

Studio Dragon

(253450 KQ)

OP margin jumps 7%p on China effects

Buy
(Maintain)

TP: W107,000
Upside: 33.3%

Mirae Asset Daewoo Co., Ltd.

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3Q20 review: A positive surprise

Revenue of W106.3bn (-19.0% YoY) and stronger-than-expected OP of W16bn (+46.8% YoY)

- Despite a decline in programming due to captive channels' production cost cuts, Studio Dragon's 3Q20 margins improved on the back of the increasing value of its library.
- OP margin gained 6.8%p YoY to 15.1% on lower production/amortization expenses and the recognition of licensing sales to China (which carry zero expenses).
- Programming: Revenue contracted 24.8% YoY to W45.7bn, hurt by a decline in the number of produced titles and an unfavorable comparison (due to a big-budget title in 3Q19).
- Licensing: Revenue related to the licensing of two older titles to China was partially recognized, and ASP of OTT-bound content gained 25% for new titles and 60% for old titles.
- Costs: Amortization expenses fell to more normalized levels thanks to the preemptive amortization of big-budget titles in 2H19-1H20.
- Content performance indicators (e.g., Netflix [NFLX US/CP: US\$513.76] rankings) were impressive. We believe this will help spur further demand for the company's content.

A preview of 2021

1) China revenue, 2) ASP gains, and 3) amortization normalization to continue in 2021

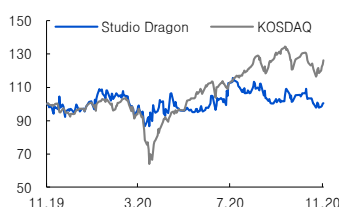
- Chinese OTTs are starting to pursue licensing rights as they prepare for expansion beyond mainland China to Southeast Asia.
- Some of these licensing sales require advance payments regardless of whether the titles are aired. The recognition of licensing sales to China is beginning to take place.
- Walt Disney (DIS US/CP: US\$126.96) and AT&T (T US/CP: US\$27.51) are looking to catch up in the OTT space by expanding their content libraries and geographical coverage. Latecomers' strong will to spend should fuel competition for quality content (price and volume).
- Production/amortization expenses should normalize partly thanks to preemptive amortization of big-budget titles (*Arthdal Chronicles* and *The King: Eternal Monarch*) in 2H19-1H20.

Maintain Buy and TP of W107,000; a clear buying opportunity

Platform diversification → stronger negotiating power → multiple expansion

- The high OP margin in 3Q20 despite an unfavorable programming environment points to improvements in underlying profitability in 2021 and beyond.
- In December, *Sweet Home* and *True Beauty*—two highly anticipated titles targeting the global audience—will air on Netflix and tvN, respectively.
- We believe the 2021 operating profit consensus (which has been consistently lowered and now stands at W68bn) has a strong chance of being revised up, assuming: 1) a sharp increase in production capacity backed by a webtoon IP/platform/content partnership with NAVER (035420 KS/Buy/TP: W430,000 CP: W299,000); and 2) recognition of revenue from China.

Key data



Current price (11/5/20, W)	80,300	Market cap (Wbn)	2,259
OP (20F, Wbn)	59	Shares outstanding (mn)	30
Consensus OP (20F, Wbn)	53	Free float (%)	38.3
EPS growth (20F, x)	63.5	Foreign ownership (%)	9.5
P/E (20F, x)	52.2	Beta (12M)	0.36
Market P/E (20F, x)	16.2	52-week low (W)	69,100
KOSDAQ	844.80	52-week high (W)	92,500

Share performance

(%)	1M	6M	12M
Absolute	-4.7	4.7	0.8
Relative	-3.2	-20.5	-19.8

Earnings and valuation metrics

(Dec.)	2016	2017	2018	2019	2020F	2021F
Revenue (Wbn)	0	287	380	469	529	635
OP (Wbn)	0	33	40	29	59	80
OP margin (%)	-	11.5	10.5	6.2	11.2	12.6
NP (Wbn)	0	24	36	26	44	57
EPS (W)	0	1,050	1,278	941	1,540	1,899
ROE (%)	0.0	12.9	9.3	6.4	9.7	11.4
P/E (x)	-	61.9	72.3	85.9	52.2	42.3
P/B (x)	-	4.9	6.5	5.3	5.1	4.6
Div. yield (%)	-	0.0	0.0	0.0	0.0	0.0

Notes: Under consolidated K-IFRS; NP is attributable to owners of the parent

Source: Company data, Mirae Asset Daewoo Research estimates

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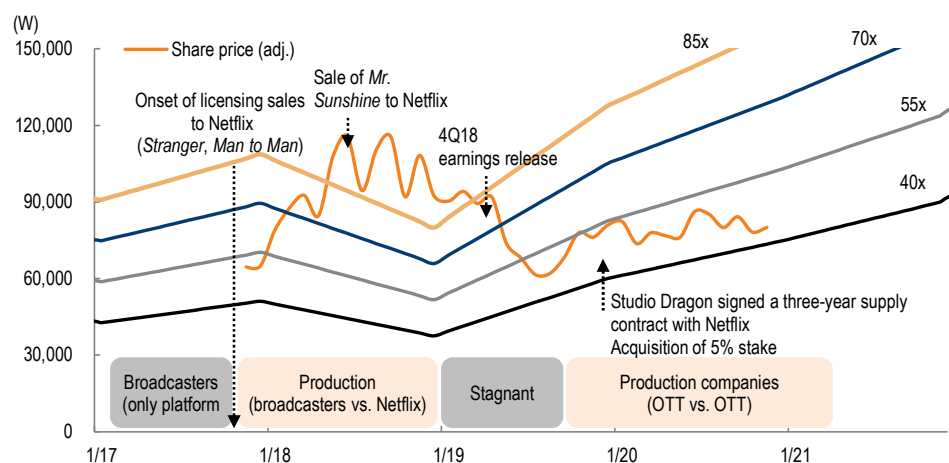
(Wbn, %)

	1Q19	2Q19	3Q19	4Q19	1Q20	2Q20	3Q20P	4Q20F	2019	2020F	2021F
Revenue	112	128	131	97	120	161	106	141	469	529	635
Programming	44	58	61	46	45	65	46	42	209	199	201
Licensing	56	60	60	43	67	76	51	87	219	280	382
Other	12	10	10	9	8	20	10	12	41	50	52
Costs	97	113	116	95	104	140	85	120	421	449	532
Production costs (incl. originals)	49	65	71	49	62	75	47	71	233	255	295
Commission fees	15	10	10	11	11	14	11	17	47	54	76
Depreciation/amortization (estimates)	27	32	28	28	26	45	19	22	115	113	127
Other	6	6	6	7	4	5	8	9	25	27	34
SG&A	4	5	4	6	5	5	5	7	19	22	23
EBITDA	38	43	40	24	38	63	35	37	145	173	208
OP	11	11	11	-4	11	17	16	14	29	59	80
OP margin	9.9	8.4	8.3	-4.2	9.5	10.5	15.1	9.9	6.1	11.2	12.7
Pretax profit	13	12	13	-5	12	17	15	15	33	59	75
NP	9	7	12	-2	8	13	11	11	26	44	57
Net margin	8.2	5.7	8.8	-1.7	7.0	8.3	10.0	7.9	5.6	8.3	9.0
YoY											
Revenue	40.0	72.5	6.0	-4.3	7.6	25.9	-19.0	44.6	23.4	12.9	20.2
Programming	8.4	70.5	24.4	-16.1	2.5	12.6	-24.8	-7.5	17.2	-4.9	1.3
Licensing	75.1	109.2	-5.4	13.3	19.1	25.5	-15.2	103.3	35.3	27.9	36.2
Other	63.1	-14.1	-9.0	-6.7	-29.2	107.1	-6.4	30.0	3.0	22.5	5.0
EBITDA	34.7	182.5	-11.5	-8.5	0.0	44.3	-10.8	52.4	26.4	19.0	20.1
OP	3.5	48.8	-49.3	TTR	4.1	56.8	46.7	TTB	-28.0	104.0	37.7
NP	16.1	-17.8	-33.1	TTR	-7.6	84.0	-8.5	TTB	-26.1	65.5	30.6
Major assumptions											
No. of titles aired	6.5	7.5	7.0	6.5	6.5	6.5	5.5	5.5	27.5	26.0	27.0
No. of titles licensed to Netflix	1.5	2.5	1.5	0.4	1.5	2.0	2.5	2.0	5.9	8.0	9.0

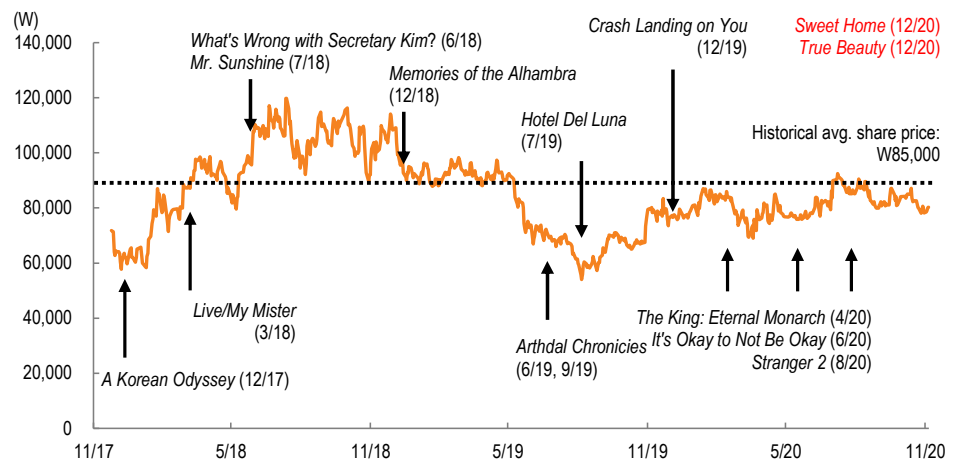
Note: Under consolidated K-IFRS

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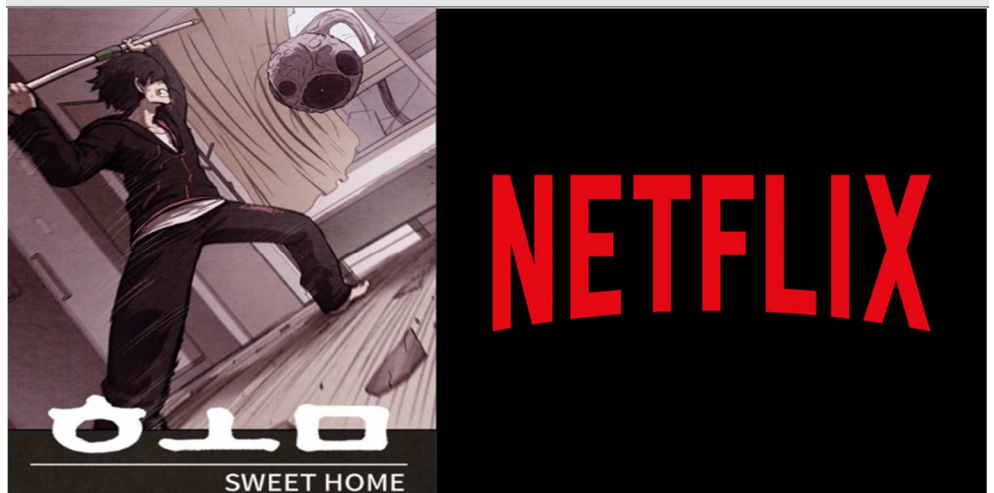
Figure 1. Studio Dragon: Stronger negotiating power in 2021 → P/E expansion



Source: WISEfn, Mirae Asset Daewoo Research

Figure 2. Shares are currently hovering around the historical avg. level

Source: WISEfn, Mirae Asset Daewoo Research

Figure 3. *Sweet Home* : To be released as a Netflix original in December; targeting global audiences

Source: Press materials, Mirae Asset Daewoo Research

Figure 4. *True Beauty*: To air on tvN in December; targeting global audiences

Source: tvN, Mirae Asset Daewoo Research

Studio Dragon (253450 KQ)

Income statement (summarized)

(Wbn)	2018	2019	2020F	2021F
Revenue	380	469	529	635
Cost of revenue	324	421	449	532
Gross profit	56	48	80	103
SG&A expenses	16	19	22	23
OP (adj.)	40	29	59	80
OP	40	29	59	80
Non-operating profit	6	4	0	-5
Net financial income	3	3	2	4
Net income from associates	0	0	0	0
Pretax profit	46	33	59	75
Income tax	10	7	15	18
Profit from continuing operations	36	26	44	57
Profit from discontinued operations	0	0	0	0
NP	36	26	44	57
Attributable to owners	36	26	44	57
Attributable to minority interests	0	0	0	0
Total comprehensive income	35	26	44	57
Attributable to owners	35	26	44	57
Attributable to minority interests	0	0	0	0
EBITDA	115	146	173	209
FCF	-29	-13	82	186
EBITDA margin (%)	30.3	31.1	32.7	32.9
OP margin (%)	10.5	6.2	11.2	12.6
Net margin (%)	9.5	5.5	8.3	9.0

Balance sheet (summarized)

(Wbn)	2018	2019	2020F	2021F
Current assets	247	244	368	594
Cash & equivalents	153	60	161	350
AR & other receivables	69	84	121	145
Inventory	1	0	0	0
Other current assets	24	100	86	99
Non-current assets	265	337	321	194
Investments in associates	0	0	0	0
PP&E	1	1	4	3
Intangible assets	199	233	179	51
Total assets	512	582	689	788
Current liabilities	108	145	210	252
AP & other payables	55	64	93	112
Short-term financial liabilities	0	2	3	3
Other current liabilities	53	79	114	137
Non-current liabilities	3	8	8	8
Long-term financial liabilities	2	8	7	7
Other non-current liabilities	1	0	1	1
Total liabilities	111	153	217	260
Equity attributable to owners	401	428	471	528
Capital stock	14	14	14	14
Capital surplus	320	322	322	322
Retained earnings	68	94	137	194
Minority interests	0	0	0	0
Shareholders' equity	401	428	471	528

Cash flow statement (summarized)

(Wbn)	2018	2019	2020F	2021F
Operating cash flow	-29	-12	85	186
NP	36	26	44	57
Non-cash income/expenses	84	124	129	142
Depreciation	0	2	2	1
Amortization	75	115	113	127
Other	9	7	14	14
Chg. in working capital	-139	-143	-73	4
Chg. in AR & other receivables	-27	-22	-42	-24
Chg. in inventory	0	1	0	0
Chg. in AP & other payables	26	9	11	5
Income tax	-10	-19	-15	-18
Cash flow from investing activities	141	-81	20	3
Chg. in PP&E	0	0	-4	0
Chg. in intangible assets	0	0	0	0
Chg. in financial assets	140	-42	38	-2
Other	1	-39	-14	5
Cash flow from financing activities	-10	0	-3	0
Chg. in financial liabilities	-8	8	0	1
Chg. in equity	1	2	0	0
Dividends	0	0	0	0
Other	-3	-10	-3	-1
Chg. in cash	102	-93	102	188
Beginning balance	51	153	60	161
Ending balance	153	60	161	350

Key valuation metrics/ratios

	2018	2019	2020F	2021F
P/E (x)	72.3	85.9	52.2	42.3
P/CF (x)	21.6	15.1	13.2	12.1
P/B (x)	6.5	5.3	5.1	4.6
EV/EBITDA (x)	21.1	15.0	12.1	9.1
EPS (W)	1,278	941	1,540	1,899
CFPS (W)	4,280	5,346	6,102	6,633
BPS (W)	14,305	15,242	15,706	17,605
DPS (W)	0	0	0	0
Dividend payout ratio (%)	0.0	0.0	0.0	0.0
Dividend yield (%)	0.0	0.0	0.0	0.0
Revenue growth (%)	32.4	23.4	12.8	20.0
EBITDA growth (%)	55.4	27.0	18.5	20.8
OP growth (%)	21.2	-27.5	103.4	35.6
EPS growth (%)	21.7	-26.4	63.7	23.3
AR turnover (x)	6.1	6.2	5.2	4.8
Inventory turnover (x)	405.4	1,620.7	0.0	0.0
AP turnover (x)	25.3	22.1	19.9	18.1
ROA (%)	7.4	4.8	6.9	7.7
ROE (%)	9.3	6.4	9.7	11.4
ROIC (%)	15.2	8.7	14.4	32.9
Debt-to-equity ratio (%)	27.7	35.8	46.1	49.2
Current ratio (%)	228.4	168.4	175.5	235.6
Net debt-to-equity ratio (%)	-39.2	-21.2	-36.6	-68.2
Interest coverage ratio (x)	343.0	58.1	59.4	78.5

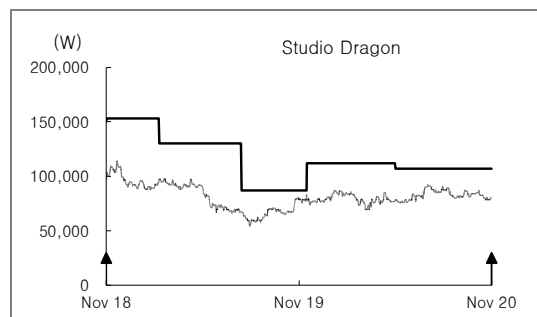
Source: Company data, Mirae Asset Daewoo Research estimates

Appendix 1

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Two-year rating and TP history

Company	Date	Rating	TP (₩)
Studio Dragon (253450)	05/08/20	Buy	107,000
	11/22/19	Buy	112,000
	07/21/19	Buy	87,000
	02/15/19	Buy	130,000
	11/08/18	Buy	153,000
	06/22/18	Buy	150,000



Stock ratings

Buy	Expected 12-month performance: +20% or greater
Trading Buy	Expected 12-month performance: +10% to +20%
Hold	Expected 12-month performance: -10% to +10%
Sell	Expected 12-month performance: -10% or worse

Sector ratings

Overweight	Expected to outperform the market over 12 months
Neutral	Expected to perform in line with the market over 12 months
Underweight	Expected to underperform the market over 12 months

Rating and TP history: Share price (—), TP (—), Not Rated (■), Buy (▲), Trading Buy (■), Hold (●), Sell (◆)

* Our investment rating is a guide to the expected return of the stock over the next 12 months.

* Outside of the official ratings of Mirae Asset Daewoo Co., Ltd., analysts may call trading opportunities should technical or short-term material developments arise.

* The TP was determined by the research analyst through valuation methods discussed in this report, in part based on estimates of future earnings.

* TP achievement may be impeded by risks related to the subject securities and companies, as well as general market and economic conditions.

Ratings distribution and investment banking services

	Buy	Trading Buy	Hold	Sell
Ratings distribution	73.62%	14.11%	11.04%	1.23%
Investment banking services	72.22%	11.11%	16.67%	0.00%

* Based on recommendations in the last 12 months (as of September 30, 2020)

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