

Studio Dragon

(253450 KQ)

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Rating **BUY**
maintain

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

CP (W)
(20.03.19) **69,100**

Media

More tricks up its sleeve

Media top pick; 6M TP reiterated at W115,000

- Our W115,000 target price for the content company is based on a residual income model.

Building on the momentum in 2Q20

- Studio Dragon is poised to report revenue of W120.0bn (up 21% qoq; up 5.4% yoy) and OP of W11.2bn (vs. a loss in 3Q19; up 1.4% yoy) for 1Q20, reflecting the solid viewership numbers of its latest drama titles – *Crash Landing on You*, *Hi Bye Mama*, and *Hospital Playlist* – released both on cable and Netflix and expectations for its new Netflix original production *My Holo Love* that debuted this quarter.
- Its dramas are likely to be aired a total of 113 times in 1Q20, down from the average of 133 from 1Q19 to 3Q19. Profit, however, will likely remain nearly unchanged thanks to higher margins from original and non-original shows for Netflix.
- The outlook is even brighter for 2Q20, given the growing demand for streaming as people spend more time indoors amid the virus outbreak.
- In the coming quarter, Studio Dragon is set to release a new drama series, *The King: Eternal Monarch*, written by Kim Eun-suk who is behind hit dramas such as *Goblin* (2017; 20.5% rating) and *Mr. Sunshine* (2018; 18.1%). Margins on the show will easily top 30%, in our view, considering the streaming deal with Netflix and ad contracts (both product placements and sponsorship).
- Shares in the company will likely far outperform the market, driven in large part by more content deals with higher margins and a regulatory ban on short selling.

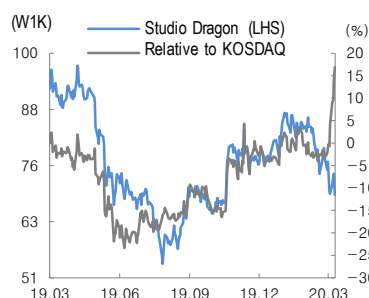
More and better deals from Netflix to add to underlying profit health

- Studio Dragon enjoyed a steady profit stream last year, delivering a quarterly average of W11bn through 3Q19. (Profit fell to negative territory (W4bn) in 4Q19, however, on higher fixed costs resulting from a thinner drama slate.)
- It is set to pad its bottom line further this year, backed by a stronger drama lineup (35, up 5 from 2019, including three Netflix originals), more lucrative Netflix deals (margins on originals to rise 10%p to 25), and four big-budget dramas* (one in each quarter).
- * Tentpole dramas cost more than W200bn to produce but carry margins two times as high as smaller-budget shows. (Hopefully, we won't see another *Arthdal Chronicles*, a W50bn buster that barely turned a profit.)
- In all, we expect OP to leap 154% to W73bn this year.

Industry 4.0 safety rating ■ Sky Blue

KOSDAQ	428.35
Market cap (Wbn)	1,941
Market cap portion (%)	0.83
Paid-in capital (common; Wbn)	14
52w high/low (W)	97,300 / 54,000
120d avg. trading volume (Wbn)	11.3
Foreign ownership (%)	8.54
Major shareholders	CJ E&M+5: 69.33%

(%)	1M	3M	6M	12M
Abs. return	-17.3	-10.1	-1.4	-25.5
Rel. return	32.1	35.9	48.6	30.3



(Wbn, %)

	1Q19	4Q19	1Q20(F)					2Q20		
			Previous estimate	Daishin estimate	YoY	QoQ	Consensus	YoY	QoQ	
Revenue	112	97	159	118	5.4	21.0	124	153	19.1	29.5
OP	11	-4	11	11	1.4	TTB	12	19	75.1	68.9
NP	9	-2	11	9	-0.3	TTB	10	15	102.8	62.1

	2018	2019	2020(F)				Growth	
			Previous estimate	Daishin estimate	Change	Consensus	2019	2020(F)
Revenue	380	469	590	539	-8.6	578	23.4	15.1
OP	40	29	75	73	-3.4	62	-28.0	153.7
NP	36	26	65	58	-12.1	52	-26.4	118.2

Source: Studio Dragon, FnGuide Daishin Securities Research Center

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

	2018A	2019A	2020F	2021F	2022F
Revenue	380	469	539	596	638
OP	40	29	73	93	116
Pretax profit	46	33	78	98	121
NP	36	26	58	72	89
NP (controlling int.)	36	26	58	72	89
EPS	1,278	940	2,048	2,580	3,175
PER	72.3	86.1	33.7	26.8	21.8
BPS	14,312	15,238	16,770	18,600	20,926
PBR	6.5	5.3	4.1	3.7	3.3
ROE	9.3	6.4	12.8	14.6	16.1

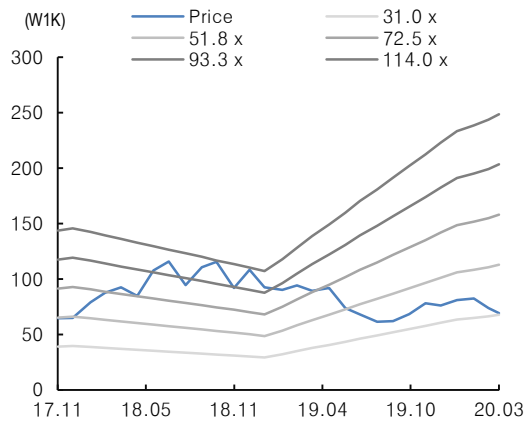
Note: EPS, BPS, and ROE are based only on the controlling interest
Source: Studio Dragon, Daishin Securities Research Center

Earnings forecast revision (Wbn, W, %, %p)

	Previous		Revised		Change	
	2020F	2021F	2020F	2021F	2020F	2021F
Revenue	590	639	539	596	-8.6	-6.7
SG&A expense	12	14	12	14	0.3	-0.9
OP	75	98	73	93	-3.4	-5.1
OP margin	12.8	15.3	13.5	15.6	0.7	0.3
Non-OP profit	13	14	5	5	-62.6	-61.0
Pretax profit	89	111	78	98	-12.1	-11.9
NP (cont. int.)	65	82	58	72	-12.1	-11.9
NP margin	11.1	12.9	10.7	12.2	-0.4	-0.7
EPS (contr. int.)	2,331	2,929	2,048	2,580	-12.1	-11.9

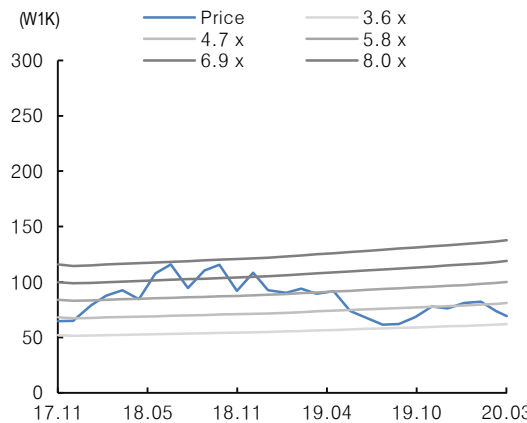
Source: Studio Dragon, Daishin Securities Research Center

Fig 1. 12-month forward P/E band



Source: Valuewise, Daishin Securities Research Center

Fig 2. 12-month forward P/B band



Source: Valuewise, Daishin Securities Research Center

Company profile

Overview

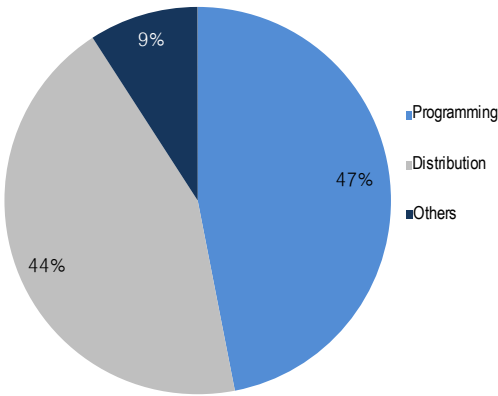
- Spun off from CJ E&M in May 2016
- Listed on the KOSDAQ in Nov 2017
- Revenue W468.6bn, OP W28.87bn, NP W26.5bn (2019)

Share price catalysts

- Earnings are rising steadily on increased drama supply to CJ ENM's channels tvN and OCN as well as Netflix.
- But the stock will likely rebound if earnings come in favorable owing to rising viewer ratings of major dramas.

Source: Studio Dragon, Daishin Securities Research Center

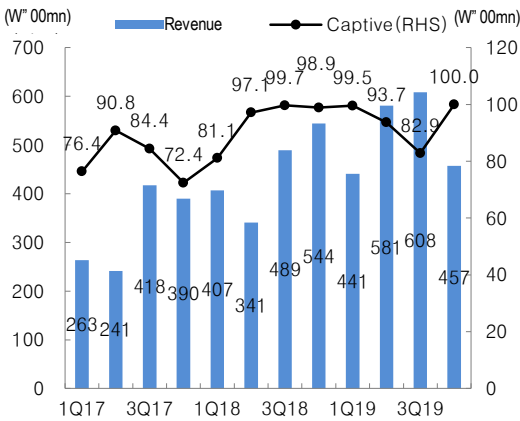
Revenue breakdown by business (4Q19)



Source: Studio Dragon, Daishin Securities Research Center

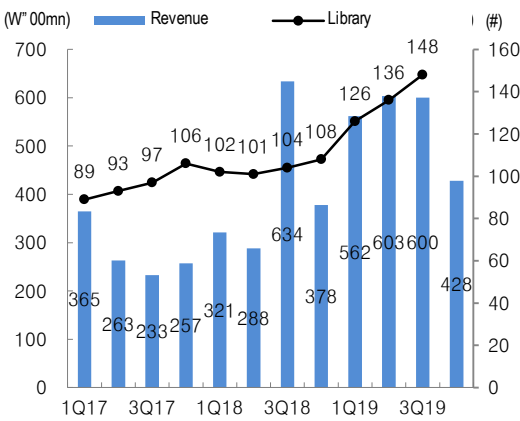
Earnings drivers

Fig 1. Programming revenue



Source: Studio Dragon, Daishin Securities Research Center

Fig 2. Distribution revenue



Source: Studio Dragon, 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)	26	58	72	89	110	121	133	146	161	177
II	Shareholders' equity (contr. int.) ^(Note 2)	428	471	523	588	668	753	844	943	1,046	1,159
	Estimated ROE	6.4	12.8	14.6	15.2	16.5	16.1	15.8	15.5	15.4	15.3
III	Required rate of return ^(Note 3)	4.2									
	Risk free rate of return ^(Note 4)	1.4									
	Market risk premium ^(Note 5)	4.0									
	Beta	0.70									
IV	Spread (estimated ROE – required rate of return)	2.2	8.6	10.4	11.0	12.3	11.9	11.6	11.3	11.2	11.1
V	Required income	17	18	20	22	25	28	32	35	40	44
VI	Residual income (I - V)	10	40	53	67	85	93	101	111	121	133
	Present value factor	1.00	0.96	0.92	0.88	0.85	0.81	0.78	0.75	0.72	0.69
	PV of residual income	10	38	49	59	72	76	79	83	87	92
VII	Sum of residual income	645									
VIII	PV of residual income following forecasting period	2,190									
	Terminal growth (g) ^(Note 6)	0.0%									
IX	Beginning shareholders' equity	401									
X	Fair market cap (VII+VIII+IX)	3,237									
	Total number of shares (thousands)	28,326									
XI	Per share value (W)	115,200									
	Current share price (W)	69.100									
	Potential (%)	66.7%									

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)				
	2018A	2019A	2020F	2021F	2022F	
Revenue	380	469	539	596	638	
Cost of goods sold	324	421	454	490	507	
Gross profit	56	48	85	106	131	
SG&A expenses	16	19	12	14	15	
OP	40	29	73	93	116	
OP margin	10.5	6.1	13.5	15.6	18.1	
EBITDA	115	131	176	205	239	
Non-OP	6	4	5	5	5	
Income from affiliates	0	0	0	0	0	
Financial revenue	7	10	13	13	13	
FX related gains	0	0	0	0	0	
Financial expense	-1	-6	-9	-9	-9	
FX related losses	0	0	0	0	0	
Others	0	0	1	1	1	
Income before taxes	46	33	78	98	121	
Income tax expense	-10	-7	-20	-25	-31	
Income from cont. op.	36	26	58	72	89	
Income from discount op.	0	0	0	0	0	
NP	36	26	58	72	89	
NP margin	9.4	5.6	10.7	12.2	14.0	
NP for non-contr. interest	0	0	0	0	0	
NP for contr. interest	36	26	58	72	89	
Valuation of AFS fin. assets	0	0	0	0	0	
Other compreh. income	-1	-1	-1	-1	-1	
Comprehensive income	35	25	56	71	88	
Comp. income for non-contr. Int.	0	0	0	0	0	
Comp. income for contr. int.	35	25	56	71	88	

Valuation metrics		(W, x, %)				
	2018A	2019A	2020F	2021F	2022F	
EPS	1,278	940	2,048	2,580	3,175	
PER	72.3	86.1	33.7	26.8	21.8	
BPS	14,312	15,238	16,770	18,600	20,926	
PBR	6.5	5.3	4.1	3.7	3.3	
EBITDAPS	4,108	4,674	6,267	7,285	8,497	
EV/EBITDA	21.1	16.1	9.9	8.4	7.0	
SPS	13,539	16,696	19,200	21,217	22,715	
PSR	6.8	4.8	3.6	3.3	3.0	
CFPS	3,930	4,564	6,104	7,118	8,315	
DPS	0	500	750	850	1,050	

Financial ratios		(W, x, %)				
	2018A	2019A	2020F	2021F	2022F	
Growth potential						
Sales growth	32.4	23.4	15.1	10.5	7.1	
OP growth	21.0	-28.0	153.7	27.2	24.7	
NP growth	50.3	-26.4	118.2	26.0	23.1	
Profitability						
ROIC	16.0	10.1	22.3	26.7	30.8	
ROA	8.2	5.4	12.9	15.0	17.0	
ROE	9.3	6.4	12.8	14.6	16.1	
Stability						
Debt ratio	27.7	27.0	25.3	23.4	21.2	
Net borrowings ratio	-39.3	-38.8	-42.3	-44.2	-46.8	
Interest coverage ratio	343.0	0.0	0.0	0.0	0.0	

Source: Studio Dragon, Daishin Securities Research Center

Balance sheet		(Wbn)				
	2018A	2019A	2020F	2021F	2022F	
Current assets	247	272	318	360	412	
Cash & cash equiv.	153	162	195	226	271	
Trade & other receive.	69	85	98	108	116	
Inventories	1	1	1	1	1	
Other current assets	25	25	25	25	25	
Long-term assets	265	271	272	285	300	
Tangible assets	1	1	1	1	1	
Investments in affiliates	0	0	0	0	0	
Other long-term assets	264	270	271	284	299	
Total assets	512	543	591	645	712	
Current liabilities	108	113	116	119	122	
Payables & other liab.	60	64	68	71	73	
Borrowings	0	0	0	0	0	
Current portion of LT debts	0	0	0	0	0	
Other current liabilities	48	48	48	48	48	
Long-term liabilities	3	3	3	3	3	
Borrowings	0	0	0	0	0	
Convertible securities	0	0	0	0	0	
Other long-term liab.	3	3	3	3	3	
Total liabilities	111	116	119	122	124	
Controlling interest	401	428	471	523	588	
Capital stock	14	14	14	14	14	
Capital surplus	320	320	320	320	320	
Retained earnings	68	94	138	189	254	
Other capital changes	0	0	0	0	0	
Non-controlling interest	0	0	0	0	0	
Total shareholder's equity	401	428	471	523	588	
Net borrowings	-158	-166	-199	-231	-275	

Cash flow statement		(Wbn)				
	2018A	2019A	2020F	2021F	2022F	
Operating cash flows	-29	-18	16	42	71	
NP	0	26	58	72	89	
Non-cash items	74	102	114	127	144	
Depreciation	75	102	103	112	123	
FX gains	-1	0	0	0	0	
Equity method gain	0	0	0	0	0	
Others	0	-1	11	16	21	
Chg in assets & liab.	-139	-150	-148	-146	-144	
Other cash flows	36	4	-8	-13	-18	
Investing cash flow	141	-106	-101	-121	-136	
Investment assets	138	0	0	0	0	
Tangible assets	0	0	0	0	0	
Others	3	-105	-101	-121	-135	
Financing cash flows	-10	0	-14	-21	-24	
Short-term borrowings	0	0	0	0	0	
Bonds payable	0	0	0	0	0	
Long-term borrowings	0	0	0	0	0	
Rights offering	0	0	0	0	0	
Cash dividends	0	0	-14	-21	-24	
Others	-10	0	0	0	0	
Net chg in cash	102	9	33	32	44	
Beginning cash balance	51	153	162	195	226	
Ending cash balance	153	162	195	226	271	
NOPLAT	31	23	54	69	86	
FCF	106	17	53	56	70	

[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)
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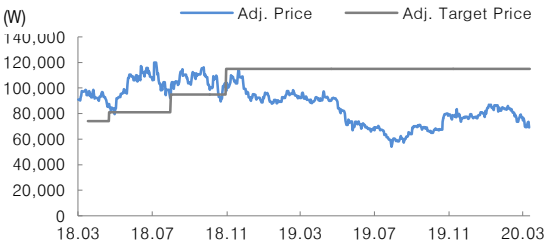
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[Investment rating & Target price history]

Studio Dragon (253450 KQ)



Date	20.03.20	19.11.07	19.05.07	18.11.07	18.08.08	18.04.29
Rating	Buy	GM passed	GM passed	Buy	Marketperform	Marketperform
Target price	115,000	115,000	115,000	115,000	95,000	81,000
Diff. (avr. %)		(30.96)	(40.20)	(17.43)	10.95	26.80
Diff. (max/min., %)		(24.35)	(21.39)	(0.78)	22.42	(1.73)
Date	18.03.25					
Rating	Marketperform					
Target price	74,000					
Diff. (avr. %)	25.72					
Diff. (max/min., %)	15.27					
Date						
Rating						
Target price						
Diff. (avr. %)						
Diff. (max/min., %)						
Date						
Rating						
Target price						
Diff. (avr. %)						
Diff. (max/min., %)						

Investment rating breakdown and framework (Mar. 17, 2020)

	BUY	MARKETPERFORM	UNDERPERFORM
Ratio	86.3%	13.7%	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