

Studio Dragon (253450 KQ)

HJ Kim
hoijae.kim@daishin.com

GY Lee
gayeon.lee@daishin.com

Rating **BUY**
maintain

6M TP (W) **115,000**
maintain

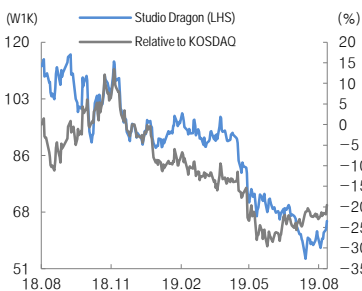
CP (W)
(19.09.03) **65,500**

Media

Industry 4.0 safety rating ■ Neutral Green

KOSDAQ	620.02
Market cap (Wbn)	1,839
Market cap portion (%)	0.88
Paid-in capital (common; Wbn)	14
52w high/low (W)	116,300 / 54,000
120d avg. trading volume (Wbn)	10.8
Foreign ownership (%)	2.81
Major shareholders	CJ E&M +5: 74.37%

(%)	1M	3M	6M	12M
Abs. return	10.3	-2.1	-30.4	-39.2
Rel. return	9.5	10.1	-17.9	-19.9



Love alarm is about to ring

BUY and 6M TP of W115,000 maintained

- The target price of W115,000 for Studio Dragon is based on our residual income model, which we believe is an appropriate valuation method given its projected NP CAGR of 26% over the next five years and an increase in its annual drama production volume (from the current 25 to 40 titles).

Stock plunges to compelling level on disappointing viewership

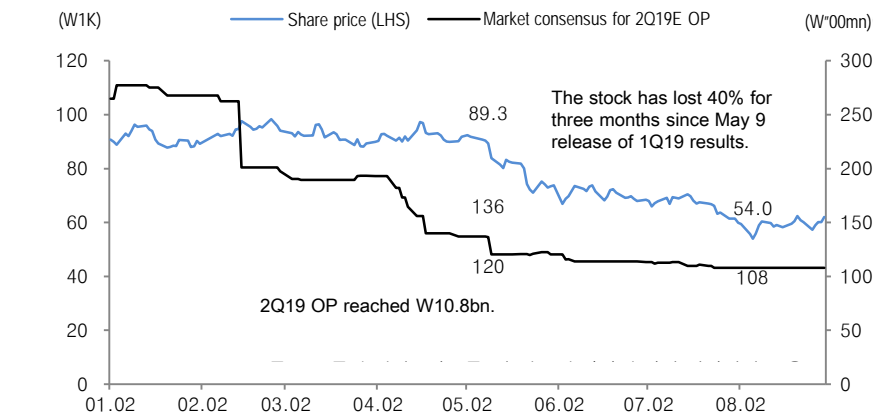
- Studio Dragon's stock has lost about 40% of its value over the past three months since the posters and teasers of *Arthdal Chronicles*, whose production cost is estimated to be about five times the average, were unveiled in early May. The K-drama production house currently trades at a valuation low enough to sound the "love alarm." (In the Studio Dragon-produced Netflix Original *Love Alarm*, an app "rings" every time someone within a 10 meter radius "loves" you.)
- Market expectations for 2Q19 OP were lowered by 20% in the three-month period amid doubts about the company's ability to recover the hefty production cost of its newest release. But the stock seems to have fallen rather dramatically even considering this.
- The major detractor was the market's concern that the company would turn in a weak quarter driven by the poor performance of *Arthdal Chronicles*. Worries over the low viewership of the tent-pole series negatively affecting tvN's ad rates and Studio Dragon's production cost structure over the long haul also rattled investors.
- Studio Dragon is predicted to create 45 titles in 2023, up from this year's 31 titles (tent-pole productions, dramas for network TV, and Netflix Originals).
- *Arthdal Chronicles* is a big-budget project, but the company's earnings won't be significantly impacted by the performance of a single drama. Contrary to market concerns, the tent-pole drama broke even in its first season, even despite having booked the set production costs for all three seasons.
- Investors should not be too concerned about Studio Dragon's tent-pole dramas as they are produced only after contracts to air them on non-tvN platforms like Netflix are secured.
- The ratings for *Arthdal Chronicles* averaged 7%, beating tvN's total average of 5%. Its ad rates were also as high as those of *Mr. Sunshine* at W21mn. The ad rates for tvN's weekend dramas have risen 400% over the past five years led by a steady increase in viewership. Those of tvN's Monday-Tuesday dramas have skyrocketed (633%).
- While Studio Dragon continues to provide competitive content to tvN, which is helping to boost tvN's ad rates, the production house is relying increasingly less on tvN for revenue as it distributes more and more content overseas. Given this profit structure, investors won't need to worry about potential declines in ad rates and revenue even if a single drama performs poorly in terms of viewership.
- Over the next five years, revenue is forecast to expand 11% annually, with OP rising 28% annually, driven by the steady rise in the number of drama titles (26 in 2018 → 45 in 2023E) and a higher share of dramas distributed overseas (29% in 2018 → 52% in 2023E).

Operating results and major financial data (Wbn, W, %)

	2017A	2018A	2019F	2020F	2021F
Revenue	287	380	475	519	579
OP	33	40	49	74	95
Pretax profit	30	46	59	87	108
NP	24	36	43	65	80
NP (controlling int.)	24	36	43	65	80
EPS	1,050	1,278	1,534	2,300	2,851
PER	61.9	72.3	42.7	28.5	23.0
BPS	16,223	14,312	15,834	17,624	19,725
PBR	4.0	6.5	4.1	3.7	3.3
ROE	9.5	9.3	10.2	13.8	15.3

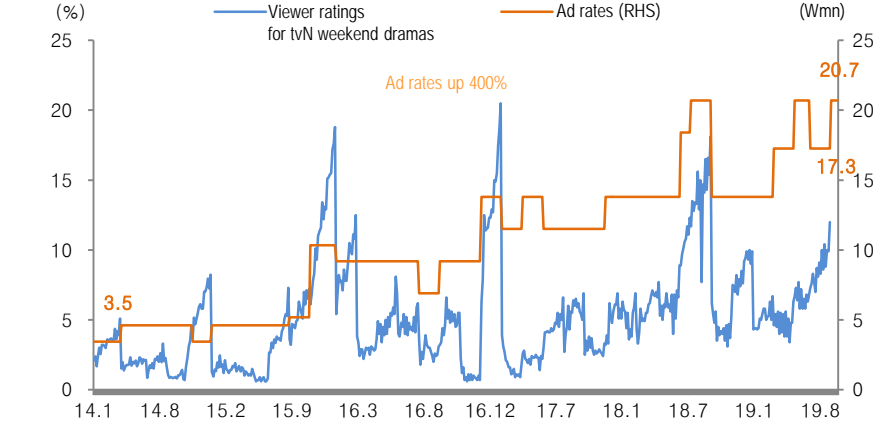
Note: EPS, BPS, and ROE are based only on the controlling interest.
Source: Studio Dragon, Daishin Securities Research Center

Fig 1. Recent share price fall seems excessive



Source: FnGuide, Daishin Securities Research Center

Fig 2. Viewer ratings and ad rates for tvN's weekend dramas are on a steady rise



Source: CJ E&M, AGB Nielsen, Daishin Securities Research Center

Fig 3. Viewer ratings and ad rates for tvN's Mon/Tue dramas are also on a steady rise

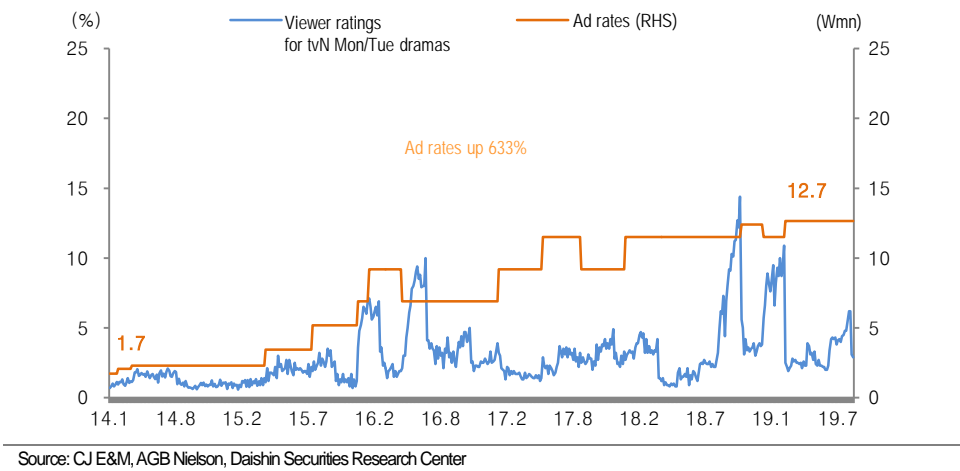


Fig 4. Revenue rising on increased drama production

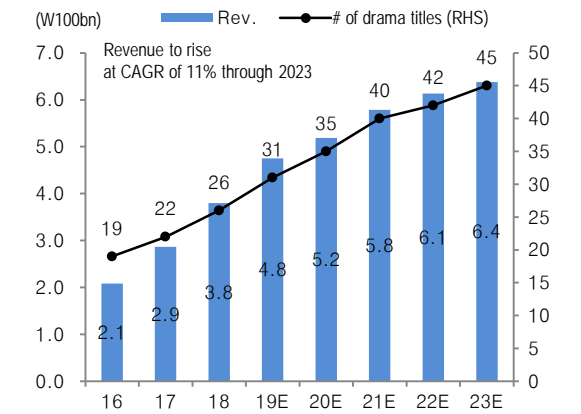


Fig 5. OP to rise 28% annually through 2023

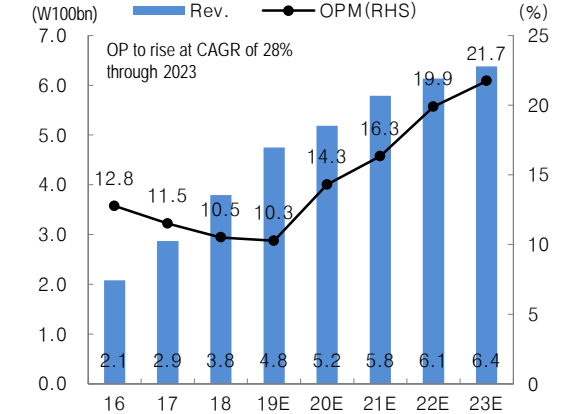


Fig 6. Rising overseas distribution holds key to revenue growth

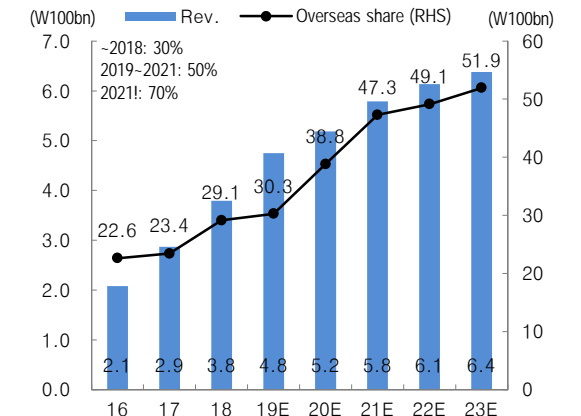
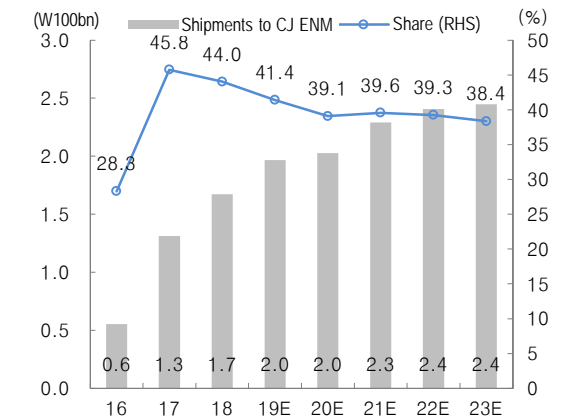


Fig 7. Growing on captive customers (tvN, OCN)



1. Company profile

Overview

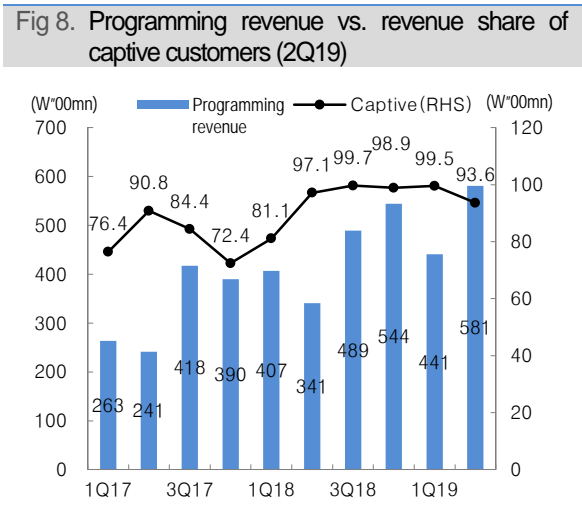
- Spun off from CJ E&M in May 2016
- Listed on the KOSDAQ in Nov 2017
- Revenue ₩379.6bn, OP ₩39.9bn, NP ₩35.8bn (2018)
- Revenue mix: programming 45%, distribution 47%, others 8% (2Q19)

Share price catalysts

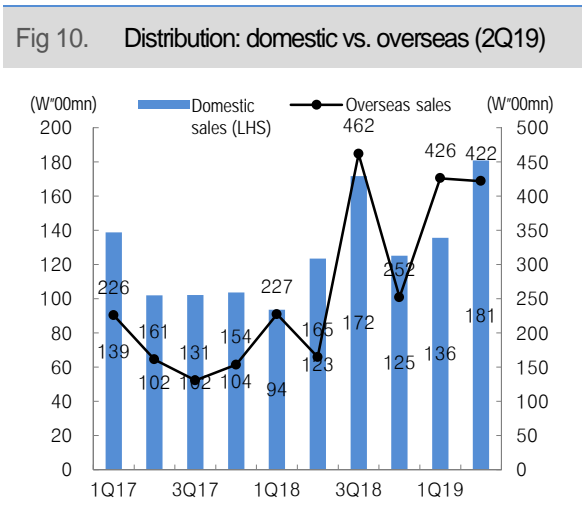
- Drama programming (tvN, OCN)
- Deals with Netflix
- Growing production of tent-pole dramas has led to market concerns over heavy production cost burden, hurting the share price.
- But the stock will rebound if earnings come in favorable owing to rising viewer ratings of major dramas.

Source: Studio Dragon, Daishin Securities Research Center

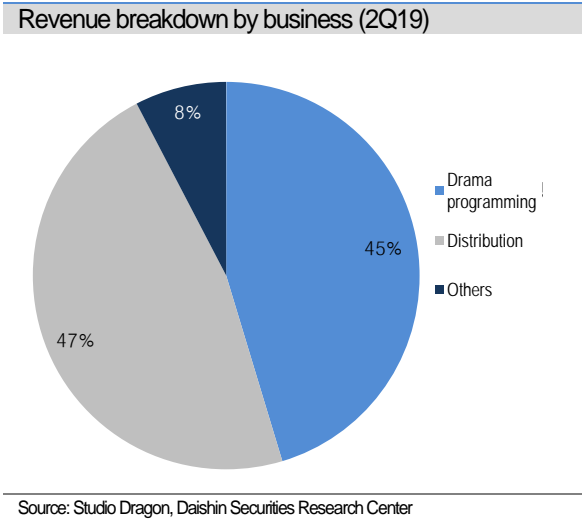
2. Earnings drivers



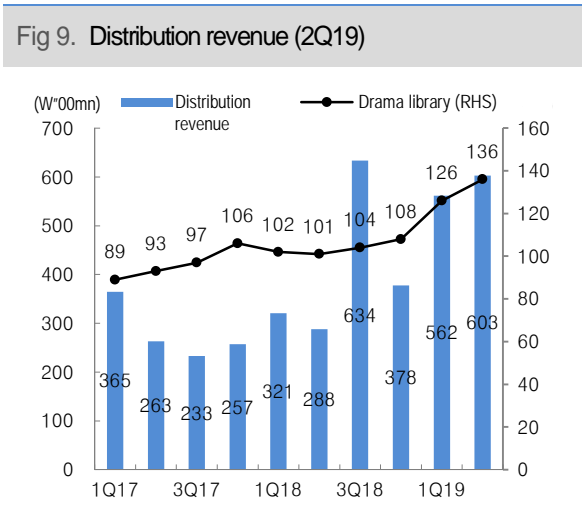
Source: Studio Dragon, Daishin Securities Research Center



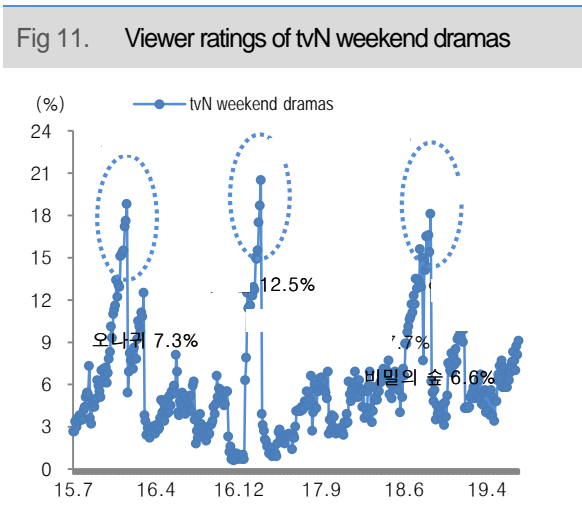
Source: Studio Dragon, Daishin Securities Research Center



Source: Studio Dragon, Daishin Securities Research Center



Source: Studio Dragon, Daishin Securities Research Center



Source: AGB Nielsen, Daishin Securities Research Center

Per share intrinsic value

Residual Income Model		(Wbn, W, %)									
		2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F	2027F	2028F
I	NP (contr. int.) ^(Note 2)	43	65	80	101	113	127	142	159	179	200
II	Shareholders' equity (contr. int.) ^(Note 2)	444	495	554	631	715	805	903	1,013	1,127	1,256
	Estimated ROE	10.2	13.8	15.3	16.0	15.9	15.8	15.8	15.7	15.8	15.9
III	Required rate of return ^(Note 3)	4.4									
	Risk free rate of return ^(Note 4)	1.6									
	Market risk premium ^(Note 5)	4.0									
	Beta	0.70									
IV	Spread (estimated ROE – required rate of return)	5.8	9.4	10.9	11.6	11.5	11.4	11.4	11.3	11.4	11.5
V	Required income	18	20	22	24	28	31	35	40	45	50
VI	Residual income (I - V)	25	45	58	76	86	96	107	120	134	150
	Present value factor	0.99	0.95	0.91	0.87	0.83	0.80	0.76	0.73	0.70	0.67
	PV of residual income	25	43	53	66	71	76	82	88	94	101
VII	Sum of residual income	699									
VIII	PV of residual income following forecasting period	2,294									
	Terminal growth (g) ^(Note 6)	0.0%									
IX	Beginning shareholders' equity	401									
X	Fair market cap (VII+VIII+IX)	3,394									
	Total number of shares (thousands)	28,051									
XI	Per share value (W)	120,843									
	Current share price (W)	65,500									
	Potential (%)	84.5%									

Note 1: Under the residual income model (RIM), we add the current shareholders' equity to the residual income based on the earnings forecast for the next ten years before adding the result to the residual income after the forecasting period to derive the value of shareholders' stakes. The RIM is considered less subjective than similar valuation models such as DDM, DCF, and EVA.

Note 2: The RIM reflects consolidated subsidiaries' earnings not in their entirety but only for the stake controlled by the company.

Note 3: The required rate of return (i.e., cost of equity) is the rate of return expected by the shareholders who take risks. It is derived by the capital asset price model: Cost of equity = Risk-free interest rate + Beta * Market risk premium.

Note 4: The yield on five-year government bonds was used as the proxy for the risk-free interest rate.

Note 5: Market risk premium refers to the gap between the expected return on the market portfolio and the risk-free interest rate. It has been lowered from 6-8% to 3-5% in reflection of the current low-growth environment.

Note 6: The terminal growth was assumed to be zero.

Financial statements

Income statement					(Wbn)
	2017A	2018A	2019F	2020F	2021F
Revenue	287	380	475	519	579
Cost of goods sold	240	324	412	432	471
Gross profit	47	56	63	87	109
SG&A expenses	14	16	14	12	14
OP	33	40	49	74	95
OP margin	11.5	10.5	10.3	14.3	16.3
EBITDA	74	115	151	177	207
Non-OP	-3	6	10	13	14
Income from affiliates	0	0	0	0	0
Financial revenue	1	7	13	13	14
FX related gains	0	0	0	0	0
Financial expense	-3	-1	-4	-1	-1
FX related losses	1	0	0	0	0
Others	0	0	0	1	1
Income before taxes	30	46	59	87	108
Income tax expense	-6	-10	-16	-23	-28
Income from cont. op.	24	36	43	65	80
Income from discount. op.	0	0	0	0	0
NP	24	36	43	65	80
NP margin	8.3	9.4	9.1	12.5	13.8
NP for non-contr. interest	0	0	0	0	0
NP for contr. interest	24	36	43	65	80
Valuation of AFS fin. assets	0	0	0	0	0
Other compreh. income	0	-1	-1	-1	-1
Comprehensive income	24	35	42	63	79
Comp. income for non-contr. int.	0	0	0	0	0
Comp. income for contr. int.	24	35	42	63	79

Valuation metrics					(W, x, %)
	2017A	2018A	2019F	2020F	2021F
EPS	1,050	1,278	1,534	2,300	2,851
PER	61.9	72.3	42.7	28.5	23.0
BPS	16,223	14,312	15,834	17,624	19,725
PBR	4.0	6.5	4.1	3.7	3.3
EBITDAPS	3,271	4,108	5,387	6,318	7,357
EV/EBITDA	22.1	21.1	11.0	9.1	7.6
SPS	12,628	13,539	16,932	18,467	20,618
PSR	5.1	6.8	3.7	3.4	3.1
CFPS	3,068	3,930	5,373	6,429	7,467
DPS	0	0	500	750	850

Financial ratios					(W, x, %)
	2017A	2018A	2019F	2020F	2021F
Growth potential					
Sales growth	85.7	32.4	25.2	9.1	11.6
OP growth	98.3	21.0	22.1	52.3	27.5
NP growth	192.9	50.3	20.1	50.1	23.9
Profitability					
ROIC	17.0	16.0	15.6	22.8	27.5
ROA	9.4	8.2	9.1	12.6	14.7
ROE	9.5	9.3	10.2	13.8	15.3
Stability					
Debt ratio	24.7	27.7	26.1	23.9	21.9
Net borrowings ratio	-49.5	-39.3	-40.9	-45.6	-47.8
Interest coverage ratio	19.0	343.0	0.0	0.0	0.0

Source: Studio Dragon, Daishin Securities Research Center

Balance sheet					(Wbn)
	2017A	2018A	2019F	2020F	2021F
Current assets	290	247	289	341	391
Cash & cash equiv.	51	153	177	221	260
Trade & other receive.	55	69	86	94	105
Inventories	1	1	1	1	1
Other current assets	182	25	25	25	25
Long-term assets	170	265	271	272	285
Tangible assets	1	1	1	1	1
Investments in affiliates	0	0	0	0	0
Other long-term assets	169	264	270	271	284
Total assets	459	512	560	613	675
Current liabilities	91	108	113	115	118
Payables & other liab.	34	60	65	67	70
Borrowings	0	0	0	0	0
Current portion of LT debts	10	0	0	0	0
Other current liabilities	47	48	48	48	48
Long-term liabilities	0	3	3	3	3
Borrowings	0	0	0	0	0
Convertible securities	0	0	0	0	0
Other long-term liab.	0	3	3	3	3
Total liabilities	91	111	116	118	121
Controlling interest	368	401	444	495	554
Capital stock	14	14	14	14	14
Capital surplus	320	320	320	320	320
Retained earnings	32	68	111	161	220
Other capital changes	3	0	0	0	0
Non-controlling interest	0	0	0	0	0
Total shareholder's equity	368	401	444	495	554
Net borrowings	-183	-158	-182	-226	-265

Cash flow statement					(Wbn)
	2017A	2018A	2019F	2020F	2021F
Operating cash flows	-7	-29	-2	27	49
NP	0	0	43	65	80
Non-cash items	46	74	108	116	130
Depreciation	41	75	102	103	112
FX gains	1	-1	0	0	0
Equity method gain	0	0	0	0	0
Others	4	0	5	13	18
Chg in assets & liab.	-73	-139	-151	-144	-146
Other cash flows	20	36	-2	-10	-15
Investing cash flow	-141	141	-106	-101	-121
Investment assets	-141	138	0	0	0
Tangible assets	0	0	0	0	0
Others	0	3	-105	-101	-121
Financing cash flows	188	-10	0	-14	-21
Short-term borrowings	-8	0	0	0	0
Bonds payable	10	0	0	0	0
Long-term borrowings	0	0	0	0	0
Rights offering	208	0	0	0	0
Cash dividends	0	0	0	-14	-21
Others	-22	-10	0	0	0
Net chg in cash	40	102	24	44	39
Beginning cash balance	12	51	153	177	221
Ending cash balance	51	153	177	221	260
NOPLAT	26	31	36	55	70
FCF	67	106	30	54	58

[Daishin House View: Industry 4.0 safety rating]

- Daishin Securities assigns safety ratings to individual sectors and companies based on analyses and discussions by our analysts.
- Depending on whether Industry 4.0 will have a positive, neutral, or negative impact, each industry and company is assigned one of three safety ratings:

Dark Gray (negative)	Neutral Green (neutral)	Sky Blue (positive)
----------------------	-------------------------	---------------------

[Compliance Notice]

In accordance with Subparagraph 5 of Paragraph 1 of Article 4-20 of the supervisory regulations for the financial investment industry, we confirm that no information or content has been shared prior to its release on Daishin's website, and that the analyst has not received nor will receive direct or indirect compensation in exchange for expressing specific opinions. Daishin is not affiliated with the company presented in this report. This report has been presented without any undue external influence or interference, and accurately reflects the personal views of the analyst who is responsible for its content.

This report is distributed for the purpose of helping investors make informed decisions. This report has been prepared from the data and information believed to be correct and reliable, but Daishin Securities does not make any guarantee as to the accuracy thereof. Investors reading this report should make final decisions based on their own judgment.

For U.S. persons only: For U.S. persons only: This independent third party research report is a product of Daishin Securities, which is the employer of the research analyst(s) who has prepared the research report. The research analyst(s) preparing the research report is/are resident outside the United States (U.S.) and are not associated persons of any U.S. regulated broker-dealer and therefore the analyst(s) is/are not subject to supervision by a U.S. broker-dealer, and is/are not required to satisfy the regulatory licensing requirements of FINRA or required to otherwise comply with U.S. rules or regulations regarding, among other things, communications with a subject company, public appearances and trading securities held by a research analyst account.

This independent third-party research report is distributed in the United States ("US") to Major US Institutional Investors (as defined in Rule 15a-6 under the Securities and Exchange Act of 1934, as amended) by Maybank Kim Eng Securities USA Inc. ("Maybank KESUSA") and Auerbach Grayson and Company LLC, broker-dealers registered in the US (registered under Section 15 of the Securities Exchange Act of 1934, as amended). All responsibility for the distribution of this report by Maybank KESUSA in the US shall be borne by Maybank KESUSA. All responsibility for the distribution of this report by Auerbach Grayson and Company LLC shall be borne by Auerbach Grayson and Company LLC.

If the recipient of this report is not a Major Institutional Investor as specified above, then it should not act upon this report and return the same to the sender. Further, this report may not be copied, duplicated and/or transmitted onward to any U.S. person, which is not the Major Institutional Investor. In reliance on the exemption from registration provided by Rule 15a-6 of the Exchange Act and interpretations thereof by the SEC in order to conduct certain business with Major Institutional Investors, Daishin Securities has entered into an agreement with two U.S. registered broker-dealers, Maybank Kim Eng Securities USA Inc and Auerbach Grayson and Company LLC. All U.S. persons receiving and/or accessing this report and wishing to effect transactions in any security mentioned within must do so with: Maybank Kim Eng Securities USA Inc. 777 Third Avenue 21st Floor New York, New York 1- (212) 688-8886 or Auerbach Grayson and Company LLC 25 West 45th Street, New York, NY 10036 and not with the issuer of this report.

Analyst Certification of Independence

The views expressed in this research report accurately reflect the analyst's personal views about any and all of the subject securities or issuers; and no part of the research analyst's compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

[Investment rating & Target price history]

Studio Dragon (253450 KQ)

Date	19.09.04	19.05.07	18.11.07	18.08.08	18.04.29	18.01.28
Rating	BUY	6M passed.	BUY	MKTPERF.	MKTPERF.	MKTPERF.
Target price	115,000	115,000	115,000	95,000	81,000	74,000
Diff. (avr. %)		(40.63)	(17.43)	10.95	26.80	19.40
Diff. (max/min, %)		(21.39)	(0.78)	22.42	(1.73)	(3.51)

Date	17.11.25
Rating	BUY
Target price	46,000
Diff. (avr. %)	44.64
Diff. (max/min, %)	25.65

Date	
Rating	
Target price	
Diff. (avr. %)	
Diff. (max/min, %)	

Date	
Rating	
Target price	
Diff. (avr. %)	
Diff. (max/min, %)	

Investment rating breakdown and framework (Sep 1, 2019)

	BUY	MARKETPERFORM	UNDERPERFORM
Ratio	89.2%	10.3%	0.0%

Sector ratings breakdown

- Overweight: industry indicators are expected to outperform the market over the next six months.
- Neutral: industry indicators are expected to be in line with the market over the next six months.
- Underweight: industry indicators are expected to underperform the market over the next six months.

Company ratings breakdown

- Buy: the stock is expected to outperform the market by at least 10%p over the next six months.
- Marketperform: the stock is expected to either outperform or underperform the market by less than 10%p over the next six months.
- Underperform: the stock is expected to underperform the market by at least 10%p over the next six months.