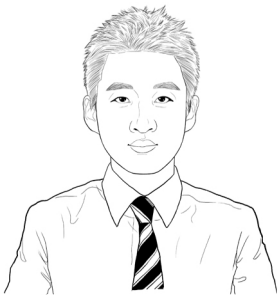


2018. 10. 3

# Company Update



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## AT A GLANCE

SELL HOLD **BUY**

**Target price** KRW140,000 (20.4%)

<b>Current price</b>	KRW116,300
Market cap	KRW3.3t/USD3.0b
Shares (float)	28,037,240 (23.9%)
52-week high/low	KRW119,800/KRW57,800
Avg daily trading value (60-day)	KRW21.5b/ USD19.3m

## ONE-YEAR PERFORMANCE

	1M	6M	12M
Studio Dragon (%)	5.2	25.6	0.0
Vs Kosdaq (%pts)	5.3	34.0	0.0

## KEY CHANGES

(KRW)	New	Old	Diff
Recommend.	BUY	BUY	
Target price	140,000	140,000	0.0%
2018E EPS	1,412	1,491	-5.3%
2019E EPS	2,364	2,398	-1.4%

## SAMSUNG vs THE STREET

No of estimates	13
Target price	134,308
Recommendation	3.9

BUY★★: 5 / BUY: 4 / HOLD: 3 / SELL: 2 / SELL★★: 1

## Studio Dragon (253450)

### Content quality still in focus

- The five Studio Dragon dramas that aired in 3Q put in solid performances, all boasting peak viewership ratings of over 5%.
- We expect the firm to post a 3Q operating profit of KRW19.3b, backed by overseas the copyright sale of *Mr. Sunshine* and brisk VOD sales in the domestic market.
- Studio Dragon should deliver strong earnings again in 4Q, when it plans to release two tent-pole dramas. The firm recently signed a production contract for a Netflix Original Series drama, and the copyright sale of this and other series to Chinese OTT operators would likely give Studio Dragon shares an additional boost.

### WHAT'S THE STORY?

**To post 3Q solid results...** Studio Dragon's 3Q results are likely to reveal another solid quarter, backed by peak viewership ratings in excess of 5% for each of its five dramas that aired in the quarter. *Mr. Sunshine*'s peak viewership rating hit 18.1%, not far off the 20.5% registered by last year's blockbuster *Goblin*. As for VOD sales, *What's Wrong with Secretary Kim?* ranked high thanks to popularity among young viewers.

**...and 4Q results:** Earnings at Studio Dragon hinge on the sale of copyrights overseas and VOD services in the local market. In 3Q, the firm recognized copyright sales of *Mr. Sunshine* from Netflix and enjoyed brisk VOD sales based on the success of its major dramas. We expect 3Q operating profit to hit a record high of KRW19.3b. The firm should also deliver solid 4Q operating results, driven by the tent pole dramas *Boysfriend* and *Memories of the Alhambra*.

**Netflix Original Series and copyright sale in China:** Studio Dragon recently signed a contract to produce an 8-episode webtoon-based drama entitled *Love Alarm* as a Netflix Original Series. On additional positive is that the Korean firm can sell the copyright in China, where the US firm lacks a presence. Studio Dragon is also in talks with the US firm to produce at least one more Netflix Original Series drama. Signing contracts with Chinese OTT operators would add to Studio Dragon's earnings momentum, a good barometer for which might be *Memories of the Alhambra* (currently in pre-production).

**Focus on growth potential over current profitability:** All year long, Studio Dragon has been investing heavily in dramas and reinforcing the competitiveness of its content. While its top-line growth—led by the massive popularity of its dramas—is drawing investors' attention, profitability has stagnated due to growing production costs. Still, we advise investors to focus on content quality (not on immediate earnings) since growth opportunities from foreign OTT platform operators (eg, Netflix) abound. We would suggest keeping an eye on whether Studio Dragon's productions grow in size and whether its content quality improves.

### SUMMARY FINANCIAL DATA

	2017	2018E	2019E	2020E
Revenue (KRWb)	287	399	556	730
Net profit (adj) (KRWb)	24	40	66	86
EPS (adj) (KRW)	1,050	1,412	2,364	3,062
EPS (adj) growth (% y-y)	84.5	34.4	67.5	29.5
EBITDA margin (%)	25.9	28.9	32.3	32.6
ROE (%)	9.5	10.2	15.0	16.6
P/E (adj) (x)	110.8	82.4	49.2	38.0
P/B (x)	8.9	8.0	6.9	5.8
EV/EBITDA (x)	41.4	26.4	16.5	12.0
Dividend yield (%)	0.0	0.0	0.0	0.0






Source: Company data, Samsung Securities estimates

Table 1. 2H drama lineup

Quarter	Title	Ratings (%)	Air dates	Channel
2	What's Wrong with Secretary Kim?	7.4	Jun 6-Jul 26	tvN
	Life on Mars	4.0	Jun 9-Aug 5	OCN
3	Mr. Sunshine	13.0	Jul 7-Sep 30	tvN
	Familiar Wife	6.8	Aug 1-Sep 20	tvN
	Voice 2	4.9	Aug 11-Sep 16	OCN
	Hundred Days' Husband	6.0	Sep 10-Oct 30	tvN
	The Guest	2.7	Sep 12-Nov 1	OCN
	Player	4.7	Sep 29-Nov 11	OCN
4	One Million Stars Falling from the Sky	-	Oct 3 -	tvN
	Room No.9	-	Oct 6 -	tvN
	Mama Fairy and the Woodcutter	-	Nov 5 -	tvN
	Boyfriend	-	Nov	tvN
	Memories of the Alhambra	-	Nov	tvN

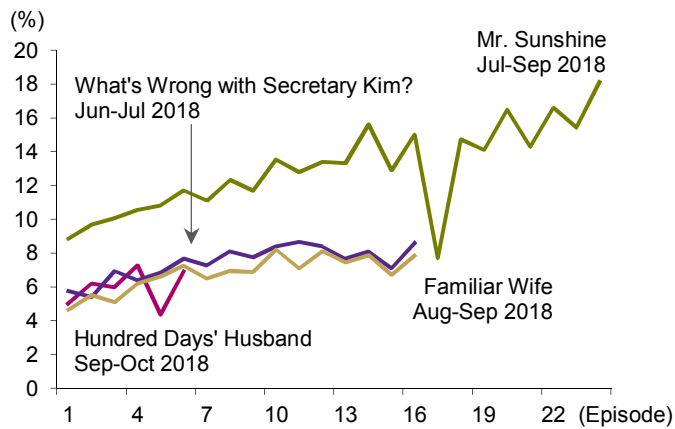
Source: Company data, AGB Nielson, Samsung Securities

Table 2. 3Q drama lineup

Title	What's Wrong with Secretary Kim?	Life on Mars	Mr. Sunshine	Familiar Wife	Voice 2
					
Premier	Jun 2018	Jun 2018	Jul 2018	Aug 2018	Aug 2018
Writer	Seon-woo Baek, Bo-rim Choi	Dae-il Lee	Eun-sook Kim	Hee-seung Yang	Jin-won Ma
Production	Bon Factory	Production H	Hwa & Dam Pictures	Chorokbaem	Contents K
Cast	Seo-jun Park, Min-young Park	Kyung-ho Jeong, Sung-woong Park, Ah-sung Koh	Byung-heon Lee, Tae-ri Kim	Ji-sung, Ji-min Han	Ha-na Lee, Jin-wook Lee, Yul Kwon
Rating	Average 7.5%; High 8.7%	Average 4%; High 5.9%	Average 13.0%; High 18.1%	Average 6.8%; High 8.2%	Average 4.9%; High 7.1%

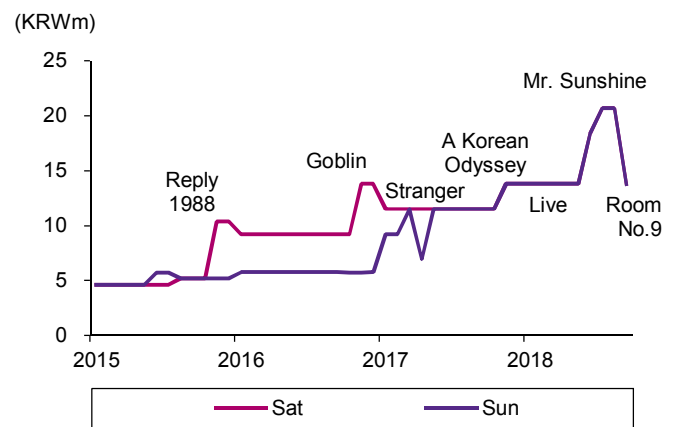
Source: Company data, AGB Nielson, Samsung Securities

Chart 1. 3Q drama ratings



Source: Company data, AGB Nielson

Chart 2. tvN: Prime-time unit ad price



Source: Company data

Table 3. Cable TV drama VOD rankings

Rank	Sep (week 2)	Sep (week 1)	Aug (week 4)	Aug (week 3)	Aug (week 2)
1	tvN Mr. Sunshine	tvN Mr. Sunshine	tvN Mr. Sunshine	tvN Mr. Sunshine	tvN Mr. Sunshine
2	KBS2 Marry Me Now	KBS2 Marry Me Now	JTBC Gangnam Beauty	JTBC Gangnam Beauty	JTBC Gangnam Beauty
3	OCN Voice 2	JTBC Gangnam Beauty	OCN Voice 22	KBS2 Marry Me Now	KBS2 Marry Me Now
4	JTBC Gangnam Beauty	OCN Voice 2	KBS2 Marry Me Now	OCN Voice 2	tvN Familiar Wife
5	tvN Familiar Wife	tvN Familiar Wife	SBS All-in	tvN Familiar Wife	OCN Life on Mars
6	OCN The Guest	JTBC Life	tvN Familiar Wife	JTBC Life	JTBC Life
7	JTBC Life	SBS Your Honor	KBS2 Wave, Wave	KBS2 Wave, Wave	tvN What's Wrong with Secretary Kim?

Source: Home Choice

Table 4. Target price calculation

(KRWb)							Note
	Current	Target					
Share price (KRW)	115,500	140,000					
Market cap	3,238	3,925					
	Actual				Assumption		
	2016	2017	2018E	2019E	Current	Target	
Net profit	13	24	42	67	162	196	Market cap/A
Sales	196	287	399	556	1,079	1,308	Net profit/B
Per-drama sales	10.3	12.9	15.4	19.2	27	33	Sales/C
Per-drama production costs	7.8	9.5	11.2	13.4	19	23	Per-drama sales*D
Per-episode production costs	0.48	0.59	0.70	0.84	1.2	1.4	Per-drama production costs/E
<b>Major indicators</b>							
Target P/E (x)	255.1	135.8	77.5	48.6	20	20	A
Net margin (%)	6.5	8.3	10.5	12.0	15.0	15.0	B
Number of dramas	19	22	26	29	40	40	C
Production cost-to-sale ratio (%)	75.4	73.1	72.8	70.1	70.0	70.0	D
Number of episodes per drama	16	16	16	16	16	16	E

Source: Samsung Securities estimates

Table 5. Results and forecasts

(KRWb)	2017	2018E	2019E	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18E	4Q18E	1Q19E	2Q19E	3Q19E	4Q19E
<b>Sales</b>	<b>287</b>	<b>399</b>	<b>556</b>	<b>75</b>	<b>62</b>	<b>77</b>	<b>72</b>	<b>80</b>	<b>74</b>	<b>127</b>	<b>118</b>	<b>132</b>	<b>143</b>	<b>131</b>	<b>149</b>
Broadcasting	131	179	224	26	24	42	39	41	34	51	53	55	56	51	61
Copyright sales	112	178	280	36	26	23	26	32	29	64	53	64	74	67	74
Other	44	42	52	13	12	12	7	7	11	12	12	12	13	13	14
<b>Cost of goods sold</b>	<b>240</b>	<b>330</b>	<b>448</b>	<b>59</b>	<b>50</b>	<b>67</b>	<b>64</b>	<b>66</b>	<b>64</b>	<b>102</b>	<b>99</b>	<b>104</b>	<b>115</b>	<b>104</b>	<b>124</b>
Production	210	291	390	49	42	60	58	59	56	89	87	90	100	90	109
Commission	17	27	42	5	4	3	4	5	4	10	8	10	11	10	11
Other	13	13	16	4	3	4	2	2	3	4	4	4	4	4	4
<b>Gross profit</b>	<b>47</b>	<b>69</b>	<b>108</b>	<b>17</b>	<b>12</b>	<b>11</b>	<b>7</b>	<b>14</b>	<b>11</b>	<b>25</b>	<b>20</b>	<b>28</b>	<b>28</b>	<b>27</b>	<b>25</b>
SG&A	14	17	20	3	3	4	4	3	3	6	5	4	4	7	6
<b>Operating profit</b>	<b>33</b>	<b>52</b>	<b>88</b>	<b>14</b>	<b>9</b>	<b>7</b>	<b>3</b>	<b>11</b>	<b>7</b>	<b>19</b>	<b>15</b>	<b>24</b>	<b>24</b>	<b>20</b>	<b>20</b>
Pre-tax profit	30	56	89	13	9	6	2	10	11	20	15	25	24	20	20
Net profit	24	42	67	13	3	6	2	7	9	15	11	18	18	15	15
Adjusted EPS (KRW)	851	1,490	2,379												
<b>Margins (%)</b>															
Operating margin	11.5	13.1	15.9	18.5	14.3	8.6	4.8	13.4	9.9	15.2	12.7	18.5	16.8	15.2	13.2
Pre-tax margin	10.6	13.9	16.0	17.6	14.5	8.2	2.3	12.3	14.9	15.4	12.8	18.6	16.9	15.4	13.3
Net margin	8.3	10.5	12.0	17.8	4.5	7.3	2.8	8.6	12.0	11.5	9.6	14.0	12.7	11.5	10.0

Source: Company data, Samsung Securities estimates

## Income statement

Year-end Dec 31 (KRWb)	2016	2017	2018E	2019E	2020E
<b>Sales</b>	<b>154</b>	<b>287</b>	<b>399</b>	<b>556</b>	<b>730</b>
Cost of goods sold	133	240	330	448	597
<b>Gross profit</b>	<b>22</b>	<b>47</b>	<b>69</b>	<b>108</b>	<b>133</b>
Gross margin (%)	14.0	16.4	17.3	19.5	18.2
SG&A expenses	5	14	17	20	25
<b>Operating profit</b>	<b>17</b>	<b>33</b>	<b>52</b>	<b>88</b>	<b>109</b>
Operating margin (%)	10.8	11.5	13.1	15.9	14.9
<b>Non-operating gains (losses)</b>	<b>(6)</b>	<b>(3)</b>	<b>0</b>	<b>0</b>	<b>7</b>
Financial profit	1	1	4	5	7
Financial costs	2	3	0	(1)	(1)
Equity-method gains (losses)	0	0	0	0	0
Other	(5)	(0)	(4)	(5)	(0)
<b>Pre-tax profit</b>	<b>10</b>	<b>30</b>	<b>53</b>	<b>88</b>	<b>116</b>
Taxes	2	6	13	22	30
Effective tax rate (%)	22.4	21.2	24.8	25.0	25.9
Profit from continuing operations	8	24	40	66	86
Profit from discontinued operations	0	0	0	0	0
<b>Net profit</b>	<b>8</b>	<b>24</b>	<b>40</b>	<b>66</b>	<b>86</b>
Net margin (%)	5.3	8.3	9.9	11.9	11.8
Net profit (controlling interests)	8	24	40	66	86
Net profit (non-controlling interests)	0	0	0	0	0
EBITDA	39	74	115	180	238
EBITDA margin (%)	25.1	25.9	28.9	32.3	32.6
EPS (parent-based) (KRW)	569	1,050	1,412	2,364	3,062
EPS (consolidated) (KRW)	569	1,050	1,412	2,364	3,062
Adjusted EPS (KRW)*	569	1,050	1,412	2,364	3,062

## Cash flow statement

Year-end Dec 31 (KRWb)	2016	2017	2018E	2019E	2020E
<b>Cash flow from operations</b>	<b>(12)</b>	<b>(7)</b>	<b>126</b>	<b>192</b>	<b>252</b>
Net profit	8	24	40	66	86
Non-cash profit and expenses	27	46	73	109	152
Depreciation	0	0	0	0	0
Amortization	22	41	63	92	130
Other	5	5	9	17	23
Changes in A/L from operating activities	(46)	(73)	27	39	44
<b>Cash flow from investments</b>	<b>(70)</b>	<b>(141)</b>	<b>(101)</b>	<b>(122)</b>	<b>(160)</b>
Change in tangible assets	(1)	(0)	0	0	0
Change in financial assets	(2)	(142)	(9)	(9)	(10)
Other	(66)	1	(92)	(112)	(150)
<b>Cash flow from financing</b>	<b>93</b>	<b>188</b>	<b>(17)</b>	<b>1</b>	<b>1</b>
Change in debt	28	(18)	(16)	0	0
Change in equity	126	208	0	0	0
Dividends	0	0	0	0	0
Other	(60)	(2)	(0)	1	1
Change in cash	12	40	8	71	93
Cash at beginning of year	0	12	51	60	131
Cash at end of year	12	51	60	131	223
<b>Gross cash flow</b>	<b>35</b>	<b>70</b>	<b>112</b>	<b>175</b>	<b>238</b>
<b>Free cash flow</b>	<b>(14)</b>	<b>(7)</b>	<b>39</b>	<b>75</b>	<b>95</b>

Note: \* Excluding one off items, \*\* Fully diluted, excluding one-off items

\*\*\* From companies subject to equity-method valuation

Source: Company data, Samsung Securities estimates

## Balance sheet

Year-end Dec 31 (KRWb)	2016	2017	2018E	2019E	2020E
<b>Current assets</b>	<b>81</b>	<b>290</b>	<b>310</b>	<b>394</b>	<b>499</b>
Cash & equivalents	12	51	60	131	223
Accounts receivable	37	55	58	61	64
Inventories	0	1	1	1	1
Other current assets	33	182	191	201	211
<b>Fixed assets</b>	<b>161</b>	<b>170</b>	<b>204</b>	<b>231</b>	<b>260</b>
Investment assets	2	4	5	7	10
Tangible assets	1	1	1	1	1
Intangible assets	124	128	152	177	204
Other long-term assets	33	37	46	46	46
<b>Total assets</b>	<b>242</b>	<b>459</b>	<b>514</b>	<b>625</b>	<b>760</b>
<b>Current liabilities</b>	<b>84</b>	<b>91</b>	<b>106</b>	<b>150</b>	<b>199</b>
Accounts payable	6	6	8	12	15
Short-term debt	8	0	(7)	(7)	(7)
Other current liabilities	71	85	104	145	190
<b>Long-term liabilities</b>	<b>21</b>	<b>0</b>	<b>0</b>	<b>1</b>	<b>1</b>
Bonds & long-term debt	20	0	0	0	0
Other long-term liabilities	2	0	0	1	1
<b>Total liabilities</b>	<b>106</b>	<b>91</b>	<b>106</b>	<b>151</b>	<b>200</b>
<b>Owners of parent equity</b>	<b>136</b>	<b>368</b>	<b>408</b>	<b>474</b>	<b>560</b>
Capital stock	11	14	14	14	14
Capital surplus	115	320	320	320	320
Retained earnings	8	32	72	138	224
Other	2	3	3	3	3
<b>Non-controlling interests' equity</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Total equity</b>	<b>136</b>	<b>368</b>	<b>408</b>	<b>474</b>	<b>560</b>
Net debt	16	(182)	(214)	(292)	(393)

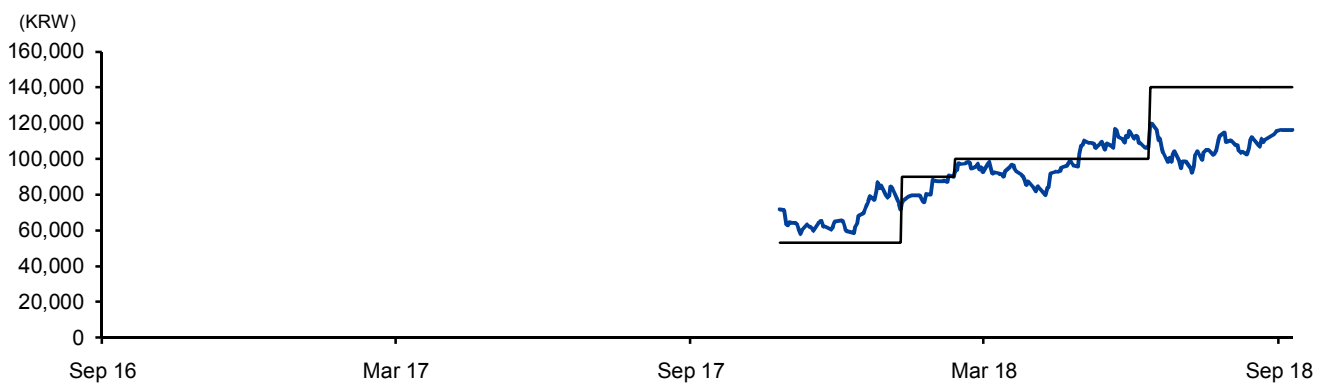
## Financial ratios

Year-end Dec 31	2016	2017	2018E	2019E	2020E
<b>Growth (%)</b>					
Sales	nm	85.7	39.3	39.2	31.2
Operating profit	nm	98.3	58.6	68.5	23.2
Net profit	nm	192.9	66.0	67.5	29.5
Adjusted EPS**	nm	84.5	34.4	67.5	29.5
<b>Per-share data (KRW)</b>					
EPS (parent-based)	569	1,050	1,412	2,364	3,062
EPS (consolidated)	569	1,050	1,412	2,364	3,062
Adjusted EPS**	569	1,050	1,412	2,364	3,062
BVPS	6,176	13,141	14,553	16,917	19,978
DPS (common)	0	0	0	0	0
<b>Valuations (x)</b>					
P/E***	204.3	110.8	82.4	49.2	38.0
P/B***	18.8	8.9	8.0	6.9	5.8
EV/EBITDA	84.4	41.4	26.4	16.5	12.0
<b>Ratios (%)</b>					
ROE	6.0	9.5	10.2	15.0	16.6
ROA	3.4	6.8	8.1	11.6	12.4
ROIC	8.5	15.6	21.3	36.6	48.6
Payout ratio	0.0	0.0	0.0	0.0	0.0
Dividend yield (common)	0.0	0.0	0.0	0.0	0.0
Net debt to equity	12.1	(49.4)	(52.5)	(61.7)	(70.1)
Interest coverage (x)	19.5	19.0	328.2	(148.5)	(183.0)

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## Target price changes in past two years



## Rating changes over past two years (adjusted share prices)

Date	2017/11/23	2018/2/8	3/13	7/12
Recommendation	BUY	BUY	BUY	BUY
Target price (KRW)	53,000	90,000	100,000	140,000
Gap* (average)	29.29	(7.62)	(1.06)	
(max or min)**	64.15	1.11	17.10	

Note: \* [(average, maximum, or minimum share price over duration of target price minus target price) / target price] x 100%

\*\* Maximum/minimum share price if new target is higher/lower than market close on the business day prior to target price change

Samsung Securities uses the following investment ratings.

### Company

<b>BUY</b>	Expected to increase in value by 10% or more within 12 months and is highly attractive within sector
<b>HOLD</b>	Expected to increase/decrease in value by less than 10% within 12 months
<b>SELL</b>	Expected to decrease in value by 10% or more within 12 months

### Industry

<b>OVERWEIGHT</b>	Expected to outperform market by 5% or more within 12 months
<b>NEUTRAL</b>	Expected to outperform/underperform market by less than 5% within 12 months
<b>UNDERWEIGHT</b>	Expected to underperform market by 5% or more within 12 months

## Percentage of ratings in 12 months prior to Jun 30, 2018

BUY (85.1%) | HOLD (14.9%) | SELL (0%)

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