

Company Update

Buy (maintained)

4 October 2017 – 12:30PM

MARKET PRICE: **EUR5.00**

TARGET PRICE: **EUR5.55 (from EUR5.16)**

Entertainment

Data

Shares Outstanding (m):	14.09
Market Cap. (EURm):	70.47
Enterprise Value (EURm):	126.60
Free Float (%):	25.8%
Av. Daily Trad. Vol. (m):	0.01
Main Shareholder:	Leone family 57.5%
Reuters/Bloomberg:	LFG.MI LFG IM
52-Week Range (EUR)	2.5 5.3

Source: Factset, UbiBanca estimates

Performance

	1m	3m	12m
Absolute	9.9%	4.1%	80.5%
Rel. to FTSE IT	5.5%	-4.0%	28.8%

Source: Factset

Graph area Absolute/Relative 12 M



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Positive results in 1H17 but some delays in releases

LFG reported positive results in the first half of the year, with sales from distribution up 6.3% (box office of about EUR25 million for 14 movies, or EUR1.8 million per movie) and sales from production increasing by 15.8% (two productions and five executive productions). The EBITDA margin fell slightly to 31.8% from 36.6% due to the different product mix (executive productions generate lower profitability than distribution) but EBIT was up 13% benefitting from lower D&A costs. The net result of EUR 1.26 million was negatively impacted by EUR0.8 million of non-recurring forex losses. Stripping out non-recurring costs net profit would have increased by about 30% based on our estimates. The company also announced the delay in the release of 6 movies and 2 minor production, but substantially confirmed its business plan which anticipates sales of EUR61 million and EBITDA of EUR29 million. We believe that the EBITDA target could be optimistic given the slowdown reported in 1H17. Against this backdrop, we have fine-tuned our estimates and reduced 2017 EBITDA estimates by 7% although we have raised EBIT and net profit projections to reflect lower D&A and taxes. We remain buyers of the stock, which should benefit from a wide range of long-term contracts with content providers, broadcasters and highly respected Italian directors, potential acquisitions or partnerships to expand outside Italy, an attractive line-up of 74 planned releases in 2017-19, the potential listing on the Star or MTA segment, a film library of almost 500 movies which generate revenues of about EUR3-4 million p.a. at no cost, higher tax credits and possible future blockbusters. We have raised our target price to EUR5.55 per share (from EUR5.16). Positive stance confirmed.

- > We believe that 1H17 results were positive: the 6.8% growth in distribution revenues was particularly notable in a challenging movie market (admissions declined by 12.2% and box office receipts dropped by 16.4%). The Productions division also turned in a positive performance.
- > We expect sales to continue to grow in the second half of the year - we estimate +14% with an improved EBITDA margin.
- > Our new target price of EUR5.55 per share (from EUR5.16) implies potential upside of 11%. The shares are now trading at a discount of about 20% to peers on EB/EBITDA multiples. Buy.

Financials	priced on 3 October 2017			
	2016	2017E	2018E	2019E
Revenues (EURm)	54.71	61.41	71.05	64.92
EBITDA (EURm)	23.52	27.47	35.17	31.67
EBITDA margin (%)	39.3%	37.0%	41.3%	41.0%
EBIT (EURm)	2.96	6.22	8.92	7.43
EPS (EUR)	0.13	0.22	0.38	0.32
CFPS (EUR)	1.90	1.43	2.10	2.16
DPS (EUR)	0.09	0.11	0.15	0.20

Source: Company Data, UBI Banca Estimates

Ratios	priced on 3 October 2017			
	2016 *	2017E	2018E	2019E
P/E(x)	20.2	22.3	13.0	15.8
P/CF(x)	1.6	2.9	2.2	2.5
P/BV(x)	1.1	2.0	1.8	1.7
Dividend Yield	3.4%	2.2%	3.0%	4.0%
EV/EBITDA(x)	3.0	4.5	3.6	3.7
Debt/Equity (x)	1.0	1.5	1.4	1.2
Debt/EBITDA (x)	1.4	1.9	1.6	1.5

Source: UBI Banca Estimates * Based on 2016 average price

Key Financials

(EURm)	2016	2017E	2018E	2019E
Revenues	54.71	61.41	71.05	64.92
EBITDA	23.52	27.47	35.17	31.67
EBIT	2.96	6.22	8.92	7.43
NOPAT	2.01	4.23	6.06	5.05
Free Cash Flow	-4.73	-19.98	-0.70	10.27
Net Capital Employed	65.31	88.45	94.57	88.75
Shareholders' Equity	33.02	34.91	38.78	41.12
Net Financial Position	32.29	53.54	55.79	47.63

Source: Company data, UBI Banca estimates

Key Profitability Drivers

	2016	2017E	2018E	2019E
Net Debt/Ebitda (x)	1.4	1.9	1.6	1.5
Net Debt/Equity (x)	1.0	1.5	1.4	1.2
Interest Coverage (%)	2.3	3.3	7.5	7.0
Free Cash Flow Yield (%)	-12.9%	nm	nm	14.6%
ROE (%)	5.5%	9.1%	14.0%	10.8%
ROI pre-tax (%)	4.7%	8.0%	9.6%	8.0%
ROCE (%)	3.3%	5.5%	6.6%	5.5%

Source: Company data, UBI Banca estimates

Key Valuation Ratios

	2016 *	2017E	2018E	2019E
P/E (x)	20.2	22.3	13.0	15.8
P/BV (x)	1.1	2.0	1.8	1.7
P/CF (x)	1.6	2.9	2.2	2.5
Dividend Yield (%)	3.4%	2.2%	3.0%	4.0%
EV/Sales (x)	1.2	1.7	1.5	1.5
EV/EBITDA (x)	3.0	4.5	3.6	3.7
EV/EBIT (x)	23.4	20.0	14.2	15.9
EV/CE (x)	1.1	1.4	1.3	1.3

Source: Company data, UBI Banca estimates

* Based on 2016 average price

Key Value Drivers

(%)	2016	2017E	2018E	2019E
Payout	69.8%	49.0%	39.1%	63.2%
NWC/Sales	4.4%	9.3%	10.5%	9.5%
Capex/Sales	52.7%	54.0%	35.6%	26.0%

Source: Company data, UBI Banca estimates

Recent Developments

- > LFG distributed 14 movies in the first half of 2017 (compared with four in 1H16), including two blockbusters (“La La Land” which generated box office receipts of EUR8 million, and “Hacksaw Ridge” with EUR6 million) contributing to total box office receipts of about EUR25 million, representing EUR1.8 million per movie, well above the average Italian box office figure, which was around EUR0.3 million per movie in 1H17, leading to an increase of 6.4% of sales from distribution. LFG’s market share (calculated on pro-forma basis, as LFG does not distribute movies directly but signs distribution agreements with major distributors in Italy) in the first half was 7.9%, ranking second amongst the Italian distributors (the leader being 01 Distribution, or RAI). Production revenues rose 15.8% with two productions completed (“Immaturo” and “Innamorati di me”) and five executive productions for foreign clients. Total revenues were up 10.8% to EUR35.3 million of which EUR3.5 million related to tax credits; sales in 1H17 represented approximately 58% of 2017 expected sales in LFG’s business plan (50.2% for distribution and 69.3% for production).
- > The EBITDA margin of 31.8% in 1H17 was slightly below last year (36.6% with Productions division at 14.0% and Distribution division at 48.9%) for two main reasons: 1) the different sales mix, reflecting a higher proportion of executive productions, which have lower profitability, and 2) the increase in labour costs (+14%) and other operating costs (+35%). However, EBIT rose 13.5% with a 8.1% margin due to lower D&A costs. The net result was 11.5% lower than in 1H16 mostly due to higher financial charges and taxes. LFG’s results were adversely impacted by non-recurring unrealized losses of EUR0.8 million on USD hedging contracts. Stripping out non-recurring costs, we estimate that net profit would have increased by about 30%. Net debt was EUR35.7 million, slightly up compared with Dec-16 (EUR32.3 million), despite higher investments (about EUR14 million) and dividend payment (EUR1.2 million), due to EUR6.2 million cash inflow from international producers to finance executive productions. The company’s film library of >500 movies had a net value of EUR49.1 million at June-17 vs. EUR45.1 million at Dec-16, corresponding to 70% of the current market cap.
- > The trend in the movie market was negative in 1H17: admissions declined by 12.2% and box office receipts dropped by 16.4% (source: *Cinetel*) partly due to lower ticket prices (-4.8% on average). In particular, the box office for the Italian distributors fell by 40.7% in the first half of the year (it should be noted that 1H16 was exceptionally strong due to “Quo Vado” which accounted for >EUR65 million of box office).
- > LFG’s buy-back program (worth up to EUR1.7 million) accounted for 107k shares, representing 0.75% of the share capital at the end of August. The buy-back programme was conceived to support possible M&A activity, enhance the liquidity of the shares and support the company’s stock option plan.

Figure 1 – 1H17 results

(EURm)	1H16A	1H17A	% Chg.
Sales total	31.90	35.33	10.8%
EBITDA	11.66	11.24	-3.6%
% margin	36.6%	31.8%	
EBIT	2.52	2.86	13.5%
% margin	7.9%	8.1%	
Pre tax profit	1.82	1.72	-5.5%
Net profit	1.42	1.26	-11.5%
Net debt/(cash)	28.38	35.66	

Source: Company data

Figure 2 – 1H17 results by division

(EURm)	1H16A	1H17A	% Chg.
Sales Distribution	16.99	18.07	6.3%
Sales Production	14.91	17.26	15.8%
EBITDA Distribution	7.50	8.84	17.8%
% margin	44.1%	48.9%	
EBITDA Production	4.17	2.41	-42.2%
% margin	28.0%	14.0%	
EBIT Distribution	0.04	1.55	nm
% margin	0.3%	8.6%	
EBIT Production	2.49	1.32	-47.0%
% margin	16.7%	7.6%	

Source: Company data

Figure 3 – Movie releases in 1H17

Movie title	Release	Box office (EUR000) E
La La Land	Jan-17	7,889
A dog's purpose	Jan-17	1,509
La battaglia di Hacksaw Ridge	Feb-17	5,804
Omicidio all'italiana	Mar-17	976
The light between the oceans	Mar-17	262
Jhon Wick 2	Mar-17	1,792
Power Rangers	Apr-17	712
Boston caccia l'uomo	Apr-17	541
Gold	May-17	920
Song to song	May-17	257
Sette minuti dopo la mezzanotte	May-17	55
Civiltà perduta	Jun-17	597
The last face	Jun-17	55
Nerve	Jun-17	1,085

Source: Cinetel

Financial Projections

- > The company gave no specific guidance for the full year but said that the release of two productions (“Hotel Gagarin” and “Notti Magiche”) have been postponed to 2018 along with the distribution of six movies, while one movie previously expected to be distributed in 2018 will be anticipated at the end of the year. These postponements should not impact the business plan presented in April 2017, which forecasts 74 releases in 2017-19 of which 56 movie distributions, 11 productions and 7 executive productions which could boost revenues to EUR67 million in 2019 with a 7.2% CAGR over the period. EBITDA could grow at 22.5% CAGR with margins rising to 64.5% in 2019 compared with 43.1% in 2016.
- > The business plan implies a strong second half in 2017 with revenues of about EUR25 million (+12% vs. 2H16) and an EBITDA margin of 70% compared with 52% in the second half of 2016. We believe that the company’s EBITDA target could be overly optimistic given the postponement of several movies. Consequently, we have downgraded our EBITDA forecast for 2017 by 7%. However, lower than expected D&A costs prompts us to reduce our projection of D&A costs, leading to an increase of 7% in our EBIT estimate. We now estimate the net result to be EUR3.2 million (+5%), incorporating the forex loss reported in 1H17 but also a lower tax rate. Net debt is expected to be EUR53.5 million, broadly in line with our previous expectations.
- > 2018 and 2019 estimates for revenues and EBITDA were just fine-tuned while the lower expected D&A costs and tax charges result in an average increase of about 10% to our bottom line forecast.

Figure 4 – Old vs. New estimates

(EURm)	2016A	2017E		2018E		2019E	
		Old	New	Old	New	Old	New
Total Sales	54.7	61.3	61.4	68.5	71.1	63.5	64.9
% change			0.2%		3.8%		2.2%
EBITDA	23.5	29.6	27.5	35.0	35.2	31.9	31.7
% change			-7.0%		0.5%		-0.9%
EBIT	3.0	5.8	6.2	8.4	8.9	7.5	7.4
% change			6.7%		6.5%		-0.8%
Net Profit	1.8	3.0	3.2	4.7	5.4	4.2	4.5
% change			4.8%		15.2%		6.1%
Net Debt/(Cash)	32.3	54.6	53.5	53.5	55.8	45.5	47.6

Source: Company data, UBI Banca estimates

Figure 5 – 2H17 estimates

(EURm)	2H16A	2H17E	% Chg.
Sales total	22.81	26.08	14.3%
EBITDA	11.85	16.23	36.9%
% margin	52.0%	62.3%	
EBIT	0.44	3.36	665.2%
% margin	1.9%	12.9%	
Pre tax profit	-0.12	2.61	nm
Net profit	0.40	1.91	379.1%
Net debt/(cash)	32.29	53.54	

Source: Company data, UBI Banca estimates

Figure 6 – 2H17 estimates by division

(EURm)	2H16A	2H17E	% Chg.
Sales Distribution	12.54	14.12	12.6%
Sales Production	4.28	5.16	20.7%
EBITDA Distribution	10.68	7.90	-26.0%
% margin	85.1%	56.0%	
EBITDA Production	1.20	2.32	92.4%
% margin	28.2%	44.9%	
EBIT Distribution	0.23	0.70	203.9%
% margin	1.8%	5.0%	
EBIT Production	-0.79	-3.32	321.8%
% margin	-18.4%	-64.3%	

Source: Company data, UBI Banca estimates

Valuation

- > Given the revisions to our forecasts, our DCF valuation has increased to EUR7.18 per share (from EUR6.60) and our relative valuation to EUR5.15 per share from EUR4.87 per share. The simple average of our DCF and the relative valuation gives a fair value of EUR6.17. We have applied a 10% liquidity discount to the fair value to take into account the limited liquidity of LFG and its modest size which generates a target price of EUR5.55 per share (vs. EUR5.74 before). This discount could diminish on listing of the company on the MTA.
- > LFG's current market capitalization (EUR70 million) is broadly in line with its net invested capital (EUR69 million at June-17) which implies that LFG may not be able to create value in future. We believe this scenario is highly unlikely given the wide line up of the company and the margin improvements expected for 2017-19.
- > At our EUR5.50 per share target price, LFG would trade at 3.8x 2018 EV/EBITDA, which is below the average multiple of our sample of peers (4.5x).

Figure 7 – Valuation summary

(EUR)		Weight	10-May-17	Delta
DCF Valuation	7.18	50.0%	6.60	8.9%
Relative Valuation	5.15	50.0%	4.87	5.8%
Fair Value	6.17		5.74	7.5%
Liquidity discount (10%)	(0.62)		(0.57)	7.5%
Target price	5.55		5.16	7.5%
Current price	5.00		4.64	7.8%
Potential upside	11.0%		11.2%	

Source: UBI Banca estimates

Figure 8 – DCF Valuation

Our model incorporates a terminal growth rate of 1.5% and an EBITDA margin of 50% at terminal value, which is below the margin included in the business plan for 2019 (64.5%) but above what we expect this year (44.7%). Our DCF valuation implies 4.3x EV/EBITDA at terminal value.

	(EUR m)	(% weight)
Sum of PV 2017-25 FCF	30.7	23%
Terminal value	103.2	77%
Total Enterprise value	133.9	100%
- minorities	0.0	
- Pension Provision	(0.3)	
- Net debt (+ cash)	(32.3)	
Total Equity value	101.3	
Fully diluted number of shares (m)	14.1	
Fair value per share (EUR)	7.18	

Source: UBI Banca estimates

Figure 9 – Peer comparison and valuation based on multiples (priced on 3 October 2017)

Company	Market Cap (EURm)	P/E			EV/EBITDA			EV/EBIT		
		2017E	2018E	2019E	2017E	2018E	2019E	2017E	2018E	2019E
EuropaCorp SA	83	27.7 x		0.4 x	2.5 x	3.3 x	0.8 x	26.2 x	45.0 x	1.3 x
Splendid Medien AG	16		10.8 x	10.3 x	4.6 x	2.4 x	9.9 x		12.4 x	13.1 x
Lions Gate	5,957	33.1 x	33.2 x	24.4 x	15.0 x	13.2 x	11.3 x	25.4 x	19.0 x	14.6 x
Entertainment One Ltd.	1,286	12.3 x	10.9 x	9.6 x	8.1 x	7.0 x	6.2 x	8.4 x	7.1 x	6.6 x
Constantin Medien AG	195	34.7 x	10.9 x	8.7 x	5.8 x	3.6 x	2.6 x	7.2 x	4.2 x	3.1 x
Highlight Communications AG	243	15.5 x	13.6 x	12.6 x	3.8 x	3.1 x	2.8 x	8.5 x	7.7 x	7.1 x
Lucisano Media Group	40	44.5 x	5.1 x	3.9 x	3.9 x	2.8 x	2.3 x	2.3 x	5.5 x	4.1 x
Mondo TV	134	10.8 x	11.9 x	9.8 x	5.1 x	3.5 x	3.1 x	7.3 x	7.0 x	5.6 x
Notorious Pictures	26	7.1 x	6.7 x	5.8 x	2.3 x	1.8 x	1.5 x	4.2 x	3.5 x	2.8 x
Average		23.2 x	12.9 x	9.5 x	5.7 x	4.5 x	4.5 x	11.2 x	12.4 x	6.5 x
Current market multiples	70	22.3 x	13.0 x	15.8 x	4.5 x	3.6 x	3.7 x	20.0 x	14.2 x	15.9 x
Discount to Average		-3.9%	0.9%	66.2%	-20.2%	-20.6%	-17.1%	78.6%	14.7%	146.3%

Source: Factset, UBI Banca estimates

Figure 10 – Implicit multiples based on our EUR5.55 target price

(x)	2017E	2018E	2019E
P/E	24.7 x	14.5 x	17.6 x
EV/EBITDA	4.8 x	3.8 x	4.0 x
EV/EBIT	21.2 x	15.1 x	17.0 x
EV/Sales	1.78 x	1.58 x	1.63 x
P/BV	2.2 x	2.0 x	1.9 x
EV/ Capital employed	1.5 x	1.4 x	1.4 x

Source: UBI Banca estimates

Income Statement

(EURm)	2016	2017E	2018E	2019E
Net Revenues	59.77	74.30	85.23	77.23
EBITDA	23.52	27.47	35.17	31.67
EBITDA margin	39.3%	37.0%	41.3%	41.0%
EBIT	2.96	6.22	8.92	7.43
EBIT margin	5.0%	8.4%	10.5%	9.6%
Net financial income /expense	-1.26	-1.89	-1.18	-1.07
Associates & Others	0.00	0.00	0.00	0.00
Profit before taxes	1.70	4.33	7.73	6.37
Taxes	0.12	-1.17	-2.32	-1.91
Minorities & discontinuing ops	0.00	0.00	0.00	0.00
Net Income	1.82	3.16	5.41	4.46

Source: Company data, UBI Banca estimates

Balance Sheet

(EURm)	2016	2017E	2018E	2019E
Net working capital	2.62	6.92	8.99	7.31
Net Fixed assets	63.79	82.76	86.99	83.58
M/L term funds	-1.11	-1.22	-1.42	-2.14
Capital employed	65.31	88.45	94.57	88.75
Shareholders' equity	33.02	34.91	38.78	41.12
Minorities	0.00	0.00	0.00	0.00
Shareholders' funds	33.02	34.91	38.78	41.12
Net financial debt/(cash)	32.29	53.54	55.79	47.63

Source: Company data, UBI Banca estimates

Cash Flow Statement

(EURm)	2016	2017E	2018E	2019E
NFP Beginning of Period	24.03	32.29	53.54	55.79
Group Net Profit	1.82	3.16	5.41	4.46
Minorities	0.00	0.00	0.00	0.00
D&A	20.55	21.25	26.26	24.24
Change in Funds & TFR	0.00	0.00	0.00	0.00
Gross Cash Flow	22.37	24.41	31.67	28.70
Change In Working Capital	4.40	-4.29	-2.07	1.68
Other	0.00	0.00	0.00	0.00
Operating Cash Flow	26.77	20.12	29.60	30.37
Net Capex	-31.50	-40.10	-30.30	-20.10
Other Investments	0.00	0.00	0.00	0.00
Free Cash Flow	-4.73	-19.98	-0.70	10.27
Dividends Paid	-1.21	-1.27	-1.55	-2.11
Other & Chg in Consolid. Area	-2.32	0.00	0.00	0.00
Chg in Net Worth & Capital Incr.	0.00	0.00	0.00	0.00
Change in NFP	-8.26	-21.25	-2.25	8.16
NFP End of Period	32.29	53.54	55.79	47.63

Source: Company data, UBI Banca estimates

Financial Ratios

(%)	2016	2017E	2018E	2019E
ROE	5.5%	9.1%	14.0%	10.8%
ROI	4.7%	8.0%	9.6%	8.0%
Net Fin. Debt/Equity (x)	1.0	1.5	1.4	1.2
Net Fin. Debt/EBITDA (x)	1.4	1.9	1.6	1.5
Interest Coverage	2.3	3.3	7.5	7.0
NWC/Sales	4.4%	9.3%	10.5%	9.5%
Capex/Sales	52.7%	54.0%	35.6%	26.0%
Pay Out Ratio	69.8%	49.0%	39.1%	63.2%

Source: Company data, UBI Banca estimates

Per Share Data

(EUR)	2016	2017E	2018E	2019E
EPS	0.13	0.22	0.38	0.32
DPS	0.09	0.11	0.15	0.20
Op. CFPS	1.90	1.43	2.10	2.16
Free CFPS	-0.34	-1.42	-0.05	0.73
BVPS	2.34	2.48	2.75	2.92

Source: Company data, UBI Banca estimates

Stock Market Ratios

(x)	2016 *	2017E	2018E	2019E
P/E	20.2	22.3	13.0	15.8
P/OpCFPS	1.4	3.5	2.4	2.3
P/BV	1.1	2.0	1.8	1.7
Dividend Yield (%)	3.4%	2.2%	3.0%	4.0%
Free Cash Flow Yield (%)	-12.9%	nm	nm	14.6%
EV (EURm)	69.38	124.33	126.60	118.46
EV/Sales	1.2	1.7	1.5	1.5
EV/EBITDA	3.0	4.5	3.6	3.7
EV/EBIT	23.4	20.0	14.2	15.9
EV/Capital Employed	1.1	1.4	1.3	1.3

Source: Company data, UBI Banca estimates

* Based on 2016 average price

Growth Rates

(%)	2016	2017E	2018E	2019E
Growth Group Net Sales	14.2%	24.3%	14.7%	-9.4%
Growth EBITDA	22.7%	16.8%	28.0%	-10.0%
Growth EBIT	-31.9%	110.0%	43.3%	-16.6%
Growth Net Profit	-49.4%	74.1%	71.1%	-17.6%

Source: Company data, UBI Banca estimates

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Hold: if the target price is 10% below or 10% above the market price, over the next 12 months.

Sell: if the target price is 10% lower than the market price, over the next 12 months.

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Market price: closing price on the day before the issue date of the report, appearing on the first page.

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Equity rating dispersion in the past 12 months

Buy	Hold	Sell	No Rating
85.7%	11.4%	0.0%	2.9%

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Buy	Hold	Sell	No Rating
100%	100%	-	100%

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Historical ratings and target prices

Date	Rating	Target Price (EUR)	Market Price (EUR)
10 May 2017	Buy	5.16	4.64