

May 29, 2019

Danny Lee Analyst
Internet, Game, Media, Leisure
82-2-6114-2960 drlee@kbf.com

Jeonghoon Son RA
82-2-6114-2910
jhson@kbf.com

Cut target price to KRW100,000 while reiterating BUY rating

We maintain our BUY rating on Studio Dragon, but cut the target price to KRW100,000, which was derived by applying a 2020 fair PER of 36x. We trimmed the target price, because we lowered our estimates for Studio Dragon’s 2019–20 NP attributable to parent by 19.2% and 17.2%, respectively, after cutting our estimates of revenues and profits from “Arthdal Chronicles” and China-related projects. That said, we maintain a positive stance on Studio Dragon, considering: 1) the upcoming airing of “Arthdal Chronicles,” the most anticipated drama this year and 2) drastic share price pullbacks seen recently.

Analysis of factors behind recent share price freefall

Studio Dragon’s stock price has declined 19.3% since May, burdened by: 1) concerns over production costs rises for “Arthdal Chronicles” and the potential for the drama’s sluggish profitability and 2) likely delays in content exports to China and joint projects with Chinese production studios.

1) Concerns over “Arthdal Chronicles” production cost rises seem excessive

We believe market jitters over the profit margin of “Arthdal Chronicles” are overblown. In fact, Studio Dragon has maintained profitability even from the stage of drama planning while eyeing advertisements, PPL, and content sales. “Arthdal Chronicles” is expected to suffer only minuscule losses or break even, considering KRW50–55bn in production costs, revenues from ads (KRW18bn estimated, KRW1bn per episode) and sales to Netflix (estimated at KRW30–35bn). If season 1 becomes a hit, this will bode well for the success of seasons 2–3, while profit-leverage effects are expected to expand from 2020, as expenses including filming sites will be fully reflected in 2019.

Buy maintain

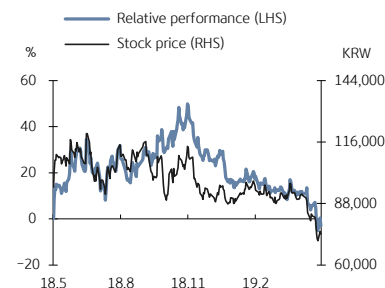
Target Price (lowered)	KRW100,000
Upside/Downside	35.0%
Current price (May 28)	KRW74,100
Consensus Target Price	KRW117,947
Market cap	USD1.8bn

Trading Data	
Free float	25.2%
Avg T/O Val (3M, KRWbn)	13.1
Foreign ownership	3.0%
Major shareholders	CJ E&M Corporation and 3 others
	74.4%

Share price performance	
(%)	1M 3M 6M 12M
Absolute	-17.6 -21.3 -34.5 -22.5
Relative	-13.1 -18.1 -34.8 -3.0

Forecast earnings & valuation

FY-end	2018A	2019E	2020E	2021E
OR (KRWbn)	380	466	536	632
OP (KRWbn)	40	55	98	122
NP to parent (KRWbn)	36	47	78	98
EPS (KRW)	1,278	1,666	2,786	3,500
EPS Growth (%)	21.7	30.4	67.2	25.6
PER (x)	72.3	44.5	26.6	21.2
EV/EBITDA (x)	21.2	14.5	12.7	11.2
PBR (x)	6.5	4.6	4.0	3.3
ROE (%)	9.3	11.0	16.0	17.1
Div. Yield (%)	NA	0.0	0.0	0.0



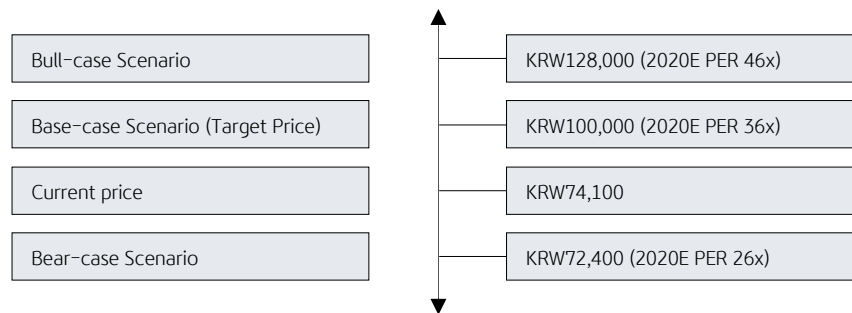
Source: Studio Dragon, KB Securities estimates

However, the TV series may face growing risks as production costs rise, considering a gap in per-episode production costs (KRW3.1bn for “Arthdal Chronicles” vs. KRW1.7bn for “Mr. Sunshine”) and the fact that its ad revenues (KRW1bn per episode) is similar to ad revenues for “Mr. Sunshine.”

2) Conservative approach needed for sales visibility in China

Concerns are mounting over possible delays in content sales to China and co-production as the US-China trade dispute continues. We stand by our previous view that co-production is more possible than content sales. However, it remains uncertain whether or not revenues from co-production will be generated starting in 2H19. A resultant reduction in sales will reach KRW25.6bn in 2019 and KRW50bn in 2020.

Investment opinion and risks



Base-case Scenario: Catalysts

- 1) Netflix original drama production volume increases
- 2) Viewership rate of drama "Arthdal Chronicles" increases

Bull-case Scenario: Upside risks

- 1) Netflix original drama production volume soars
- 2) Viewership rate of drama "Arthdal Chronicles" soars

Bear-case Scenario: Downside risks

- 1) Netflix original drama production volume decreases
- 2) Viewership rate of drama "Arthdal Chronicles" decreases

Revised earnings estimates

(KRWbn, %)	Previous		Revised		Change	
	2019E	2020E	2019E	2020E	2019E	2020E
OR	491.4	586.3	465.8	536.4	-5.2	-8.5
OP	70.0	119.0	55.3	97.7	-20.9	-17.9
NP to parent	57.9	94.4	46.7	78.1	-19.2	-17.2

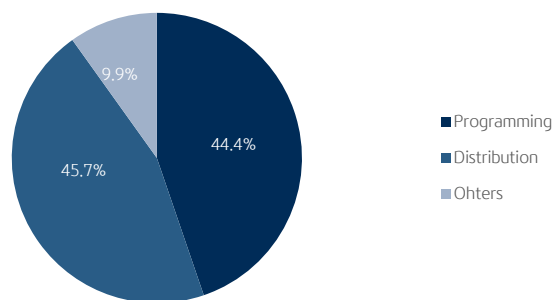
Source: KB Securities estimates

KB estimate vs. Consensus

(KRWbn, %)	KB est.		Consensus		Difference	
	2019E	2020E	2019E	2020E	2019E	2020E
OR	465.8	536.4	488.0	580.8	-4.6	-7.6
OP	55.3	97.7	59.8	90.2	-7.5	8.3
NP to parent	46.7	78.1	50.4	74.8	-7.3	4.5

Source: Wisefn, KB Securities estimates

OR composition (2019E, %)



Source: Company data, KB Securities

Valuation and target price calculation

- 1) Valuation method:
PER Valuation
- 2) Target price calculation:
2020E EPS KRW2,786 X Multiple 36x
- 3) Target price range:
KRW128,000 ~ KRW72,400
- 4) Valuation at target price:
2020E PER 36x

Earnings sensitivity analysis

(%)	EPS change	
	2019E	2020E
1%p rise in interest rate	+2.0	+2.1
1% rise in FX rate	+0.3	+0.4

Peer group comparison

(KRWbn, X, %)	Market Cap	PER		PBR		EV/EBITDA		ROE		Dividend Yield	
		2019E	2020E	2019E	2020E	2019E	2020E	2019E	2020E	2019E	2020E
Jcontentree	683	24.0	19.4	1.8	1.7	10.5	9.4	8.7	9.8	n/a	n/a
Netflix	185,196	87.6	52.0	21.9	15.5	52.2	35.1	23.6	29.0	0.0	0.0
Zhejiang Huace Film&TV	1,951	16.5	13.6	1.4	1.3	14.4	12.9	9.3	10.1	0.6	0.8
Beijing HualuBaina Film&TV	842	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a

Source: Bloomberg, KB Securities

Table 1. Studio dragon's 2Q19 consolidated earnings preview

(KRWon, %, %p)	2Q19E	1Q19	QoQ	2Q18	YoY	Prior	Diff.	Consensus	Diff.
OR	107.2	111.8	(4.2)	74.3	44.3	106.1	1.0	113.7	(5.7)
OP	9.9	11.0	(10.4)	7.3	34.9	9.8	1.2	12.3	(19.4)
OP margin	9.2	9.9	(0.6)	9.9	(0.6)	9.2	0.0	10.8	(1.6)
NP to parent	8.6	9.1	(5.5)	8.9	(2.8)	8.5	1.1	10.5	(17.7)
NP margin	8.1	8.2	(0.1)	12.0	(3.9)	8.0	0.0	9.2	(1.2)

Source: FnGuide, KB Securities estimates

Table 2. Studio Dragons's consolidated earnings trend and estimates

(KRWbn)	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19E	3Q19E	4Q19E	2017	2018	2019E	2020E
OR	79.9	74.3	123.7	101.7	111.8	107.2	139.7	107.1	286.8	379.5	465.8	536.4
(QoQ %)	11.1	(7.0)	66.5	(17.7)	9.9	(4.2)	30.3	(23.3)	-	-	-	-
(YoY %)	6.0	19.6	59.6	41.5	40.0	44.3	12.9	5.3	46.7	32.3	22.7	15.1
Programming	40.7	34.1	48.9	54.4	44.1	49.1	62.4	51.3	131.2	178.1	206.9	248.0
Distribution	32.1	28.8	63.4	37.8	56.2	46.1	65.3	45.3	111.8	162.1	212.9	237.8
Others	7.1	11.4	11.4	9.5	11.5	12.0	12.0	10.5	43.7	39.4	46.0	50.6
OP	10.7	7.3	21.5	0.4	11.0	9.9	17.5	16.9	33.0	39.9	55.3	97.7
(QoQ %)	207.1	(31.3)	193.5	(97.9)	2,400.7	(10.4)	77.2	(3.4)	-	-	-	-
(YoY %)	(23.7)	(17.7)	223.0	(87.3)	3.5	34.9	(18.5)	3,736.0	55.6	21.0	38.7	76.5
OP margin (%)	13.3	9.9	17.4	0.4	9.9	9.2	12.5	15.8	11.5	10.5	11.9	18.2
NP to parent	7.9	8.9	17.3	1.7	9.1	8.6	14.6	14.4	23.8	35.7	46.7	78.1
(QoQ %)	293.5	13.0	94.2	(89.9)	422.6	(5.5)	69.2	(1.4)	-	-	-	-
(YoY %)	(41.3)	217.2	204.6	(12.5)	16.2	(2.8)	(15.4)	723.6	-	49.9	30.8	67.2
NP margin (%)	9.8	12.0	14.0	1.7	8.2	8.1	10.5	13.4	8.3	9.4	10.0	14.6

Source: Company data, KB Securities estimates

Table 3. Comparison of revised earnings estimates

(KRWbn, %, %p)	2019E					2020E				
	Changed	Previous	Diff.	Cons.	Diff.	Changed	Previous	Diff.	Cons.	Diff.
OR	465.8	491.4	(5.2)	488.0	(4.6)	536.4	586.3	(8.5)	580.8	(7.6)
OP	55.3	70.0	(20.9)	59.8	(7.5)	97.7	119.0	(17.9)	90.2	8.3
OP margin	11.9	14.2	(2.4)	12.3	(0.4)	18.2	20.3	(2.1)	15.5	2.7
NP to parent	46.7	57.9	(19.2)	50.4	(7.3)	78.1	94.4	(17.2)	74.8	4.5
NP margin	10.0	11.8	(1.7)	10.3	(0.3)	14.6	16.1	(1.5)	12.9	1.7

Source: FnGuide, KB Securities estimates

Table 4. PER Valuation

(KRWbn, %, '000, KRW)	Note
2020E NP to parent	78.1
Target PER	36.0
Fair market cap.	2,813
# of outstanding shares	28,037
Target price	100,000

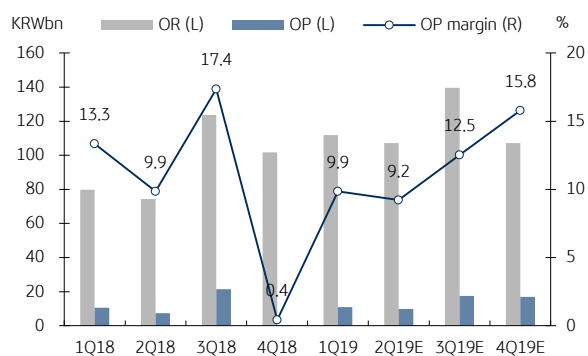
Source: KB Securities estimates

Table 5. Studio dragon's main drama line-up

Year	No.	distributor	Title	Episode date	#	Writer	Director	Main cast	Viewership rating (avg/high)	
2019	1	tvN	The Crowned Clown	Jan. 7~Mar. 4	16	Kim Seon-Duk	Kim Hee-Won	Yeo Jin-Gu, Lee Se-Young	8.1	10.5
	2		Romance is a Bonus Book	Jan. 26~Mar. 17	16	Jung Hyun-Jung	Lee Jung-Hyo	Lee Jong-Suk, Lee Na-Young	5.0	6.4
	3		Touch Your Heart	Feb. 6~Mar. 28	16	Lee Myung-Sook	Park Joon-Hwa	Lee Dong-Wook, Yoo In-Na	4.5	4.6
	4		He is Psychometric	Mar. 11~Apr. 30	16	Yang Jin-Ah	Kim Byung-Soo	Jin Young, Shin Ye-Eun	2.3	2.7
	5		Confession	Mar. 23~May. 12	16	Lim Hee-Chul	Kim Cheol-Kyu	Lee Jun-Ho, Yoo Jae-Myoung	4.6	5.4
	6		Her Private Life	April. 10~May. 30	16	Kim Hye-Young	Hong Jong-Chan	Park Min-Young, Kim Jae-Wook	2.5	3.0
	7		Abyss	May .6~June. 25	16	Moon Soo-Yeon	Yoo Je-Won	Park Bo-Young, Ahn Hyo-Seop	3.6	3.7
	8		Arthdal Chronicles	Jun. 1~	18	Kim Young-Hyun	Kim Won-Seok	Song Joong-Ki	-	-
	9		Search: WWW	Jun. 5~Jul. 25	16	Kwon Do-Eun	Jung Ji-Hyun	Im Soo-Jung	-	-
	10		When the Devil Calls Your Name	2H19	16	Noh Hae-young	Min Jin-kee	Jeong Kyeong-Ho	-	-
	11		60 Days, Designated Survivor	2H19	16	Kim Tae-hee	Yoon Jong-sun	Ji Jin-Hui	-	-
	12		Man Who Bakes Bread	2H19	-	Joo Hwa-mi	Lee Jong-jae	Seo Ji-Hun	-	-
	13		Let Me Melt	2H19	-	Baek Mi-kyoung	Shin Woo-cheol	Ji Chang-Wook	-	-
	14		The Great Show	2H19	-	Seol Joon-seok	Shin Yong-hui	Song Seung-Heon	-	-
	15		Hotel Del Luna	2H19	-	Hong Jung-eun	Oh Choong-hwan	Yeo Jin-Gu	-	-
	16		Paul Who Fell From The Sky	Undefined	-	-	Kim Sang-ho	Yun Hyeon-Min	-	-
	17	OCN	Trap	Feb .9~March. 3	7	Nam Sang-wook	Park Shin-woo	Lee Seo Jin	3.7	4.0
	18		Possessed	Mar .6~April .25	16	Park Hee-Kang	Choi Do-Hoon	Song Sae-Byeok , Ko Joon-Hee	1.8	2.6
	19		Kill It	Mar .23~April .28	12	Son Hyun-Soo	Nam Sung-Woo	Jang Ki-Yong, Na-Na	1.7	2.7
	20		Save Me 2	May .8~Jun. 20	14	Seo Joo-Yeon	Lee Kwon	Lee Som, Uhm Tae-Gu	1.4	1.4
	21		Voice 3	May .11~Jun. 30	16	Ma Jin-Won	Nam Ki-Hun	Lee Ha Na	-	-
	22		Hell is Other People	2H19	10	Jung Yi-do	Lee Chang-hee	Lee Dong-Wook	-	-
	23	Netflix	Love alarm	2019	8	Lee Ah-hyun	Lee Na-jeong	Kim So-Hyun	-	-
	24		I am Alone	2019	12	Ryu Yong-jae	Lee Sang-hyup	Ko Seong-Hee	-	-
	25	MBC	Spring Night	May. 22~July. 11	16	Kim Eun	Ahn Pan-Suk	Jung Hae-In	-	-
	26	SBS	Doctor Room	July ~		Kim Ji-eun	Cho Soo-won	Ji Sung	-	-

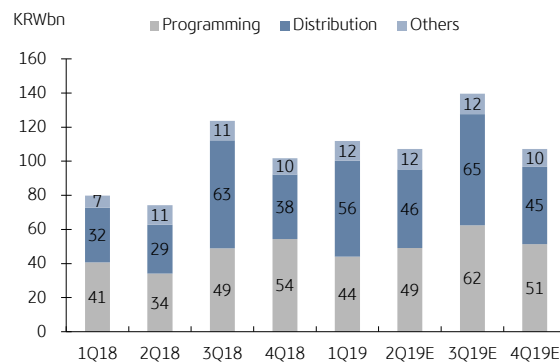
Source: Company data, KB Securities

Fig 1. Earnings trend and estimates



Source: Company data, KB Securities estimates

Fig 2. OR composition



Source: Company data, KB Securities estimates

Profit & Loss					
(KRWbn)	2017A	2018A	2019E	2020E	2021E
(Reporting standard)	(IFRS-C)	(IFRS-C)	(IFRS-C)	(IFRS-C)	(IFRS-C)
Operating revenue	287	380	466	536	632
Cost of sales	240	324	392	418	486
Gross profit	47	56	74	119	146
SG&A expenses	14	16	18	21	24
Operating profit	33	40	55	98	122
EBITDA	74	115	125	133	141
Non-operating accounts	-3	6	7	5	7
Interest income	1	4	9	6	8
Interest expenses	2	0	2	1	1
Profit on equity method	0	0	0	0	0
Net other non-operating income	0	0	0	0	0
Profit before tax	30	46	63	103	129
Income tax expense	6	10	16	25	31
Net profit	24	36	47	78	98
NP to parent	24	36	47	78	98
Adj. net profit	24	36	47	78	98

Operating Statistics & Ratios					
(%)	2017A	2018A	2019E	2020E	2021E
OR growth	85.7	32.4	22.7	15.2	17.8
OP growth	98.3	21.0	38.7	76.5	25.0
EBITDA growth	91.4	55.1	8.3	6.6	5.6
NP growth of parent	193.0	50.2	30.5	67.2	25.6
GP margin	16.4	14.6	15.8	22.1	23.1
OP margin	11.5	10.5	11.9	18.2	19.3
EBITDA margin	25.9	30.3	26.8	24.8	22.2
EBT margin	10.6	12.0	13.5	19.2	20.5
NP margin	8.3	9.4	10.0	14.6	15.5

Cash Flow					
(KRWbn)	2017A	2018A	2019E	2020E	2021E
Cash flow from operating activities	-7	-29	126	125	130
Net profit	24	36	47	78	98
Depreciation & amortization	41	75	69	35	18
Other non-cash adjustments	5	-1	16	25	31
Investments in working capital	-73	-139	10	11	13
Decrease(Increase) in Receivables	-14	-27	-3	-3	-3
Decrease(Increase) in Inventories	-2	0	0	0	0
Increase(Decrease) in Payables	9	26	2	3	3
Other operating cash flow	20	36	-16	-25	-31
Cash flow from investing activities	-141	141	-9	-10	-11
Capital expenditure	0	0	-1	-1	-1
Investments in intangibles	0	0	-1	-1	-1
Changes in investment assets	-141	138	0	0	0
Other investment cash flow	0	3	-7	-8	-8
Cash flow from financing activities	188	-10	33	6	7
Proceeds from (repayments of) debt	-18	-10	33	6	7
Changes in equity	208	0	0	0	0
Dividends paid	0	0	0	0	0
Other financing cash flow	-2	0	0	0	0
Other cash flow	0	0	0	0	0
Increase/decrease in cash	40	102	150	121	126
Cash and cash equivalents at FYE	51	153	303	423	549
Free cash flow	-7	-29	125	124	129
Net cash flow	199	-29	117	115	119
Net cash (net debt)	183	153	270	385	504

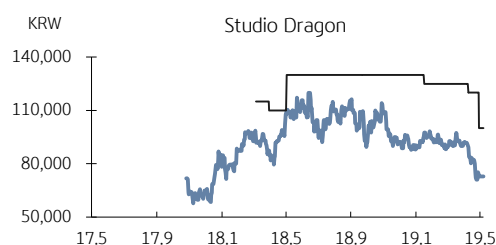
Source: Studio Dragon, KB Securities estimates

Statement of financial position					
(KRWbn)	2017A	2018A	2019E	2020E	2021E
(Reporting standard)	(IFRS-C)	(IFRS-C)	(IFRS-C)	(IFRS-C)	(IFRS-C)
Total assets	459	512	606	705	827
Current assets	290	247	401	525	655
Cash and cash equivalents	51	153	303	423	549
Current financial assets	141	2	3	3	3
Trade receivables	55	69	72	74	77
Inventories	1	1	1	1	1
Other current assets	41	22	23	24	25
Non-current assets	170	265	205	180	172
Investment assets	4	4	4	4	4
Property, plant and equipment	1	1	2	3	4
Intangible assets	128	199	131	97	80
Other non-current assets	36	53	60	67	76
Total liabilities	91	111	158	179	203
Current liabilities	91	108	122	137	154
Trade payables	6	20	22	25	28
Short-term financial liabilities	10	0	0	0	0
Other current liabilities	75	89	100	112	126
Non-current liabilities	0	3	36	42	49
Non-current financial liabilities	0	2	35	41	48
Other non-current liabilities	0	0	0	0	0
Total equity	368	401	448	526	624
Issued capital	14	14	14	14	14
Share premium	320	320	320	320	320
Other equity interest	3	0	0	0	0
Accumulated other comprehensive income	0	-1	-1	-1	-1
Retained earnings	32	68	114	193	291
Equity attributable to owners of parent	368	401	448	526	624
Non-controlling Interests	0	0	0	0	0

Key Ratio					
(X, %, KRW)	2017A	2018A	2019E	2020E	2021E
Multiples					
PER	61.9	72.3	44.5	26.6	21.2
PBR	4.9	6.5	4.6	4.0	3.3
PSR	5.1	6.8	4.5	3.9	3.3
EV/EBITDA	22.1	21.2	14.5	12.7	11.2
EV/EBIT	49.7	61.1	32.7	17.3	12.9
Dividend yield, ordinary (%)	NA	NA	0.0	0.0	0.0
EPS	1,050	1,278	1,666	2,786	3,500
BPS	13,141	14,305	15,972	18,758	22,258
SPS	12,628	13,539	16,605	19,120	22,518
DPS (Annual, Ordnry.)	0	0	0	0	0
Cash dividends payout ratio (%)	0.0	0.0	0.0	0.0	0.0
Operating performance					
ROE	9.5	9.3	11.0	16.0	17.1
ROA	6.8	7.4	8.4	11.9	12.8
ROIC	15.6	15.1	20.5	50.3	78.2
Financial structure (%)					
Total liab./equity	24.7	27.7	35.2	34.0	32.5
Net debt/equity	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash
Current Ratio	3.2	2.3	3.3	3.8	4.3
Interest coverage (x)	19.0	343.0	26.4	81.4	101.8
Activity ratios					
Asset turnover (x)	0.8	0.8	0.8	0.8	0.8
Receivables turnover (x)	6.2	6.1	6.6	7.4	8.3
Inventory turnover (x)	0.0	405.4	805.4	927.4	1,092.2

Disclosures

Rating and Target Price Changes (Share price —, Target Price —)



Studio Dragon (253450)

Date	Rating	Target Price (KRW)	Differential (%)	
			Avg.	Max/Min
18-04-03	Buy	115,000	-20.05	-15.74
18-04-29	Buy	110,000	-15.81	-2.00
18-06-01	Buy	130,000	-18.37	-7.85
18-12-01	6 month later	130,000	-28.13	-16.08
19-02-15	Buy	125,000	-25.98	-21.36
19-05-09	Buy	120,000	-34.46	-30.08
19-05-29	Buy	100,000		

KB Securities has not provided in advance the material contained in this report to any institutional investor or third party. The analyst(s), who wrote this report, does not have any financial interest in the company(ies) covered herein. The author(s) of this report confirms that the material contained herein correctly represents his/her/their opinion and that it has been prepared faithfully without any undue influence or intervention.

Proportion of investment rating (as of March 31, 2019)

Buy	Hold	Sell
71.9	28.1	-

* Note: Based on reports presented with investment ratings over the past one year

Classification and Standards for Investment Rating

Investment Rating for Company

(based on estimation of six-month absolute returns)

Buy: +15% or beyond	Hold: Between 15% and -15%	Sell: -15% or beyond
---------------------	----------------------------	----------------------

Note: KB Securities's classification of investment ratings has shifted from four stages (Strong BUY, BUY, Marketperform, Underperform) to three stages (Buy, Hold, Sell) based on Korean reports since February 23, 2017.

Investment Rating for Industry

(based on estimation of six-month absolute returns)

Positive:	Neutral:	Negative:
To outperform market	To match market performance	To underperform market

Notes: The industry rating system of KB Securities has shifted from (Overweight, Neutral, Underweight) to (Positive, Neutral, Negative) as of Jun 28, 2017

All KB Securities Research is available via the following electronic databases: Bloomberg, Thomson Reuters, FactSet. Contact your KB Securities sales representative for access.

This report has been prepared for informational purposes only, and does not constitute an offer or solicitation of a contract for trading. Opinions in this report reflect professional judgment at this date based on information and data obtained from sources KB Securities considers reliable. However, KB Securities does not guarantee that the information and data are accurate or complete, and, therefore, this report is subject to change without prior notice. Individual investments should be made based on each client's own judgment and we expressly disclaim all liability for any investment decisions and any results thereof. This report is a copyrighted material of KB Securities and, thus, it may not be reproduced, distributed, or modified without the prior consent of KB Securities. This report is not prepared for academic purposes and any third party wishing to quote from it for academic publications should receive the prior consent of KB Securities.