

Studio Dragon (253450)

Improving Cash Flows

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Maintain BUY, target price of KRW93,000

We maintain BUY and our DCF-based TP of KRW93,000 on Studio Dragon. We see free cash flow turning positive from 2024 on the back of profitability gains and a faster recovery rate in accounts receivable. The stock, which is trading at 29.7x/21.5x 2023E/2024E P/E, deserves a valuation premium given strong demand, strengthened negotiating power and potential to sustain strong growth based on better cash flows.

Virtuous cycle of investment to raise OPM by 1.5pp YoY in 2024

Despite revenue growth, Studio Dragon has suffered negative cash flows due to weak OPM and a pileup of accounts receivable with long recovery periods. Contract renewals with major OTTs, which entail improved terms on pre-order/original content, should resolve these issues. However, original content produced last year and due for release in this year are not subject to the improved terms, thus only pre-order content should see margin improvement; full-fledged profitability gains should begin next year (11.1% 2024E OPM; +1.5pp YoY). Also, cash flow should improve, as recovery rates of accounts receivable should rise following contract renegotiation. Content demand should remain strong in the long term, so less financial burden stemming from better cash flow should lead to aggressive investments, supporting strong growth and reinvestment.

Expect better earnings in second half

We forecast 1Q23 revenue at KRW169.9bn (40.3% YoY, -10.8% QoQ) and OP at KRW19.0bn (4.8% YoY; 11.2% OPM), with OP missing the market consensus. No. of episodes for OTT and TV should rise 15 and 20, respectively, to 36 and 73, but sales from old titles should decline. In 2Q23, OP should decline YoY on reduced lineups and lower sales from old titles. Given the size of proactive investment and *The Big Door Prize* Season 2 production confirmed, earnings should beat market expectations in 2H23 and 2024.

Buy Maintain

Target Price (Maintain)	KRW93,000
Dividend yield*	0.0%
Total return	32.5%
Current price (Apr 17)	KRW70,200
Consensus target price	KRW102,154
Market capitalization	USD1.6bn

^{* 12-}month forward

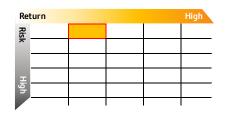
Trading Data										
Free float										
Avg. T/O val. (3m,	Avg. T/O val. (3m, KRWbn)									
Foreign ownership				10.5%						
Major shareholder	Major shareholders CJ ENM and 3 others									
	Naver			6.3%						
Stock Price Perfo	rmance (t	otal return	n)							
(%)	1M	3M	6M	12N						
Absolute	-2.0	-10.3	8.8	-25.						
Relative	-14.0	-30.0	-19.0	-24.						

Earnings Forecast & Valuation

Larrings rorccast & valuation				
Fiscal year-end	2022E	2023E	2024E	2025E
Revenue (KRWbn)	663	802	1,003	1,253
OP (KRWbn)	74	90	133	179
NP to control, int. (KRWbn)	61	74	111	150
EPS (KRW)	2,030	2,452	3,697	5,004
EPS growth (%)	56.0	20.8	50.8	35.4
P/E (x)	42.4	28.6	19.0	14.0
EV/EBITDA (x)	12.0	9.0	7.1	5.5
P/B (x)	3.8	2.8	2.4	2.1
ROE (%)	8.9	10.3	13.7	16.0
Div. yield (%)	0.0	0.0	0.0	0.0

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Risk & Total Return (annualized over three years)



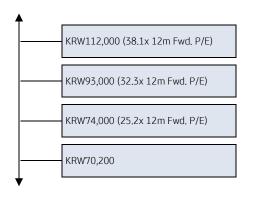
Stock Price & Relative Performance



Source(s): Company data, KB Securities

Investment Opinion & Risks





Base-case scenario: Catalysts

- 1) 2023E pre-order content at 170 titles
- 2) 2023E OTT-bound original content at 130

Bull-case scenario: Upside risks

- 1) 2023E pre-order content over 180 titles
- 2) 2023E OTT-bound original content over 140

Bear-case scenario: Downside risks

- 1) 2023E pre-order content under 150 titles
- 2) 2023E OTT-bound original content under 110

Revised Earnings Estimates

(KRWbn, %)	Previo	ous	Revise	ed	Change		
	2023E	2024E	2023E	2024E	2023E	2024E	
Revenue	802.0	1,003.0	866.9	1,045.5	8.1	4.2	
OP	90.0	133.0	83.1	116.4	-7.6	-12.5	
NP (to control. int.)	74.0	111.0	69.1	95.3	-6.6	-14.2	

Source(s): KB Securities estimates

KB Estimates vs. Consensus

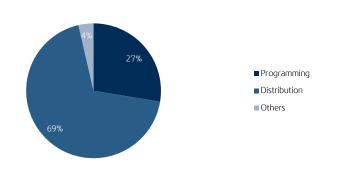
(KRWbn, %)	KB Estin	nates	Consen	sus	Difference		
	2023E	2024E	2023E	2024E	2023E	2024E	
Revenue	866.9	1,045.5	810.4	931.7	7.0	12.2	
OP	83.1	116.4	89.1	107.7	-6.7	8.1	
NP (to control. int.)	69.1	95.3	71.6	84.6	-3.5	12.5	

Source(s): Quantiwise, KB Securities estimates

Valuation & Target Price Calculation

- 1) Valuation method: Discounted cash flow model
- 2) Target price calculation: 8.63% WACC, 2% TGR
- 3) Target price range: KRW74,000 - KRW112,000
- 4) Valuation at target price: 32.3x 12m fwd P/E

Revenue Composition (2023E)



Earnings Sensitivity Analysis

(%)	EPS Change					
	2023E	2024E				
+1% in FX rate	+1.1	+1.1				
+1pp in interest rate	-0.6	0.1				

Source(s): Company data, KB Securities estimates

Peer Group Comparison

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(KRWtn, x, %)	Market	P/E	P/E P/B		EV/EBITDA		ROE		Dividend Yield		
	Cap.	2023E	2024E	2023E	2024E	2023E	2024E	2023E	2024E	2023E	2024E
Studio Dragon	2.1	29.4	24.5	2.76	2.49	9.1	8.3	9.8	10.7	0.0	0.0
CJ ENM	1.8	18.4	11.0	0.49	0.47	3.8	3.5	2.6	4.3	1.9	2.2
Netflix	198.1	29.1	22.6	6.09	4.87	21.3	17.2	21.8	22.0	0.0	0.0
Walt Disney	239.8	24.6	18.4	1.84	1.70	15.1	12.7	7.3	9.2	8.0	1.1

Source(s): Bloomberg consensus, KB Securities estimates

Table 1. Earnings Forecast

(KRWbn, %)	1Q22	2Q22	3Q22	4Q22	1Q23E	2Q23E	3Q23E	4Q23E	2021	2022	2023E	2024E
Revenue	121.1	157.5	228.9	190.5	169.9	173.2	260.1	263.7	487.1	697.9	866.9	1045.5
Programming	35.4	43.8	59.4	54.0	49.8	52.1	64.6	64.6	161.3	192.5	231.0	267.4
Distribution	77.7	103.9	165.8	132.8	116.3	117.2	191.5	195.0	275.5	480.2	620.0	760.3
Others	8.0	9.8	3.8	3.7	3.8	3.9	4.0	4.1	50.3	25.2	15.9	17.8
YoY %	3.4	48.5	97.2	28.8	40.3	10.0	13.6	38.4	-7.3	43.3	24.2	20.6
Programming	-19.1	<i>55.4</i>	64.0	1.5	40.7	19.0	8.8	19.7	-18.1	19.4	20.0	15.7
Distribution	23.0	53.8	<i>155.2</i>	66.4	49.6	12.8	15.5	46.8	-1.5	74.3	29.1	22.6
Others	-21.5	-5.1	-74.8	- <i>75.3</i>	-52.4	-60.1	6.6	12.6	2.6	-49.9	-37.0	12.6
QoQ %	-18.1	30.0	45.3	-16.8	-10.8	2.0	50.1	1.4				
Programming	-33.4	23.7	<i>35.5</i>	-9.1	-7. <i>7</i>	4.6	23.9	0.0				
Distribution	-2.6	33.7	59.5	-19.9	-12.4	0.8	63.3	1.8				
Others	-46.6	22.8	-61.4	-2.4	3.0	3.0	3.0	3.0				
OP	18.1	27.0	18.9	1.2	19.0	21.5	23.3	19.4	52.6	65.2	83.1	116.4
(YoY %)	1.4	95.7	29.9	-81.4	4.8	-20.2	22.9	1540.5	7.0	24.0	27.5	39.9
(QoQ %)	185.4	49.1	-29.9	- <i>93.8</i>	<i>1508.7</i>	13.5	8.0	-16.8				
OPM (%)	15.0	17.1	8.3	0.6	11.2	12.4	8.9	7.3	10.8	9.3	9.6	11.1
NP to control. int.	15.6	25.6	17.8	-8.5	16.2	19.3	23.5	10.1	39.0	50.6	69.1	95.3
(YoY %)	0.4	170.2	20.5	RR	3.8	-24.6	31.9	ТТВ	31.8	29.5	36.7	37.8
(QoQ %)	TTB	63.8	-30.3	TTR	TTB	19.0	22.0	-57.1				
NPM (%)	12.9	16.2	7.8	-4.4	9.5	11.1	9.0	3.8	8.0	7.2	8.0	9.1

Note: TTB=turn to black, TTR=turn to red, RR=remain in red

Source(s): Company data, KB Securities estimates

Table 2. Key Valuation Measures

(KRWbn, x, '000 shares, KRW)	2018	2019	2020	2021	2022	2023E	2024E
EV/sales	6.4x	4.6x	5.1x	5.5x	3.8x	2.6x	2.1x
Revenue	380	469	526	487	698	867	1,045
% YoY	32.4	23.5	12.2	(7.3)	43.3	24.2	20.6
EV/EBITDA	21,1x	14.9x	16.2x	17.6x	12.1x	7.5x	5.8x
EBITDA	115	146	165	152	219	294	376
% YoY	55.1	26.4	13.6	(8.3)	44.1	<i>34.7</i>	27.8
P/E	72.3x	85.9x	88.7x	69.9x	51.1x	30.5x	22,2x
EPS	1,278	941	1,044	1,301	1,684	2,299	3,169
% YoY	21.7	(26.3)	10.9	24.6	29.4	<i>36.5</i>	37.8
P/B	6.46x	5.31x	4.56x	3.99x	3.91x	2.89x	2.56x
BVPS	14,305	15,242	20,309	22,785	21,982	24,281	27,450
% YoY	8.9	6.5	33.2	12.2	(3.5)	10.5	13.1
Share price	92,400	80,900	92,600	91,000	86,000	70,200	70,200
No. of shares	28,038	28,068	28,369	30,008	30,020	30,058	30,058
Market cap.	2,592	2,273	2,778	2,731	2,585	2,110	2,110

Source(s): Company data, KB Securities estimates

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Table 3. Valuation: Discounted Cash Flow Model

(KRWbn, %, k shares, KRW)	2017	2018	2019	2020	2021	2022	2023E	2024E	2025E	2026E	2027E	2028E	Terminal
NOPLAT	26.6	30.1	22.1	37.2	39.6	57.2	65.9	92.5	127.1	175.1	238.0	319.9	
Operating profit	33.0	39.9	28.7	49.1	52.6	65.2	83.1	116.4	163.1	224.6	305.1	409.9	
Taxes	(6.4)	(9.8)	(6.6)	(11.9)	(13.0)	(8.1)	(17.3)	(23.8)	(36.0)	(49.5)	(67.2)	(90.0)	
D&A	41.3	75.3	116.8	116.2	99.1	153.3	211.1	259.6	298.3	332.2	363.7	394.3	
Depreciation	0.3	0.3	1.8	2.9	3.8	3.3	3.8	3.9	3.9	3.9	4.0	4.0	
Amortization	41.0	75.0	115.0	113.3	95.3	150.0	207.3	255.7	294.4	328.2	359.7	390.3	
(-)Change in working capital	(72.9)	(139.4)	(142.9)	(144.1)	(154.9)	(279.6)	(38.0)	26.6	(27.7)	(35.6)	(43.3)	(52.6)	
Decrease/increase in trade and other receivables	(13.7)	(27.2)	(21.8)	(31.4)	2.2	(35.2)	(42.4)	26.5	(32.1)	(41.0)	(49.9)	(60.6)	
Decrease/increase in inventories	(2.1)	0.3	0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Decrease/increase in other trade and payables	9.0	25.9	8.6	(11.5)	18.7	11.7	4.4	0.1	4.4	5.4	6.6	8.0	
Other	(66.1)	(138.4)	(130.2)	(101.2)	(175.8)	(256.0)	0.0	0.0	0.0	0.0	0.0	0.0	
(-) Tangible capital expenditures	(0.0)	(0.2)	(0.5)	(7.2)	(1.8)	(3.9)	(4.0)	(4.0)	(4.0)	(4.0)	(4.0)	(4.0)	
(-) Intangible capital expenditures	(0.2)	(0.1)	(0.3)	(1.2)	(8.0)	(2.5)	(282.6)	(339.2)	(362.9)	(388.3)	(415.5)	(444.6)	
(-) Other	(2.1)	5.0	(8.2)	(4.1)	7.9	6.2	3.2	2.7	16.9	23.0	30.7	40.3	
Free cash flow	(7.5)	(29.4)	(13.0)	(3.1)	(11.0)	(69.3)	(44.4)	38.3	47.6	102.4	169.6	253.2	3,898.2
(I/DIA/La Of Lashania I/DIA)	2015	2010	2010	2020	2021	2022	20275	20245	20255	20265	20255	20205	r:
(KRWbn, %, k shares, KRW)	2017	2018	2019	2020	2021	2022	2023E	2024E	2025E	2026E	2027E		Terminal
Operating cash flow	(7.2)	(29.1)	(12.2)	5.2	(8.4)	(62.9)	242.2	381.5	414.5	494.8	589.1	701.8	
(-) Tangible capital expenditures	(0.0)	(0.2)	(0.5)	(7.2)	(1.8)	(3.9)	(4.0)	(4.0)	(4.0)	(4.0)	(4.0)	(4.0)	
(-) Intangible capital expenditures	(0.2)	(0.1)	(0.3)	(1.2)	(8.0)	(2.5)	(282.6)	(339.2)	(362.9)	(388.3)	(415.5)	(444.6)	
Free cash flow	(7.5)	(29.4)	(13.0)	(3.1)	(11.0)	(69.3)	(44.4)	38.3	47.6	102.4	169.6	253.2	3,898.2

Note: Studio Dragon's content investments are reflected in intangible capital expenditure (cash flow in investment activity), not in operating cash flow

Source(s): Company data, KB Securities estimates

Table 4. Valuation: Discounted Cash Flow Model

(KRWbn, %, k shares, KRW)	Valuation
Total PV of 2023–2028 cash flow	416.9
PV of terminal value	2,471.6
Enterprise value	2,888.5
(-) Net debt	103.4
(-) Non-controlling interests	0.0
(+) Investments in non-consolidated affiliates	12.6
Equity value	2,797.7
(÷) No. of shares	30,058.5
Target price	93,000
Current price	70,200
Upside	32.5
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Source(s): KB Securities estimates

Table 5. WACC Calculation

(KRWbn, %)	Revised	Notes
COE (A) = a + b x c	8.91	
Risk-free rate (a)	3.61	Avg. 1y MSB yield (last three months)
Adj. beta (b)	0.98	Adj. beta
Risk premium (c = d - e)	5.41	
Market (d)	8.72	2001-2021 annual avg. WMI500 total return
Risk-free rate (e)	3.32	2001–2021 annual avg. 1y MSB total return
COD (B)	4.27	Avg. yield of Studio Dragon's short-term debt
Fair equity value	2,797	Value of outstanding shares implied by TP
Debt	183	
Weight of equity value (f)	0.94	
Weight of debt (g)	0.06	
WACC (C) = $(A \times f) + (B \times g)$	8.63	

Source(s): KB Securities estimates (last revised as of Oct 17, 2022)

Income Statement						Statement of Financial Position					
(KRWbn)	2021A	2022E	2023E	2024E	2025E	(KRWbn)	2021A	2022E	2023E	2024E	2025E
(Reporting standard)	(IFRS-C)	(IFRS-C)	(IFRS-C)	(IFRS-C)	(IFRS-C)	(Reporting standard)	(IFRS-C)	(IFRS-C)	(IFRS-C)	(IFRS-C)	(IFRS-C)
Revenue	487	663	802	1,003	1,253	Total assets	884	1,024	1,155	1,393	1,703
Cost of revenue	407	556	678	828	1,022	Current assets	233	395	643	860	1,148
Gross profit	80	106	124	175	231	Cash and cash equivalents	65	133	355	410	585
SG&A expenses	27	32	34	42	52	Current financial assets	5	5	5	6	8
Operating profit	53	74	90	133	179				128	251	313
EBITDA EBITDA	152	221	220	277	340	Trade receivables	124 0	108	0	0	0
	-1	4	5	12	15	Inventory					
Non-operating accounts Interest income	1	1	3	3	3	Other current assets	39	149	155	194	242
						Non-current assets	652	628	512	533	555
Interest expenses	1	0	4	4	4	Investment assets	241	248	255	263	271
Profit on equity method	0	0	0	0	0	Property, plant and equipment	8	11	14	14	15
Net other non-operating income	-1	4	5	12	15	Intangible assets	298	336	210	222	236
Profit before tax	52	78	94	144	194	Other non-current assets	105	33	33	33	33
Income tax expense	13	17	21	33	43	Total liabilities	200	461	518	646	805
Net profit	39	61	74	111	150	Current liabilities	184	448	504	630	787
NP attributable to controlling interests	39	61	74	111	150	Trade payables	17	11	13	16	20
Adj. net profit	39	61	74	111	150	Short-term financial liabilities	0	187	211	263	329
						Other current liabilities	167	249	281	351	439
Operating Statistics & Ratios						Non-current liabilities	17	13	15	16	17
(%)	2021A	2022E	2023E	2024E	2025E	Non-current financial liabilities	7	8	10	10	10
Revenue growth	-7.4	36.0	21,1	25.0	25.0	Other non-current liabilities	9	5	5	6	8
OP growth	7.0	41.0	21.0	47.9	34.9	Total equity	684	682	755	867	1,017
EBITDA growth	-8.3	45.5	-0.4	26.2	22.5	Issued capital	15	15	15	15	15
NP growth of parent	31,8	56.1	20.9	50.8	35.4	Share premium	470	470	470	470	470
GP margin	16.4	16.0	15.4	17.4	18.4	·	0	0	0	0	0
OP margin	10.8	11,2	11,2	13.2	14.3	Other equity interest					
		33.3	27.4	27.7	27.1	Accumulated other comprehensive income	37	-26	-26	-26	-26
EBITDA margin	31,1	11,8		14.4		Retained earnings	162	223	296	408	558
EBT margin	10.7		11.8		15.5	Controlling interests	684	682	755	867	1,017
NP margin of parent	8.0	9.2	9,2	11,1	12,0	Non-controlling interests	0	0	0	0	0
Statement of Cash Flows						Key Ratios					
(KRWbn)	2021A	2022E	2023E	2024E	2025E	(x, %, KRW)	2021A	2022E	2023E	2024E	2025E
Cash flow from operating activities	-8	-28	-3	16	123	Multiples					
Net profit	39	61	74	111	150	P/E	69.9	42.4	32.6	21.6	16.0
Depreciation & amortization	99	146	130	145	161	P/B	4.0	3.8	3.2	2.8	2.4
Other non-cash adjustments	20	13	21	33	43	P/S	5.6	3.9	3.0	2.4	1.9
Investments in working capital	-155	-239	-207	-240	-188	EV/EBITDA	17.6	12,0	10.3	8.2	6.3
Decrease(Increase) in receivables	2	22	-20	-123	-63	EV/EBIT	50.8	35.6	25.2	17.0	12.0
Decrease(Increase) in inventory	0	0	0	0	0	Dividend yield, ordinary (%)	0.0	0.0	0.0	0.0	0.0
Increase(Decrease) in payables	19	7									
• •			1	3	4	EPS OVER	1,301	2,030	2,452	3,697	5,004
Investments in other working capital	-176	-267	-189	-120	-129	BVPS	22,785	22,679	25,131	28,828	33,832
Other operating cash flow	-11	-10	-21	-33	-43	SPS	16,233	22,057	26,683	33,354	41,693
Cash flow from investing activities	27	-48	-6	-15	-16	DPS (annual, ordinary)	0	0	0	0	0
Capital expenditure	-2	-5	-6	-5	-5	Cash dividends payout ratio (%)	0.0	0.0	0.0	0.0	0.0
Investments in intangibles	-1	-2	0	-2	-2	Operating performance					
Changes in investment assets	28	-14	0	-8	-8	ROE	6.0	8.9	10.3	13.7	16.0
Other investment cash flow	1	-26	0	-1	-2	ROA	4.8	6.4	6.8	8.7	9.7
Cash flow from financing activities	-3	138	232	54	67	ROIC	6.1	7.8	8.4	10.9	12,4
Proceeds from (repayment of) debt	-2	174	25	53	66	Financial structure (%)					
Changes in equity	0	0	0	0	0	Total liab./equity	29.3	67.6	68,6	74.5	79.1
Dividends paid	0	0	0	0	0	Net debt/equity	Net Cash	8.3	Net Cash	Net Cash	Net Cash
Other financing cash flow	-1	-36	207	1	2	Current ratio	1.3	0.9	1.3	1,4	1.5
Other cash flow	0	6	0	0	0	Interest coverage (x)	67.6	184,3	23.8	35.2	47.5
Increase/decrease in cash	16	69	222	55	175	Activity ratios					
Cash and cash equivalents at FYE	65	133	355	410	585	Asset turnover (x)	0.6	0.7	0.7	0.8	0.8
Free cash flow	-11	-35	-9	10	117	Receivables turnover (x)	4,2	5.7	6.8	5.3	4.4
Net cash flow	-30	-120	197	3	111	Payables turnover (x)	4.2	47.2	67.9	71.3	71.3
IVEC COSTITION	-50	120	177	Э	111	r dyddies turriover (x)	42.0	41.2	07.9	71,3	/1.5

Source(s): Company data, KB Securities estimates

-57

140

143

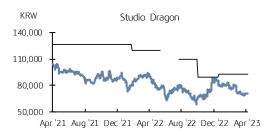
254 Inventory turnover (x)

0.0

0.0

0.0

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



Date	Rating	Analyst	TP Differential (%)			
			(KRW)	Avg.	Max/Min	
Feb-23-2021	Buy	Danny Lee	127,000	-27.54		
Feb-11-2022	Buy	Danny Lee	120,000	-32.37	-21.17	
Aug-08-2022	Buy	Yonghyun Choi	110,000	-35.02	-25,91	
Oct-17-2022	Buy	Yonghyun Choi	90,000	-17.07	-1,22	
Jan-04-2023	Buy	Yonghyun Choi	93,000			

Classification of Investment Ratings

Stock Ratings (based on expected 12m performance)	
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Buy: +15% or beyond Hold: Between 15% and -15% Sell: -15% or beyond Note: Classification revised from four ratings (Strong BUY, BUY, Marketperform, Underperform) to three (Buy, Hold, Sell) as of Feb 23, 2017; Basis for ratings revised from expected 6m return to expected 12m

Ratings Distribution (as of M	tings Distribution (as of March 31, 2023)				
Buy	Hold	Sell			
88.1	11.9	-			

Note: Based on recommendations in the last 12 months

Sector Ratings (based on expected 12m performance)

Positive.	Neutrat.	negative.				
To outperform market	To perform in line with market	To underperform market				
Note: Classification revised from Overweight/Neutral/Underweight to Positive/Neutral/Negative as of Jun						
28, 2017; Basis for ratings revised from expected 6m return to expected 12m return as of Eeb 10, 2020						

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return as of Feb 10, 2020

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