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Company Update



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Studio Dragon (253450)

Content to drive growth

- Studio Dragon posted a 3Q operating profit of KRW21.5b (up 223% y-y), missing consensus of KRW24.5b by 12.4%.
- The firm enjoyed solid sales domestically and overseas thanks to the popularity of its dramas (such as *Mr. Sunshine* and *What's Wrong with Secretary Kim?*). The sale of other tent pole dramas in 4Q should boost earnings momentum.
- We maintain BUY on Studio Dragon, with a target price of KRW140,000.

WHAT'S THE STORY?

3Q review: Studio Dragon yesterday posted 3Q results showing operating profit up 223% y-y to KRW21.5b, missing consensus of KRW24.5b by 12.4%. Nevertheless, the results were still decent thanks to stable performances from dramas and the sales of *Mr. Sunshine* copyright at home and overseas. As the firm's productions grew in size, sales climbed 59.7% y-y to KRW123.7b, resulting in a record operating margin of 17.4% (up 8.8%pts y-y).

Content sales outstanding: Booking the copyright sale of *Mr. Sunshine* to Netflix was the major driver behind earnings momentum. But we also note that domestic VOD sales leapt 68.5% y-y to KRW17.2b, backed by popularity of other dramas (including *What's Wrong with Secretary Kim?*). Earnings momentum should remain strong in 4Q, supported by tent pole dramas *Encounter* and *Memories of the Alhambra*, but exactly how strong will depend on the sale of copyright for the latter in China.

Growth potential outweighs valuation burden: Shares are trading at 39.4x 2019 P/E. Although some may deem that demanding, we reiterate our BUY rating and target price of KRW140,000, noting the ample growth potential related to: 1) growing content sales to Chinese OTT operators; 2) the likelihood of contracts to produce one or two more Netflix Original Series dramas that will air next year; and 3) the joint production of dramas with Chinese OTT service providers—a possibility first mentioned only recently.

AT A GLANCE

SELL HOLD **BUY**

Target price KRW140,000 (43.6%)

Current price KRW97,500

Market cap	KRW2.7/USD2.4b
Shares (float)	28,037,240 (23.9%)
52-week high/low	KRW119,800/KRW57,800
Avg daily trading value (60-day)	KRW18.0b/ USD16.0m

ONE-YEAR PERFORMANCE

	1M	6M	12M
Studio Dragon (%)	-10.2	16.2	n/a
Vs Kosdaq (%pts)	1.8	45.8	n/a

KEY CHANGES

(KRW)	New	Old	Diff
Recommend.	BUY	BUY	
Target price	140,000	140,000	0.0%
2018E EPS	1,426	1,412	1.0%
2019E EPS	2,473	2,364	4.6%

SAMSUNG vs THE STREET

No of estimates	15
Target price	136,067
Recommendation	3.9

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

SUMMARY OF 3Q RESULTS

(KRWb)	3Q18	Chg		Diff (%)	
		(% y-y)	(% q-q)	Samsung	Consensus
Sales	124	59.6	66.5	(2.5)	1.5
Operating profit	21	222.8	193.1	11.1	(12.4)
Pre-tax profit	22	246.8	99.5	12.9	(15.6)
Net profit	17	206.3	95.2	18.5	(9.2)
Margins (%)					
Operating profit	17.4				
Pre-tax profit	17.8				
Net profit	14.0				

Source: Company data, Samsung Securities estimates

VALUATION SUMMARY

	2017	2018E	2019E
Multiples (x)			
P/E	92.9	68.4	39.4
P/B	7.4	6.7	5.7
EV/EBITDA	34.3	22.0	13.3
Div yield (%)	0.0	0.0	0.0
EPS growth (% y-y)	84.5	35.8	73.5
ROE (%)	9.5	10.3	15.6
Per-share data (KRW)			
EPS	1,050	1,426	2,473
BVPS	13,141	14,567	17,040
DPS	0	0	0

Table 1. 3Q results

(KRWb)	3Q18			Diff (%)		3Q17	2Q18	Chg	
	Actual	Samsung	Consensus	Samsung	Consensus			(% y-y)	(% q-q)
Sales	124	127	122	(2.5)	1.5	77	74	59.6	66.5
Broadcasting rights	49	51	n/a	n/a	n/a	42	34	17.1	43.6
Copyright sales	63	64	n/a	n/a	n/a	23	29	172.0	119.8
Other	11	12	n/a	n/a	n/a	12	11	(8.3)	(0.1)
COGS	99	102	n/a	n/a	n/a	67	64	48.2	55.4
SG&A costs	3	6	n/a	n/a	n/a	4	3	(16.6)	0.9
Operating profit	21	19	25	11.1	(12.4)	7	7	222.8	193.1
Pre-tax profit	22	20	26	12.9	(15.6)	6	11	246.8	99.5
Net profit	17	15	19	18.5	(9.2)	6	9	206.3	95.2
Margins (%)									
Operating margin	17.4	15.2	20.1			8.6	9.9		
Pre-tax margin	17.8	15.4	21.4			8.2	14.9		
Net margin	14.0	11.5	15.7			7.3	12.0		

Source: Company data, FnGuide, Samsung Securities

Table 2. Forecast revisions

(KRWb)	2018E					2019E				
	Old	New	Chg (%)	Consensus	Diff (%)	Old	New	Chg (%)	Consensus	Diff (%)
Sales	399	394	(1.4)	386	2.0	556	558	0.3	507	10.1
COGS	330	327	(0.8)	309	6.0	448	448	0.0	389	15.1
SG&A costs	17	14	(14.6)	16	(7.7)	20	18	(11.1)	18	2.9
Operating profit	52	52	(0.9)	61	(15.6)	88	92	4.6	100	(8.0)
Pre-tax profit	56	56	0.5	67	(16.0)	89	94	6.2	105	(10.0)
Net profit	42	43	2.4	52	(18.0)	67	71	6.2	81	(13.0)
EBITDA	115	115	(0.6)	113	1.4	180	184	2.2	81	125.7
Adj. EPS (KRW)	1,412	1,426	1.0	1,852	(23.0)	2,473	2,473	(0.0)	2,898	(14.7)
Margins (%)										
Operating margin	13.1	13.2		15.9		15.9	16.5		19.8	
Pre-tax margin	13.9	14.2		17.2		16.0	16.9		20.7	
Net margin	10.5	10.9		13.5		12.0	12.7		16.1	
EBITDA margin	28.9	29.1		29.3		32.3	32.9		16.1	

Source: Samsung Securities estimates

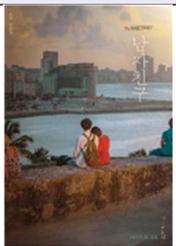
Table 3. 3Q drama lineup

Title	Ratings (%)	Air dates	Channel
Mr. Sunshine	12.5	Jul 7-Sep 30	tvN
Familiar Wife	6.6	Aug 1-Sep 20	tvN
Voice 2	4.8	Aug 11-Sep 16	OCN
Hundred Days' Husband	8.7	Sep 10-Oct 30	tvN
Hand: The Guest	2.9	Sep 12-Nov 1	OCN
Player	4.7	Sep 29-Nov 11	OCN
The Smile Has Left Your Eyes	3.0	Oct 3-Nov 22	tvN
Room No. 9	4.9	Oct 6-Nov 25	tvN
Tale of Fairy	5.3	Nov 5-Dec 25	tvN

Note: As of Nov 7

Source: Company data, AGB Nielson, Samsung Securities

Table 4. 4Q drama lineup

Title	The Smile Has Left Your Eyes	Room No. 9	Tale of Fairy	Encounter	Memories of the Alhambra
					
Premier	Oct 3	Oct 6	Nov 5	Nov 28	Dec 1
Writer	Hye-jin Song	Sung-hee Jung	Kyung-seon Yu	Young-a Yu	Jae-jung Song
Channel	tvN	tvN	tvN	tvN	tvN
Cast	In-guk Seo, So-min Jung, Sung-woong Park	Hee-seon Kim, Hae-suk Kim	Chae-won Moon, Hyun-min Yun	Bo-gum Park, Hye-kyo Song	Hyun-bin, Shin-hye Park

Source: Company data

Key takeaways from 3Q earnings conference call

Q: Joint productions with and drama sales to Chinese OTT operators?

Studio Dragon is in talks with several Chinese OTT service providers—although it cannot yet specify which ones—to co-produce a number of dramas annually based on its own intellectual property (IP). At present, the firm is likely to co-produce one or two dramas with Chinese firms next year. Meanwhile, Studio Dragon is also in negotiations with Chinese firms for the copyright sale of *Memories of the Alhambra*, which should air in Korea in December.

Q: Library sales trends?

With the Studio Dragon’s IP expanding, its number of dramas available for library sales is on the rise. However, the library sales portion of total copyright sales has not increased much as production costs of new dramas are growing (implying a rise in sales of new dramas).

Table 5. Results and forecasts

(KRWb)	2017	2018E	2019E	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18	4Q18E	1Q19E	2Q19E	3Q19E	4Q19E
Sales	287	394	558	75	62	77	72	80	74	124	116	131	143	136	148
Broadcasting	131	178	224	26	24	42	39	41	34	49	54	55	56	51	61
Copyright sales	112	175	283	36	26	23	26	32	29	63	50	64	74	72	73
Other	44	42	51	13	12	12	7	7	11	11	12	12	12	13	13
Cost of goods sold	240	327	448	59	50	67	64	66	64	99	99	104	115	105	124
Production	210	289	390	49	42	60	58	59	56	86	88	90	100	90	109
Commission	17	26	42	5	4	3	4	5	4	10	8	10	11	11	11
Other	13	12	15	4	3	4	2	2	3	3	4	4	4	4	4
Gross profit	47	66	110	17	12	11	7	14	11	25	17	28	28	31	24
SG&A	14	14	18	3	3	4	4	3	3	3	5	4	4	4	6
Operating profit	33	52	92	14	9	7	3	11	7	21	12	24	24	26	18
Pre-tax profit	30	56	94	13	9	6	2	10	11	22	13	25	24	27	19
Net profit	24	43	71	13	3	6	2	7	9	17	10	18	18	20	14
Adjusted EPS (KRW)	1,050	1,426	2,473												
Margins (%)															
Operating margin	11.5	13.2	16.5	18.5	14.3	8.6	4.8	13.4	9.9	17.4	10.7	18.2	16.5	19.5	12.2
Pre-tax margin	10.6	14.2	16.9	17.6	14.5	8.2	2.3	12.3	14.9	17.8	11.2	18.7	16.9	20.0	12.6
Net margin	8.3	10.9	12.7	17.8	4.5	7.3	2.8	8.6	12.0	14.0	8.4	14.0	12.7	15.0	9.5

Source: Company data, Samsung Securities

Income statement

Year-end Dec 31 (KRWb)	2016	2017	2018E	2019E	2020E
Sales	154	287	394	558	732
Cost of goods sold	133	240	327	448	597
Gross profit	22	47	66	110	135
Gross margin (%)	14.0	16.4	16.8	19.8	18.5
SG&A expenses	5	14	15	18	22
Operating profit	17	33	52	92	114
Operating margin (%)	10.8	11.5	13.2	16.5	15.5
Non-operating gains (losses)	(6)	(3)	0	0	7
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
Pre-tax profit	10	30	52	92	121
Taxes	2	6	12	23	32
Effective tax rate (%)	22.4	21.2	23.4	25.0	26.3
Profit from continuing operations	8	24	40	69	89
Profit from discontinued operations	0	0	0	0	0
Net profit	8	24	40	69	89
Net margin (%)	5.3	8.3	10.2	12.4	12.2
Net profit (controlling interests)	8	24	40	69	89
Net profit (non-controlling interests)	0	0	0	0	0
EBITDA	39	74	115	184	243
EBITDA margin (%)	25.1	25.9	29.1	32.9	33.2
EPS (parent-based) (KRW)	569	1,050	1,426	2,473	3,178
EPS (consolidated) (KRW)	569	1,050	1,426	2,473	3,178
Adjusted EPS (KRW)*	569	1,050	1,426	2,473	3,178

Cash flow statement

Year-end Dec 31 (KRWb)	2016	2017	2018E	2019E	2020E
Cash flow from operations	(12)	(7)	125	197	255
Net profit	8	24	40	69	89
Non-cash profit and expenses	27	46	72	109	154
Depreciation	0	0	0	0	0
Amortization	22	41	63	92	129
Other	5	5	8	18	24
Changes in A/L from operating activities	(46)	(73)	25	41	44
Cash flow from investments	(70)	(141)	(100)	(122)	(160)
Change in tangible assets	(1)	(0)	0	0	0
Change in financial assets	(2)	(142)	(8)	(10)	(10)
Other	(66)	1	(92)	(112)	(150)
Cash flow from financing	93	188	(17)	1	1
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	76	96
Cash at beginning of year	0	12	51	59	135
Cash at end of year	12	51	59	135	231
Gross cash flow	35	70	111	179	243
Free cash flow	(14)	(7)	38	80	99

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
Current assets	81	290	309	398	507
Cash & equivalents	12	51	59	135	231
Accounts receivable	37	55	58	61	64
Inventories	0	1	1	1	1
Other current assets	33	182	191	201	211
Fixed assets	161	170	204	231	260
Investment assets	2	4	5	7	10
Tangible assets	1	1	1	1	1
Intangible assets	124	128	151	177	204
Other long-term assets	33	37	46	46	46
Total assets	242	459	513	629	767
Current liabilities	84	91	104	150	199
Accounts payable	6	6	8	12	15
Short-term debt	8	0	(7)	(7)	(7)
Other current liabilities	71	85	102	145	191
Long-term liabilities	21	0	0	1	1
Bonds & long-term debt	20	0	0	0	0
Other long-term liabilities	2	0	0	1	1
Total liabilities	106	91	105	151	200
Owners of parent equity	136	368	408	478	567
Capital stock	11	14	14	14	14
Capital surplus	115	320	320	320	320
Retained earnings	8	32	72	141	231
Other	2	3	3	3	3
Non-controlling interests' equity	0	0	0	0	0
Total equity	136	368	408	478	567
Net debt	16	(182)	(213)	(297)	(400)

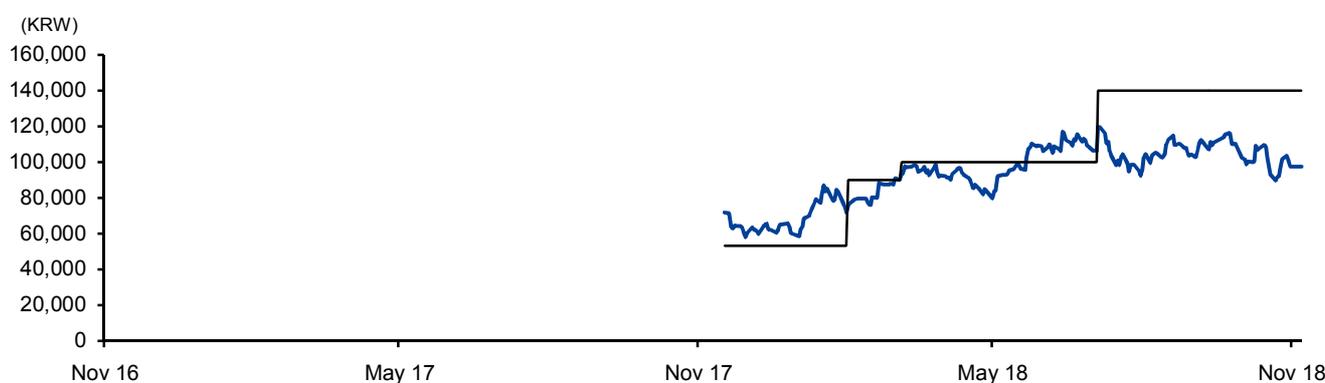
Financial ratios

Year-end Dec 31	2016	2017	2018E	2019E	2020E
Growth (%)					
Sales	nm	85.7	37.3	41.7	31.2
Operating profit	nm	98.3	57.2	77.8	23.2
Net profit	nm	192.9	67.6	73.5	28.5
Adjusted EPS**	nm	84.5	35.8	73.5	28.5
Per-share data (KRW)					
EPS (parent-based)	569	1,050	1,426	2,473	3,178
EPS (consolidated)	569	1,050	1,426	2,473	3,178
Adjusted EPS**	569	1,050	1,426	2,473	3,178
BVPS	6,176	13,141	14,567	17,040	20,218
DPS (common)	0	0	0	0	0
Valuations (x)					
P/E***	171.3	92.9	68.4	39.4	30.7
P/B***	15.8	7.4	6.7	5.7	4.8
EV/EBITDA	70.9	34.3	22.0	13.3	9.6
Ratios (%)					
ROE	6.0	9.5	10.3	15.6	17.1
ROA	3.4	6.8	8.2	12.1	12.8
ROIC	8.5	15.6	21.5	38.2	50.8
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)	(52.3)	(62.1)	(70.6)
Interest coverage (x)	19.5	19.0	325.3	(155.3)	(191.3)

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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

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BUY (85%) | HOLD (15%) | SELL (0%)

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