

Studio Dragon (253450 KS)

Media/entertainment



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Rating	BUY (M)
Target price	W136,000 (U)
Current price (Oct 2)	W110,100
Upside potential	24%

Market cap (Wbn)	3,087
Shares outstanding	28,037,240
Avg daily T/O (2M, Wbn)	22
Avg daily volume (2M, shrs)	204,801
52-week high (won)	119,800
52-week low (won)	57,800
Foreign ownership (%)	2.1
Major shareholders (%)	
	CJ ENM & others 75.7

Stock performance

(%)	1M	3M	12M
Absolute	(0.4)	(1.2)	0.0
Relative	2.4	(1.8)	0.0
Abs (US\$)	(0.9)	(1.1)	0.0

Roll over base year to 2020

Increased visibility on goal of producing 40 dramas in 2020

- CJ ENM added a new drama slot for OCN on Wednesdays and Thursdays in Sep 2018, increasing the number of its drama slots to 6 (3 on tvN and 3 on OCN). The first drama series airing on OCN's Wednesday~Thursday slot is "The Guest" and the next will be "Priest," both of which are produced by Studio Dragon. Currently, it is supplying drama series for 5 out of CN ENM's 6 drama slots (excluding only OCN's Monday~Tuesday slot).
- When it conducted its IPO in Nov 2017, Studio Dragon put forward a goal of producing 40 drama series in 2020. **Assuming Studio Dragon supplies drama series for all of CJ ENM's 6 slots, it could theoretically supply 39 drama series to captive channels per year (6.5 drama series with 16 episodes per slot x 6 slots).** CJ ENM also programmed a drama series "Eunju's Room," produced by Studio Dragon, for Olive, one of its channels, in Nov 2018. Although it is not certain whether Olive will continue to air the series, there is a high likelihood that the number of CJ ENM's drama slots will increase in the long term.
- The number of writers belonging to Studio Dragon increased from 64 in Nov 2017 to 71 as of end-Jun 2018. As CJ Group has fostered broadcasting/screen writers via its O'PEN program, its writing pool should continue expanding. **Given increased visibility on its goal of producing 40 drama series in 2020 and interest in Korean content from Chinese private over-the-top (OTT) content providers, we believe the valuation base year should be rolled over to 2020.**

Revise up target price

- We maintain BUY, but revise up our target price from W114,000 to W136,000, which implies a target P/E of 25x and 2020E EPS of W5,448.**
- We expect 2020 OP to reach W195.6bn (consensus W123.2bn), assuming: 1) the company produces 42 drama series in 2020 (including two Netflix original dramas); and 2) the resumption of drama exports to China boosts the average gross margin of dramas.** Currently, the firm's average gross margin for dramas stands at 15~20%. We estimate gross margin of "Mr. Sunshine," a blockbuster drama, at 26%, and this will rise above 40% including revenue from its transmission rights to a Chinese OTT. If the Chinese government lifts its ban on Korean cultural content in 2019, Studio Dragon's 2020 earnings estimates will have to be revised. FYI, Huace Film and TV, a Chinese drama production firm, enjoys a gross margin of 20~30%. When Studio Dragon is able to sell dramas to global and Chinese OTT plays, its gross margin will likely exceed Huace Film and TV's.

Quarterly earnings

(Wbn)	3Q18E	% YoY	% QoQ	Consens	vs consens (%)
Sales	121		62.4	121	-0.5
OP	21		190.8	24	-11.2
Pre-tax net profit	22		100.6	25	-11.2
Net profit, CI	17		89.0	21	-20.6
OPM (%)	17.6		+7.7 %pt	19.8	-2.2 %pt
NPM (%)	13.9		+1.9 %pt	17.5	-3.6 %pt

Source: Yuanta Securities

Forecasts and valuations (K-IFRS, consolidated)

	FY ends Dec	2016A	2017A	2018E	2019E
Sales		154	287	367	453
OP		17	33	58	105
Net profit, CI		8	24	48	83
P/E (x)		-	60.3	63.7	37.0
P/B (x)		-	4.8	7.4	6.2
EV/EBITDA		-	21.4	27.5	20.4
ROE (%)		12.0	9.5	12.3	18.2

Source: Yuanta Securities

Studio Dragon: earnings forecast

(Wbn)

	2017				2018				Full-year				
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE	2016	2017	2018E	2019E	2020E
No of TV series produced	-	-	-	-	-	-	-	-	19	22	27	33	40
Revenue	75.3	62.1	77.5	71.9	79.9	74.3	120.7	91.8	195.5	286.8	366.6	452.9	580.0
- Programming	26.3	24.1	41.8	39.0	40.7	34.1	55.1	50.7	87.8	131.2	180.6	231.7	280.9
- Distribution	36.5	26.3	23.3	25.7	32.1	28.8	49.2	28.8	75.4	111.8	138.9	171.6	247.1
- Others	12.5	11.6	12.4	7.2	7.1	11.4	16.4	12.3	32.3	43.7	47.2	49.5	52.0
Growth (% YoY)	-	-	-	-	6	20	56	28	101	47	28	24	28
- Programming	-	-	-	-	54	41	32	30	60	49	38	28	21
- Distribution	-	-	-	-	-12	9	111	12	93	48	24	24	44
- Others	-	-	-	-	-43	-2	32	72	797	35	8	5	5
Domestic distribution revenue	13.9	10.2	10.2	10.3	9.4	12.3	-	-	31.2	44.6	-	-	-
Overseas distribution revenue	22.6	16.1	13.1	15.4	22.7	16.5	-	-	44.2	67.2	-	-	-
COGS	58.6	49.9	66.8	64.4	66.2	63.7	96.1	68.7	168.3	239.7	294.6	330.9	362.4
COGS-to-sales (%)	78	80	86	90	83	86	80	75	86	84	80	73	62
Gross profit	16.8	12.2	10.6	7.4	13.7	10.6	24.6	23.1	27.2	47.0	72.0	122.0	217.6
Gross margin (%)	22	20	14	10	17	14	20	25	14	16	20	27	38
SG&A expense	2.8	3.3	4.0	4.0	3.0	3.3	3.3	4.5	6.0	14.1	14.1	16.9	22.0
SG&A-to-sales (%)	4	5	5	6	4	4	3	5	3	5	4	4	4
Operating profit	14.0	8.9	6.6	3.5	10.7	7.3	21.3	18.6	21.2	33.1	57.9	105.1	195.6
Operating margin (%)	19	14	9	5	13	10	18	20	11	11	16	23	34
Pre-tax profit	13.2	9.0	6.4	1.7	10.8	11.0	22.2	19.6	-	30.3	63.7	110.1	201.5
Pre-tax margin (%)	18	14	8	2	14	15	18	21	-	11	17	24	35
Net profit	13.4	2.8	5.7	2.0	7.9	8.9	16.8	14.9	-	23.8	48.4	83.4	152.8
Net margin (%)	18	5	7	3	10	12	14	16	-	8	13	18	26
Growth (% YoY)													
Revenue	-	-	-	-	6	20	17	20	101	47	28	24	28
Operating profit	-	-	-	-	-24	-18	220	436	715	56	76	81	86
Net profit	-	-	-	-	-41	217	197	645	-	-	103	72	83

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

Mr. Sunshine: revenue forecast

	Value	Major assumption
Revenue	W58.3bn	(a)
- tvN transmission rights	W21.5bn	Per-episode production cost W1.8bn x 50%
- Product placement	W6.5bn	Per-episode production cost W1.8bn x 15%
- Domestic VOD	W4.8bn	W0.2bn per episode
- Netflix transmission rights	W30.0bn	
COGS	W47.5bn	(b)
- Production cost	W43.0bn	
- Overseas sales commission	W4.5bn	Revenue from Netflix transmission rights W30.0bn – commissions paid to CJ ENM W4.5bn (15%)
Gross profit	W15.3bn	(c) = (a) – (b)
GPM (%)	26	(c) / (a)
[Assuming the drama series will be sold to a Chinese OTT]		
- Transmission rights revenue	W20.0bn	Revenue estimate if sold as new drama while being aired on tvN ... (d)
- Overseas sales commission	W3.0bn	Commissions paid to CJ ENM (15%) ... (e)
Gross profit (revised)	W32.3bn	(f) = (c) + (d) – (e)
GPM (%)	41	(f) / { (a) + (d) }

Source: Yuanta Securities

2020E revenue scenario

(42 dramas in total = 37 non-blockbuster + 3 blockbusters + 2 Netflix originals)

[Gross profit estimate for 37 non-blockbuster dramas with 16 episodes]

(Wbn)		Per-episode production cost for non-blockbuster drama				
		0.5	0.55	0.6	0.65	0.7
Average GPM for non-blockbuster	15%	44.4	48.8	53.3	57.7	62.2
	20%	59.2	65.1	71.0	77.0	82.9
	25%	74.0	81.4	88.8	96.2	103.6
	30%	88.8	97.7	106.6	115.4	124.3
	35%	103.6	114.0	124.3	134.7	145.0
	40%	118.4	130.2	142.1	153.9	165.8

[Gross profit estimate for 3 blockbuster dramas]

(Wbn)		Gross profit per blockbuster drama (excl sales to China)				
		10.0	15.0	20.0	25.0	30.0
Gross profit per blockbuster drama (sales to China)	No sales	30.0	45.0	60.0	75.0	90.0
	10.0	60.0	75.0	90.0	105.0	120.0
	15.0	75.0	90.0	105.0	120.0	135.0
	20.0	90.0	105.0	120.0	135.0	150.0
	25.0	105.0	120.0	135.0	150.0	165.0
	30.0	120.0	135.0	150.0	165.0	180.0

[Gross profit estimate for 2 Netflix originals]

Per-episode production cost W1.5bn x 10 episodes x GPM 20% x 2 series = **W6.0bn**

Gross profit W217.6bn
 - 37 non-blockbuster - W106.6bn
 - 3 blockbusters - W105.0bn
 - 2 Netflix originals - W6.0bn

Operating profit W195.6bn
 Net profit W152.8bn

Fair market cap W3.82tn (net profit W152.8bn x target P/E 25x) → **W136,000/share**

Source: Yuanta Securities

2020E revenue scenario

(42 dramas in total = 36 non-blockbuster + 4 blockbusters + 2 Netflix originals)

[Gross profit estimate for 36 non-blockbuster dramas with 16 episodes]

(Wbn)		Per-episode production cost for non-blockbuster drama				
		0.5	0.55	0.6	0.65	0.7
Average GPM for non-blockbuster	15%	43.2	47.5	51.8	56.2	60.5
	20%	57.6	63.4	69.1	74.9	80.6
	25%	72.0	79.2	86.4	93.6	100.8
	30%	86.4	95.0	103.7	112.3	121.0
	35%	100.8	110.9	121.0	131.0	141.1
	40%	115.2	126.7	138.2	149.8	161.3

[Gross profit estimate for 4 blockbuster dramas]

(Wbn)		Gross profit per blockbuster drama (excl sales to China)				
		10.0	15.0	20.0	25.0	30.0
Gross profit per blockbuster drama (sales to China)	No sales	40.0	60.0	80.0	100.0	120.0
	10.0	80.0	100.0	120.0	140.0	160.0
	15.0	100.0	120.0	140.0	160.0	180.0
	20.0	120.0	140.0	160.0	180.0	200.0
	25.0	140.0	160.0	180.0	200.0	220.0
	30.0	160.0	180.0	200.0	220.0	240.0

[Gross profit estimate for 2 Netflix originals]

Per-episode production cost W1.5bn x 10 episodes x GPM 20% x 2 series = **W6.0bn**

Gross profit W249.7bn
 - 36 non-blockbuster - W103.7bn
 - 4 blockbusters - W140.0bn
 - 2 Netflix originals - W6.0bn

Operating profit W232.8bn
 Net profit W180.9bn

Fair market cap W4.53tn (net profit W180.9bn x target P/E 25x) → **W161,000/share**

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	453	580
Cost of sales	133	240	295	331	362
Gross profit	22	47	72	122	218
SG&A	5	14	14	17	22
Operating profit	17	33	58	105	196
EBITDA	39	74	105	138	235
Non-op profit/loss	-6	-3	6	5	6
Forex gain/loss	0	-1	3	0	0
Net interest income	-1	-1	4	5	7
Equity-meth gain/loss	0	0	0	0	0
Other	-5	0	0	0	-2
Net prof before income tax	10	30	64	110	202
Income tax	2	6	15	27	49
Net profit from continuing ops	8	24	48	83	153
Net profit from discontinued ops	0	0	0	0	0
Net profit	8	24	48	83	153
NP for controlling interest	8	24	48	83	153
Total comprehensive income	8	24	48	83	152
Total comprehensive income, CI	8	24	34	60	109

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	321	406	567
Cash & cash equivalents	12	51	51	128	267
Accts rec & other	39	55	69	77	98
Inventory	0	1	2	3	4
Non-current assets	161	170	187	187	187
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	508	593	754
Current liabilities	84	91	90	92	100
Accts payable & other	20	34	40	41	50
ST financial liabilities	8	0	0	0	0
Liquid LT liabilities	0	10	0	0	0
Non-current liabilities	21	0	1	1	1
LT financial liabilities	0	0	0	0	0
Debentures	20	0	0	0	0
Total liabilities	106	91	91	93	101
Equity, controlling interest	136	368	417	500	653
Paid-in capital	11	14	14	14	14
Capital surplus	115	320	320	320	320
Retained earnings	8	32	80	164	317
Equity, non-controlling interest	0	0	0	0	0
Total equity	136	368	417	500	653
Net debt	16	-182	-204	-281	-420
Total debt	28	10	0	0	0

Cash flow statement

FY ends Dec (Wbn)	2016A	2017A	2018E	2019E	2020E
Operating cash flow	-12	-7	18	44	113
Net profit	8	24	48	83	153
Depreciation & amortization	0	0	0	0	0
Forex gain/loss	0	1	-2	0	0
Affiliate invest gain/loss	0	0	0	0	0
Inc (dec) in net working cap	-46	-73	-76	-73	-81
Other	25	41	47	33	40
Investing cash flow	-70	-141	-32	-33	-40
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	-32	-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	-10	0	0
Inc (dec) in equity	56	208	0	0	0
Cash dividend	0	0	0	0	0
Other	10	-2	0	0	0
Other cash flow	0	0	25	66	67
Inc (dec) in cash & equivalents	12	40	0	77	139
Beginning cash & equivalents	0	12	0	51	128
Ending cash & equivalents	12	51	51	128	267
NOPLAT	17	33	58	105	196
FCF	-12	-6	15	38	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: Yuenta Securities

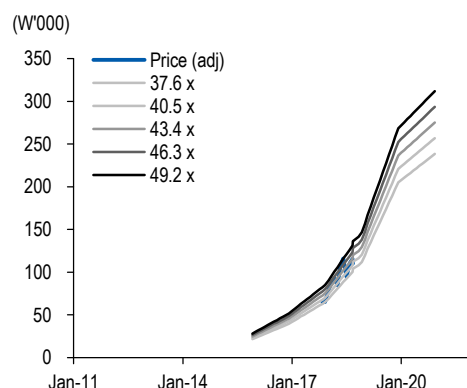
Valuation

FY ends Dec	2016A	2017A	2018E	2019E	2020E
EPS (won)	569	1,050	1,727	2,976	5,448
BPS (won)	6,176	13,141	14,873	17,838	23,286
EBITDA/shr (won)	27,127	3,271	3,736	4,912	8,385
SPS (won)	10,795	12,628	13,077	16,152	20,686
DPS (won)	0	0	0	0	0
P/E (x)	-	60.3	63.7	37.0	20.2
P/B (x)	-	4.8	7.4	6.2	4.7
EV/EBITDA (x)	-	21.4	27.5	20.4	11.3
P/S (x)	-	5.0	8.4	6.8	5.3

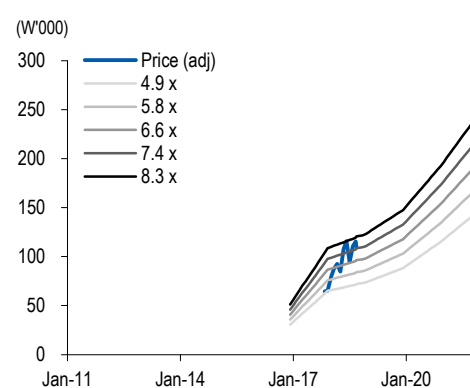
Key financial data

FY ends Dec	2016A	2017A	2018E	2019E	2020E
Sales (% YoY)	0.0	85.7	27.8	23.5	28.1
Operating profit (%YoY)	na	98.3	75.5	81.6	86.1
Net profit, CI (%YoY)	na	192.9	103.1	72.3	83.1
Gross margin (%)	14.0	16.4	19.6	26.9	37.5
Operating margin (%)	10.8	11.5	15.8	23.2	33.7
Net margin, CI (%)	5.3	8.3	13.2	18.4	26.3
EBITDA margin (%)	25.1	25.9	28.6	30.4	40.5
ROIC (%)	21.8	19.7	28.3	47.1	82.8
ROA (%)	6.7	6.8	10.0	15.2	22.7
ROE (%)	12.0	9.5	12.3	18.2	26.5
Debt-to-equity (%)	77.8	24.7	21.9	18.5	15.5
Net debt-to-equity (%)	12.1	-49.4	-49.0	-56.2	-64.4
OP/financing cost (x)	19.5	19.0	1,273.2	0.0	0.0

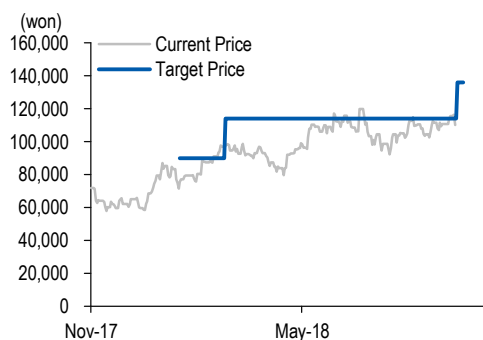
P/E band chart



P/B band chart



Studio Dragon (253450 KS) ratings and target price history



Date	Ra ing	TP (won)	TP time f a e	Difference (%)	
				vs avg price	vs high (low)
2018/10/04	BUY	136,000	1 yr		
2018/03/19	BUY	114,000	1 yr	-10.46	5.09
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	1.1
BUY	86.9
HOLD	11.4
SELL	0.6
Total	100.0

Note: As of Sep 29

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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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