8	64.4	66.2	63.7	96.1	68.7	91.1	168.3	239.7	294.6	320.4
COGS-to-sales (%)	78	80	86	90	83	86	80	75	94	86	84	80	70
<b>Gross profit</b>	<b>16.8</b>	<b>12.2</b>	<b>10.6</b>	<b>7.4</b>	<b>13.7</b>	<b>10.6</b>	<b>24.6</b>	<b>23.1</b>	<b>6.3</b>	<b>27.2</b>	<b>47.0</b>	<b>72.0</b>	<b>136.8</b>
Gross margin (%)	22	20	14	10	17	14	20	25	6	14	16	20	30
SG&A expense	2.8	3.3	4.0	4.0	3.0	3.3	3.3	4.5	3.7	6.0	14.1	14.1	16.9
SG&A-to-sales (%)	4	5	5	6	4	4	3	5	4	3	5	4	4
<b>Operating profit</b>	<b>14.0</b>	<b>8.9</b>	<b>6.6</b>	<b>3.5</b>	<b>10.7</b>	<b>7.3</b>	<b>21.3</b>	<b>18.6</b>	<b>2.6</b>	<b>21.2</b>	<b>33.1</b>	<b>57.9</b>	<b>119.9</b>
Operating margin (%)	19	14	9	5	13	10	18	20	3	11	11	16	26
Pre-tax profit	13.2	9.0	6.4	1.7	10.8	11.0	21.6	19.0	-	-	30.3	62.4	121.9
Pre-tax margin (%)	18	14	8	2	14	15	24	22	-	-	11	17	27
<b>Net profit</b>	<b>13.4</b>	<b>2.8</b>	<b>5.7</b>	<b>2.0</b>	<b>7.9</b>	<b>8.9</b>	<b>16.4</b>	<b>14.4</b>	<b>-</b>	<b>-</b>	<b>23.8</b>	<b>47.5</b>	<b>92.4</b>
Net margin (%)	18	5	7	3	10	12	18	17	-	-	8	13	20
<b>Growth (% YoY)</b>													
Revenue	-	-	-	-	6	20	17	20	-6	101	47	28	25
Operating profit	-	-	-	-	-24	-18	220	436	-38	715	56	76	107
Net profit	-	-	-	-	-41	217	189	622	-	-	-	99	95

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

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

Statement of comprehensive income					
FY ends Dec (Wbn)	2016A	2017A	2018E	2019E	2020E
Sales	154	287	367	457	568
Cost of sales	133	240	295	320	412
Gross profit	22	47	72	137	156
SG&A	5	14	14	17	20
Operating profit	17	33	58	120	136
EBITDA	39	74	106	152	175
Non-op profit/loss	-6	-3	5	2	3
Forex gain/loss	0	-1	0	0	0
Net interest income	-1	-1	2	2	3
Equity-meth gain/loss	0	0	0	0	0
Other	-5	0	3	0	0
Net prof before income tax	10	30	62	122	138
Income tax	2	6	15	30	33
Net profit from continuing ops	8	24	48	92	105
Net profit from discontinued ops	0	0	0	0	0
Net profit	8	24	48	92	105
NP for controlling interest	8	24	48	92	105
Total comprehensive income	8	24	48	92	105
Total comprehensive income, CI	8	24	25	48	54

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

Statement of financial position					
FY ends Dec (Wbn)	2016A	2017A	2018E	2019E	2020E
Current assets	81	290	322	415	522
Cash & cash equivalents	12	51	67	150	241
Accts rec & other	39	55	56	65	81
Inventory	0	1	2	2	2
Non-current assets	161	170	174	174	174
Tangible assets	1	1	1	1	1
Investment in affiliates	0	0	0	0	0
Other non-current	2	4	4	4	4
Total assets	242	459	496	589	696
Current liabilities	84	91	79	80	82
Accts payable & other	20	34	28	28	30
ST financial liabilities	8	0	0	0	0
Liquid LT liabilities	0	10	0	0	0
Non-current liabilities	21	0	0	0	0
LT financial liabilities	0	0	0	0	0
Debentures	20	0	0	0	0
Total liabilities	106	91	80	80	83
Equity, controlling interest	136	368	416	509	613
Paid-in capital	11	14	14	14	14
Capital surplus	115	320	320	320	320
Retained earnings	8	32	80	172	277
Equity, non-controlling interest	0	0	0	0	0
Total equity	136	368	416	509	613
Net debt	16	-182	-224	-307	-398
Total debt	28	10	0	0	0

Cash flow statement					
FY ends Dec (Wbn)	2016A	2017A	2018E	2019E	2020E
Operating cash flow	-12	-7	65	96	111
Net profit	8	24	48	92	105
Depreciation & amortization	0	0	0	0	0
Forex gain/loss	0	1	0	0	0
Affiliate invest gain/loss	0	0	0	0	0
Inc (dec) in net working cap	-46	-73	-32	-30	-35
Other	25	41	49	34	41
Investing cash flow	-70	-141	-52	-34	-41
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	-141	-52	-33	-40
Financing cash flow	93	188	-10	0	0
Inc (dec) in ST fin liab	7	-8	0	0	0
Inc (dec) in LT fin liab	20	-10	0	0	0
Inc (dec) in equity	56	208	0	0	0
Cash dividend	0	0	0	0	0
Other	10	-2	-10	0	0
Other cash flow	0	0	12	21	21
Inc (dec) in cash & equivalents	12	40	15	83	91
Beginning cash & equivalents	0	12	0	67	150
Ending cash & equivalents	12	51	67	150	241
NOPLAT	17	33	58	120	136
FCF	-12	-6	60	93	107

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

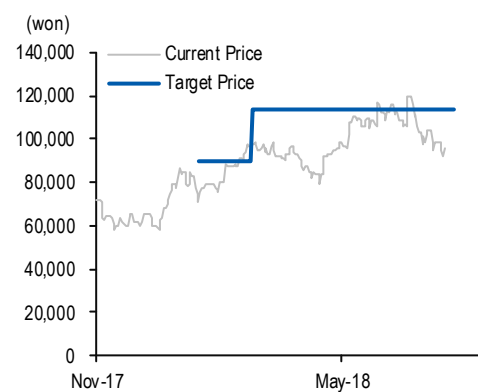
For ROA or ROE, assets and equity are averages of end-of-year figures for the given year and the year prior

Source: Yunta Securities

Valuation					
FY ends Dec	2016A	2017A	2018E	2019E	2020E
EPS (won)	569	1,050	1,694	3,296	3,740
BPS (won)	6,176	13,141	14,842	18,138	21,878
EBITDA/shr (won)	27,127	3,271	3,764	5,439	6,248
SPS (won)	10,795	12,628	13,077	16,307	20,264
DPS (won)	0	0	0	0	0
P/E (x)	-	60.3	56.7	29.1	25.7
P/B (x)	-	4.8	6.5	5.3	4.4
EV/EBITDA (x)	-	21.4	23.4	15.6	13.1
P/S (x)	-	5.0	7.3	5.9	4.7

Key financial data					
FY ends Dec	2016A	2017A	2018E	2019E	2020E
Sales (% YoY)	0.0	85.7	27.8	24.7	24.3
Operating profit (%YoY)	na	98.3	75.5	107.2	13.2
Net profit, CI (%YoY)	na	192.9	99.2	94.5	13.5
Gross margin (%)	14.0	16.4	19.6	29.9	27.5
Operating margin (%)	10.8	11.5	15.8	26.2	23.9
Net margin, CI (%)	5.3	8.3	13.0	20.2	18.5
EBITDA margin (%)	25.1	25.9	28.8	33.4	30.8
ROIC (%)	21.8	19.7	30.0	59.6	62.8
ROA (%)	6.7	6.8	9.9	17.0	16.3
ROE (%)	12.0	9.5	12.1	20.0	18.7
Debt-to-equity (%)	77.8	24.7	19.2	15.8	13.5
Net debt-to-equity (%)	12.1	-49.4	-53.7	-60.3	-64.9
OP/financing cost (x)	19.5	19.0	1,363.7	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)
2018/08/09	BUY	114,000	1 yr		
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	1.7
BUY	85.5
HOLD	12.8
SELL	0.0
Total	100.0

Note: As of Aug 7

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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.

### Stock and sector ratings

- **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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