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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

<b>Target Price (Maintain)</b>	<b>KRW93,000</b>
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

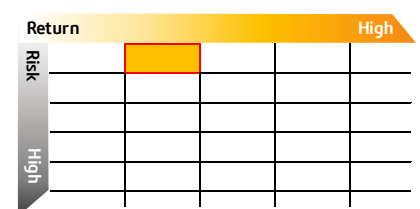
#### Trading Data

Free float	45.2%
Avg. T/O val. (3m, KRWbn)	14.5
Foreign ownership	10.5%
Major shareholders	CJ ENM and 3 others 54.8%
	Naver 6.3%

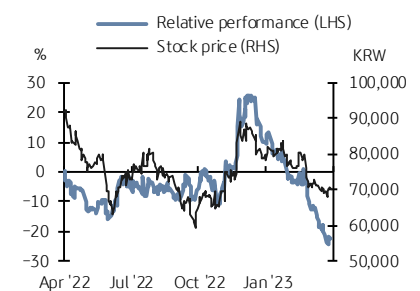
#### Stock Price Performance (total return)

(%)	1M	3M	6M	12M
Absolute	-2.0	-10.3	8.8	-25.2
Relative	-14.0	-30.0	-19.0	-24.5

#### Risk & Total Return (annualized over three years)



#### Stock Price & Relative Performance



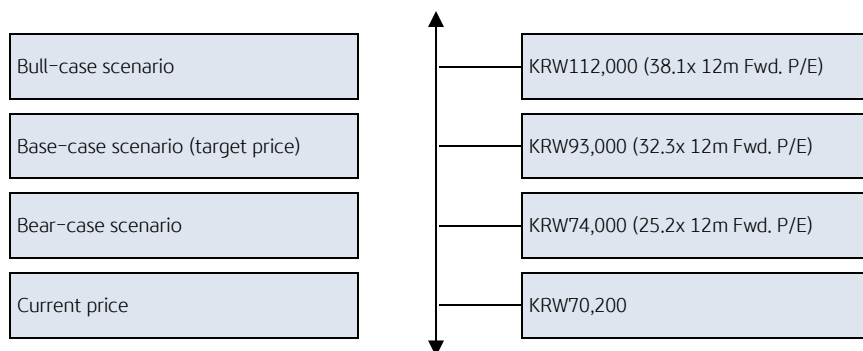
#### Earnings Forecast & Valuation

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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Source(s): Company data, KB Securities

## Investment Opinion & Risks



### Base-case scenario: Catalysts

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

### Bull-case scenario: Upside risks

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

### Bear-case scenario: Downside risks

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

## Revised Earnings Estimates

(KRWbn, %)	Previous		Revised		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

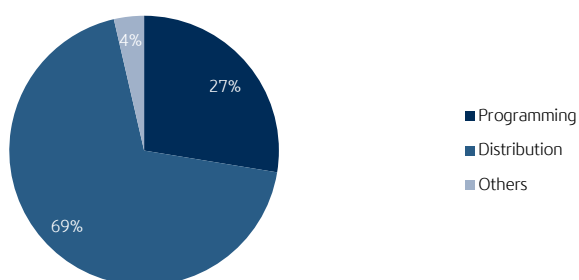
Source(s): KB Securities estimates

## KB Estimates vs. Consensus

(KRWbn, %)	KB Estimates		Consensus		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): Quantwise, KB Securities estimates

## Revenue Composition (2023E)



Source(s): Company data, KB Securities estimates

## Peer Group Comparison

(KRWtn, x, %)	Market Cap.	P/E		P/B		EV/EBITDA		ROE		Dividend Yield	
		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	0.8	1.1

Source(s): Bloomberg consensus, KB Securities estimates

## Valuation & Target Price Calculation

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

## Earnings Sensitivity Analysis

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

**Table 1. Earnings Forecast**

(KRWbn, %)	1Q22	2Q22	3Q22	4Q22	1Q23E	2Q23E	3Q23E	4Q23E	2021	2022	2023E	2024E
<b>Revenue</b>	<b>121.1</b>	<b>157.5</b>	<b>228.9</b>	<b>190.5</b>	<b>169.9</b>	<b>173.2</b>	<b>260.1</b>	<b>263.7</b>	<b>487.1</b>	<b>697.9</b>	<b>866.9</b>	<b>1045.5</b>
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
<b>YoY %</b>	<b>3.4</b>	<b>48.5</b>	<b>97.2</b>	<b>28.8</b>	<b>40.3</b>	<b>10.0</b>	<b>13.6</b>	<b>38.4</b>	<b>-7.3</b>	<b>43.3</b>	<b>24.2</b>	<b>20.6</b>
Programming	-19.1	55.4	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	155.2	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	-75.3	-52.4	-60.1	6.6	12.6	2.6	-49.9	-37.0	12.6
<b>QoQ %</b>	<b>-18.1</b>	<b>30.0</b>	<b>45.3</b>	<b>-16.8</b>	<b>-10.8</b>	<b>2.0</b>	<b>50.1</b>	<b>1.4</b>				
Programming	-33.4	23.7	35.5	-9.1	-7.7	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				
<b>OP</b>	<b>18.1</b>	<b>27.0</b>	<b>18.9</b>	<b>1.2</b>	<b>19.0</b>	<b>21.5</b>	<b>23.3</b>	<b>19.4</b>	<b>52.6</b>	<b>65.2</b>	<b>83.1</b>	<b>116.4</b>
(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	-93.8	1508.7	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
<b>NP to control. int.</b>	<b>15.6</b>	<b>25.6</b>	<b>17.8</b>	<b>-8.5</b>	<b>16.2</b>	<b>19.3</b>	<b>23.5</b>	<b>10.1</b>	<b>39.0</b>	<b>50.6</b>	<b>69.1</b>	<b>95.3</b>
(YoY %)	0.4	170.2	20.5	RR	3.8	-24.6	31.9	TTB	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
<b>EV/sales</b>	<b>6.4x</b>	<b>4.6x</b>	<b>5.1x</b>	<b>5.5x</b>	<b>3.8x</b>	<b>2.6x</b>	<b>2.1x</b>
Revenue	380	469	526	487	698	867	1,045
% YoY	32.4	23.5	12.2	(7.3)	43.3	24.2	20.6
<b>EV/EBITDA</b>	<b>21.1x</b>	<b>14.9x</b>	<b>16.2x</b>	<b>17.6x</b>	<b>12.1x</b>	<b>7.5x</b>	<b>5.8x</b>
EBITDA	115	146	165	152	219	294	376
% YoY	55.1	26.4	13.6	(8.3)	44.1	34.7	27.8
<b>P/E</b>	<b>72.3x</b>	<b>85.9x</b>	<b>88.7x</b>	<b>69.9x</b>	<b>51.1x</b>	<b>30.5x</b>	<b>22.2x</b>
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	36.5	37.8
<b>P/B</b>	<b>6.46x</b>	<b>5.31x</b>	<b>4.56x</b>	<b>3.99x</b>	<b>3.91x</b>	<b>2.89x</b>	<b>2.56x</b>
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

**Table 3. Valuation: Discounted Cash Flow Model**

(KRWbn, %, k shares, KRW)	2017	2018	2019	2020	2021	2022	2023E	2024E	2025E	2026E	2027E	2028E Terminal
<b>NOPLAT</b>	<b>26.6</b>	<b>30.1</b>	<b>22.1</b>	<b>37.2</b>	<b>39.6</b>	<b>57.2</b>	<b>65.9</b>	<b>92.5</b>	<b>127.1</b>	<b>175.1</b>	<b>238.0</b>	<b>319.9</b>
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)
<b>D&amp;A</b>	<b>41.3</b>	<b>75.3</b>	<b>116.8</b>	<b>116.2</b>	<b>99.1</b>	<b>153.3</b>	<b>211.1</b>	<b>259.6</b>	<b>298.3</b>	<b>332.2</b>	<b>363.7</b>	<b>394.3</b>
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
<b>(-)Change in working capital</b>	<b>(72.9)</b>	<b>(139.4)</b>	<b>(142.9)</b>	<b>(144.1)</b>	<b>(154.9)</b>	<b>(279.6)</b>	<b>(38.0)</b>	<b>26.6</b>	<b>(27.7)</b>	<b>(35.6)</b>	<b>(43.3)</b>	<b>(52.6)</b>
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
<b>(-) Tangible capital expenditures</b>	<b>(0.0)</b>	<b>(0.2)</b>	<b>(0.5)</b>	<b>(7.2)</b>	<b>(1.8)</b>	<b>(3.9)</b>	<b>(4.0)</b>	<b>(4.0)</b>	<b>(4.0)</b>	<b>(4.0)</b>	<b>(4.0)</b>	<b>(4.0)</b>
<b>(-) Intangible capital expenditures</b>	<b>(0.2)</b>	<b>(0.1)</b>	<b>(0.3)</b>	<b>(1.2)</b>	<b>(0.8)</b>	<b>(2.5)</b>	<b>(282.6)</b>	<b>(339.2)</b>	<b>(362.9)</b>	<b>(388.3)</b>	<b>(415.5)</b>	<b>(444.6)</b>
<b>(-) Other</b>	<b>(2.1)</b>	<b>5.0</b>	<b>(8.2)</b>	<b>(4.1)</b>	<b>7.9</b>	<b>6.2</b>	<b>3.2</b>	<b>2.7</b>	<b>16.9</b>	<b>23.0</b>	<b>30.7</b>	<b>40.3</b>
<b>Free cash flow</b>	<b>(7.5)</b>	<b>(29.4)</b>	<b>(13.0)</b>	<b>(3.1)</b>	<b>(11.0)</b>	<b>(69.3)</b>	<b>(44.4)</b>	<b>38.3</b>	<b>47.6</b>	<b>102.4</b>	<b>169.6</b>	<b>253.2 3,898.2</b>
<b>(KRWbn, %, k shares, KRW)</b>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023E</b>	<b>2024E</b>	<b>2025E</b>	<b>2026E</b>	<b>2027E</b>	<b>2028E Terminal</b>
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)	(0.8)	(2.5)	(282.6)	(339.2)	(362.9)	(388.3)	(415.5)	(444.6)
<b>Free cash flow</b>	<b>(7.5)</b>	<b>(29.4)</b>	<b>(13.0)</b>	<b>(3.1)</b>	<b>(11.0)</b>	<b>(69.3)</b>	<b>(44.4)</b>	<b>38.3</b>	<b>47.6</b>	<b>102.4</b>	<b>169.6</b>	<b>253.2 3,898.2</b>

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
<b>Enterprise value</b>	<b>2,888.5</b>
(-) Net debt	103.4
(-) Non-controlling interests	0.0
(+) Investments in non-consolidated affiliates	12.6
<b>Equity value</b>	<b>2,797.7</b>
(÷) No. of shares	30,058.5
<b>Target price</b>	<b>93,000</b>
Current price	70,200
<b>Upside</b>	<b>32.5</b>

Source(s): KB Securities estimates

**Table 5. WACC Calculation**

(KRWbn, %)	Revised	Notes
<b>COE (A) = a + b x c</b>	<b>8.91</b>	
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
<b>COD (B)</b>	<b>4.27</b>	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	
<b>WACC (C) = (A x f) + (B x g)</b>	<b>8.63</b>	

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





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