

Company Update

Buy (maintained)

13 April 2018 – 5:30PM

MARKET PRICE: EUR5.05

TARGET PRICE: EUR6.86 (from EUR6.34)

Entertainment

Data

Shares Outstanding (m):	14.09		
Market Cap. (EURm):	71.17		
Enterprise Value (EURm):	106.7		
Free Float (%):	25.6%		
Av. Daily Trad. Vol. (m):	0.01		
Main Shareholder:	Leone family 57.8%		
Reuters/Bloomberg:	LFG.MI	LFG IM	
52-Week Range (EUR)	4.0	5.3	

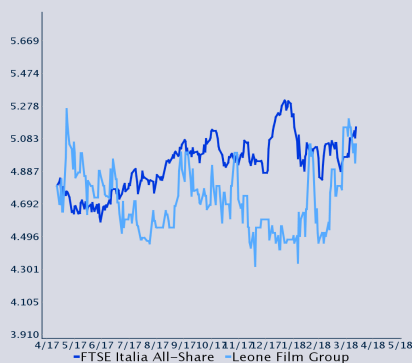
Source: Factset, UbiBanca estimates

Performance

	1m	3m	12m
Absolute	10.3%	13.2%	26.3%
Rel. to FTSE IT	8.2%	14.6%	9.4%

Source: Factset

Graph area Absolute/Relative 12 M



Source: Factset

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2017 above expectations and upcoming rights issue

LFG reported 2017 sales of EUR105.6 million (+93% for the full year and +209% in 2H17), slightly above the preliminary results (+7%), while the EBITDA increased by 25% vs. 2016, consistent with the 2017-2019 business plan and 10% above the preliminary results announced last February. Despite the high D&A of EUR24 million due to the 2017 positive box office performance, the EBIT remained in line with the business plan at EUR 5.4 million (+80% vs. 2016) and net profit (EUR3.9 million) was well above our expectations and the business plan benefitting from ax credits for executive productions. LFG also announced a share capital increase (already approved by EGM) up to EUR30 million in one or more tranches, without share option rights and reserved for institutional investors. The aim of the capital increase is to provide LFG with fresh financial resources to even increase the investments in the core activities and increase the free float; we believe a first tranche could arrive shortly. Lastly, the 2018 kickoff was strongly positive with 3 blockbusters released (“Wonder”, “The Post” and “A Casa Tutti Bene”) and >EUR24 million box office takings to date (around 55% of the box office reported in the whole of 2017). We have revised our estimates upward (top line forecasts for 2018-19 +6% on average and EBITDA +5% on average). Buy confirmed with a new target price of EUR6.86 per share (from EUR6.34).

- > We were surprised by 2017 results above the preliminary outcome and by the robust start to the year. Our new estimates point to a sales CAGR of 7.7% until 2020 with an EBITDA which could exceed EUR44 million in 2020 and a bottom line >8 million. Net debt, excluding the cash in from the upcoming rights issue, should progressively decline to EUR26 million at Dec-20.
- > Assuming a rights issue of EUR10 million at to the current market price, thus implying an issue price of about EUR5.0 per share, we estimate an EPS dilution of around 9.6% for current shareholders and free float growing up to 34.1% from current 24.8%. Leone family would be diluted to 51.3% stake.
- > Our new target price of EUR6.86 per share (from EUR6.34) implies potential upside of >35%. The shares are now trading at a discount of about 58% to the average 2018-19 EV/EBITDA of peers and at a 38% discount to P/E. Positive stance confirmed.

Financials

	2017	2018E	2019E	2020E
Revenues (EURm)	105.76	117.60	125.33	131.71
EBITDA (EURm)	29.42	42.38	42.33	44.62
EBITDA margin (%)	25.1%	32.8%	31.0%	30.8%
EBIT (EURm)	5.38	13.34	13.14	14.77
EPS (EUR)	0.28	0.52	0.53	0.62
CFPS (EUR)	1.98	2.58	2.59	2.73
DPS (EUR)	0.00	0.15	0.20	0.20

Source: Company Data, UBI Banca Estimates

Ratios

priced on 12 April 2018

	2017 *	2018E	2019E	2020E
P/E(x)	15.5	9.7	9.6	8.2
P/CF(x)	2.2	2.0	1.9	1.8
P/BV(x)	1.7	1.7	1.5	1.3
Dividend Yield	0.0%	3.0%	4.0%	4.0%
EV/EBITDA(x)	3.4	2.7	2.5	2.1
Debt/Equity (x)	1.1	1.0	0.7	0.4
Debt/EBITDA (x)	1.4	1.0	0.8	0.5

Source: UBI Banca Estimates * Based on 2017 average price

Key Financials

(EURm)	2017	2018E	2019E	2020E
Revenues	105.79	117.60	125.33	131.71
EBITDA	29.42	42.38	42.33	44.62
EBIT	5.42	13.34	13.14	14.77
NOPAT	3.69	9.07	8.93	10.04
Free Cash Flow	-4.53	-0.04	12.48	16.43
Net Capital Employed	76.33	86.14	83.53	78.24
Shareholders' Equity	35.79	43.10	48.39	54.26
Net Financial Position	40.54	43.04	35.14	23.98

Source: Company data, UBI Banca estimates

Key Profitability Drivers

	2017	2018E	2019E	2020E
Net Debt/Ebitda (x)	1.4	1.0	0.8	0.5
Net Debt/Equity (x)	1.1	1.0	0.7	0.4
Interest Coverage (%)	1.9	5.5	6.3	8.2
Free Cash Flow Yield (%)	-7.5%	nm	17.5%	23.1%
ROE (%)	10.9%	17.0%	15.3%	16.0%
ROI pre-tax (%)	7.6%	16.2%	15.3%	18.0%
ROCE (%)	5.2%	11.2%	10.5%	12.4%

Source: Company data, UBI Banca estimates

Key Valuation Ratios

	2017 *	2018E	2019E	2020E
P/E (x)	15.5	9.7	9.6	8.2
P/BV (x)	1.7	1.7	1.5	1.3
P/CF (x)	2.2	2.0	1.9	1.8
Dividend Yield (%)	0.0%	3.0%	4.0%	4.0%
EV/Sales (x)	0.9	0.9	0.8	0.7
EV/EBITDA (x)	3.4	2.7	2.5	2.1
EV/EBIT (x)	18.7	8.6	8.1	6.5
EV/CE (x)	1.3	1.3	1.3	1.2

Source: Company data, UBI Banca estimates

* Based on 2017 average price

Key Value Drivers

(%)	2017	2018E	2019E	2020E
Payout	0.0%	28.9%	38.1%	32.5%
NWC/Sales	1.2%	1.4%	1.4%	1.4%
Capex/Sales	28.7%	27.8%	17.6%	15.2%

Source: Company data, UBI Banca estimates

Recent Developments

- > LFG reported EUR105.8 million revenues, slightly above preliminary results, crushing the EUR54.7 million reached in 2016 (+93%). This outstanding result can be attributed to: 1) the good results of the movies distributed and produced, and 2) the exceptional growth of international executive productions (EUR41.7 million in the top line), which also benefitted from changes in the accounting methodology (prior to 2016 LFG only recognized the international executive production fees within sales, without incorporating revenues and production costs, while in 2017 it recognized the full cost and revenues of the international executive productions).
- > As a result of executive productions, the EBITDA margin suffered a dilutive effect moving from 43% in 2016 to 28% in 2017, while the performance of the movies released pushed the EBITDA in absolute terms up by 25% to EUR29.4 million, above our expectations and in line with the business plan projections. The positive results of the box office in 2017 determined a significant increase in D&A, which pushed the EBIT below our estimate (EUR5.4 million actual vs. EUR6.1 million estimate), but still in line with the plan. The net profit experienced significant growth (+117% for the full year) stopping at EUR3.9 million, thanks to the tax credit for executive productions, which more than offset corporate taxes and the negative effect of mark to market of derivatives on USD for around EUR1.5 million.
- > The preliminary results regarding the net financial position are confirmed: the sharp improvement compared to the business plan is due to lower capex (related to the postponement of movie releases) and to significant advances from co-producers. Moreover, it is worth mentioning that the net financial position includes advances of EUR12.3 million relating to movies and projects whose economic results will only be forthcoming in the next few years.
- > Contrary to last year, LFG will not distribute dividends. This is explained by the substantial break-even condition of the parent company, mainly due to the mark to market of derivatives on USD and by the share capital increase currently being raised. There is nothing to prevent LFG from distributing more dividends next year and we assume a DPS of EUR0.15 on 2018 result.
- > The company announced a share capital increase (already approved by EGM on March 28) of up to EUR30 million in one or more tranches, without share option rights and reserved for institutional investors. The rights issue should be finalized by the end of December 2018. The price will be set by the Board and should be above the book value per share at June-17 (or EUR2.36 per share). We believe that a first tranche of the capital increase could be completed by the end of April through accelerated book-building. Assuming a rights issue of EUR10 million at the current market price, thus implying an issue price of about EUR5.0 per share, we estimate an EPS dilution of around 9.6% for current shareholders and free float growing to 34.1% from the current 24.9%. The rights issue aims to reinforce LFG's financial structure in order to sustain its growth strategy while increasing the free float of the company. According to the management, the two main shareholders, Andrea and Raffaella Leone (who together now own a 58.5% stake), could be diluted to a stake below 50%.
- > In addition, a further capital increase of EUR1 million was approved by the EGM: this rights issue is reserved for the successful film director Paolo Genovese, who has signed a multi-year exclusive contract (until 2023) with LFG. Mr. Genovese already has a 1% stake in LFG and is subject to a 5-year lock-up.

- > LFG distributed 25 movies in 2017, including several blockbusters (“La La Land” which generated box office receipts of >EUR8 million, “Wonder” with >EUR12 million box office, and “Hacksaw Ridge” with almost EUR4 million) contributing to total box office receipts of about EUR44.2 million, representing around EUR1.7 million per movie, well above the average Italian box office figure, which was around EUR1.1 million per movie in 2017. LFG’s market share (calculated on a pro-forma basis, as LFG does not distribute movies directly but signs distribution agreements with major distributors in Italy) in the full year was about 7.6%, placing it top among Italian distributors.
- > The trend in the movie market was negative in 2017: admissions dropped by 12.4% in 2017 and box office receipts were down by 11.6% (source: Cinetel) with a sharp decrease in average theatrical sales per movie (-8.7% at EUR1.09 million).
- > LFG’s buy-back program (worth up to EUR1.7 million) accounted for 161k shares, representing 1.14% of the share capital at the end of March. 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.

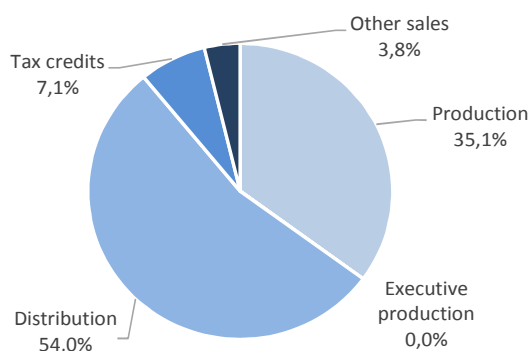
Figure 1 – 2017 results

(EURm)	2016A	2017A	% Chg.	2017E	% Chg.
Sales Distribution	29.54	31.60	7.0%	32.19	-1.8%
Sales Production	19.18	55.16	187.6%	59.44	-7.2%
Sales Other	5.99	19.00	217.2%	12.90	47.3%
Sales total	54.71	105.76	93.3%	104.53	1.2%
EBITDA	23.52	29.42	25.1%	26.66	10.4%
% margin	43.0%	27.8%		25.5%	
EBIT	2.96	5.38	81.7%	6.12	-12.0%
% margin	5.4%	5.1%		5.9%	
Pre tax profit	1.70	2.48	46.3%	3.73	-33.4%
Net profit	1.82	3.88	113.8%	2.72	42.8%
Net debt/(cash)	32.29	40.50	25.6%	40.74	-0.6%

Source: Company data, UBI Banca estimates

Figure 2 – 2016 sales breakdown by product

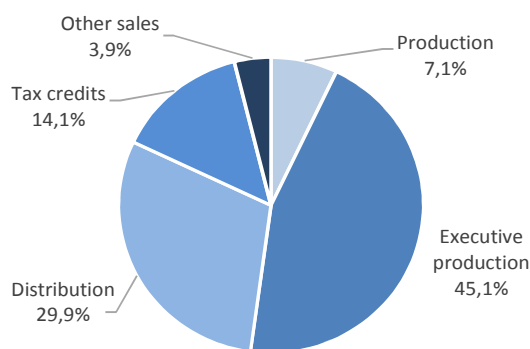
In 2016 the bulk of revenues were represented by Distribution and Production...



Source: Company data

Figure 3 – 2017 sales breakdown by product

...But in 2017, the breakdown change substantially: executive productions represented >45% of sales and tax credits increase significantly.



Source: UBI Banca estimates based on company data

Figure 4 – 2H17 results

(EURm)	2H16A	2H17A	% Chg.
Sales Distribution	12.54	13.53	7.9%
Sales Production	4.28	37.90	786.5%
Sales Other	5.99	19.00	217.2%
Sales total	22.81	70.43	208.8%
EBITDA	11.85	18.18	53.4%
% margin	52.0%	25.8%	
EBIT	0.44	2.52	474.2%
% margin	1.9%	3.6%	
Pre tax profit	-0.12	0.76	nm
Net profit	0.40	2.63	560.5%

Source: Company data

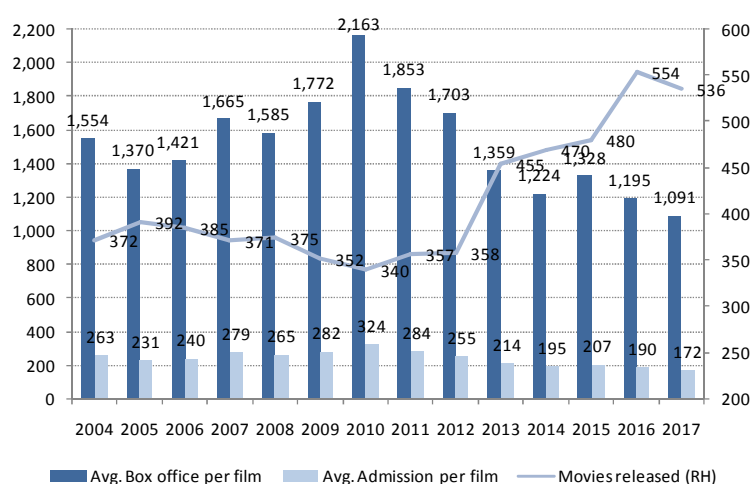
Figure 5 – Sensitivity based on the issue price of EUR10 million capital increase

A right issue of EUR10 million at current market price would generate an EPS dilution of around 9.6% based on our calculations. A capital increase of EUR30 million (the maximum approved by the EGM) at current market price would dilute EPS by 27% reducing the stake of the Leone family to 41.1% and increasing the free float to 47.1%

Issue price (EUR)	5.05	4.80	4.55	4.29
Discount on actual price	0.0%	-5.0%	-10.0%	-15.0%
New shares	1.98	2.08	2.20	2.33
Total shares	16.07	16.18	16.29	16.42
Dilution on share number	12.3%	12.9%	13.5%	14.2%
EPS accretion 2018	2.7%	2.7%	2.7%	2.7%
Total EPS dilution	9.6%	10.1%	10.8%	11.4%
Free float	34.1%	34.5%	35.0%	35.5%
Andrea and Raffaella Leone	51.3%	50.9%	50.6%	50.2%

Source: UBI Banca estimates

Figure 6 – Movies released, box office and admissions in Italy – average per movie (000)



Source: UBI Banca on Cinetel data

Financial Projections

- > The Company has not yet provided an outlook (pending the share capital increase), however we can expect a potential expansion in foreign markets and/or additional investments in Italy. The outlook will therefore be provided with the business plan update, released once the capital increase is closed, according to the press release. At that point the management will know the amount of the cash in and therefore the financial resources available for future growth. It should be noted that the business plan presented in April 2017 anticipated 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.
- > We have updated our forecasts following 2017 results and added 2020 projections. 2018 started strongly with “Wonder” generating box office receipts of the year of almost EUR7.2 million, “The Post” taking EUR6.4 million and “A Casa Tutti Bene” reaching EUR9.1 million. Together all the movies released by LFG since the start of the year (“Wonder”, “A Casa Tutti Bene”, “The Post”, “Based on a True Story”, “Wind River”) generated box office receipts of EUR25.3 million (source: *Cinetel, Mymovies*), compared to EUR41.7 million in the full year 2017. Consequently, we have upgraded our top line estimates for 2018 and 2019 and also EBITDA has been increased by 5% on average in 2018-19 leading to an average increase of net result forecasts for 2018-19 of around 10%.

Figure 7 – Old vs. New estimates

(EURm)	2017A	2018E		2019E		2020E
		Old	New	Old	New	New
Total Sales	105.8	111.2	117.6	118.1	125.3	131.7
% change			5.8%		6.1%	
EBITDA	29.4	40.9	42.4	39.9	42.3	44.6
% change			3.7%		6.0%	
EBIT	5.4	12.1	13.3	11.5	13.1	14.8
% change			10.5%		14.4%	
Net Profit	3.9	6.7	7.3	6.9	7.4	8.7
% change			8.7%		7.1%	
Net Debt/(Cash)	40.5	46.2	43.0	37.1	35.1	24.0
EBIT margin	5.1%	10.9%	11.3%	9.7%	10.5%	11.2%
EBITDA margin	27.8%	36.7%	36.0%	33.8%	33.8%	33.9%

Source: Company data, UBI Banca estimates

Valuation

- > Given the revisions to our forecasts, our DCF valuation has increased to EUR7.88 per share (from EUR7.52) and our relative valuation to EUR7.36 per share from EUR6.56 per share. The simple average of our DCF and the relative valuation gives a fair value of EUR7.62. 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 EUR6.86 per share (vs. EUR6.34 before) offering >35% upside. The 10% discount we apply could diminish when the company is listed on the MTA.
- > LFG's current market capitalization (EUR71 million) is below its net invested capital (EUR77 million at Dec-17), which implies that LFG may not be able to create value in the future. We believe this scenario is highly unlikely given the wide line-up of the company and the growing EBITDA expected for 2018-20.
- > At our EUR6.86 per share target price, LFG would trade at 10.0x 2019 EV/EBIT, which is below the average multiple of our sample of peers (11.6x).

Figure 8 – Valuation summary

(EUR)		Weight	4 February 18	Delta
DCF Valuation	7.88	50.0%	7.52	4.8%
Relative Valuation	7.36	50.0%	6.56	12.2%
Fair Value	7.62		7.04	8.3%
Liquidity discount (10%)	(0.76)		(0.70)	8.3%
Target price	6.86		6.34	8.3%
Current price	5.05		4.64	8.8%
Potential upside	35.8%		36.6%	

Source: UBI Banca estimates

Figure 9 – DCF Valuation

Our DCF valuation implies 4.0x EV/EBITDA at terminal value.

(EURm)	(EUR m)	(% weight)
Sum of PV 2018-26 FCF	84.5	56%
Terminal value	67.4	44%
Total Enterprise value	152.0	100%
- minorities	0.0	
- Pension Provision	(0.3)	
- Net debt (+ cash)	(40.5)	
Total Equity value	111.1	
Fully diluted number of shares (m)	14.1	
Fair value per share (EUR)	7.88	

Source: UBI Banca estimates

Figure 10 – Peer comparison and valuation based on multiples (priced on 12 February 2018)

Company	Market Cap (EURm)	P/E		EV/EBITDA		EV/EBIT	
		2018E	2019E	2018E	2019E	2018E	2019E
EuropaCorp SA	100			5.4 x	4.9 x		
Splendid Medien AG	13	6.6 x	5.6 x	1.2 x	1.2 x	8.5 x	6.6 x
Lions Gate	4,457	54.6 x	32.9 x	12.2 x	10.3 x	20.7 x	16.5 x
Entertainment One Ltd.	1,495	11.9 x	10.5 x	8.7 x	8.1 x	8.9 x	8.3 x
Constantin Medien AG	196	52.3 x	34.8 x	22.5 x	16.8 x	56.2 x	29.2 x
Lucisano Media Group	32	7.8 x	3.2 x	4.3 x	2.5 x	8.9 x	4.4 x
Notorious Pictures	29	12.3 x	10.0 x	2.6 x	2.2 x	6.6 x	4.8 x
Average		24.2 x	16.2 x	8.1 x	6.6 x	18.3 x	11.6 x
Median		12.3 x	10.3 x	5.4 x	4.9 x	8.9 x	7.5 x
Current market multiples	71	15.5 x	9.7 x	3.4 x	2.7 x	18.7 x	8.6 x
Discount to Average		-36.0%	-39.9%	-57.5%	-58.9%	2.2%	-26.2%

Source: Factset, UBI Banca estimates

Figure 11 – Implicit multiples based on our EUR6.86 target price

(x)	2018E	2019E	2020E
P/E	12.9 x	12.8 x	11.2 x
EV/EBITDA	3.3 x	3.1 x	2.8 x
EV/EBIT	10.4 x	10.0 x	8.3 x
EV/Sales	1.10 x	0.97 x	0.84 x
P/BV	2.2 x	2.0 x	1.8 x
EV/ Capital employed	1.6 x	1.6 x	1.5 x

Source: UBI Banca estimates

Income Statement

(EURm)	2017	2018E	2019E	2020E
Value of production	117.21	129.36	136.61	144.88
EBITDA	29.42	42.38	42.33	44.62
EBITDA margin	25.1%	32.8%	31.0%	30.8%
EBIT	5.42	13.34	13.14	14.77
EBIT margin	4.6%	10.3%	9.6%	10.2%
Net financial income /expense	-2.92	-2.43	-2.08	-1.81
Associates & Others	0.00	0.00	0.00	0.00
Profit before taxes	2.50	10.91	11.06	12.96
Taxes	1.40	-3.60	-3.65	-4.28
Minorities & discontinuing ops	0.00	0.00	0.00	0.00
Net Income	3.90	7.31	7.41	8.68

Source: Company data, UBI Banca estimates

Balance Sheet

(EURm)	2017	2018E	2019E	2020E
Net working capital	1.42	1.81	1.93	2.03
Net Fixed assets	75.70	85.26	82.68	77.80
M/L term funds	-0.79	-0.93	-1.08	-1.59
Capital employed	76.33	86.14	83.53	78.24
Shareholders' equity	35.79	43.10	48.39	54.26
Minorities	0.00	0.00	0.00	0.00
Shareholders' funds	35.79	43.10	48.39	54.26
Net financial debt/(cash)	40.54	43.04	35.14	23.98

Source: Company data, UBI Banca estimates

Cash Flow Statement

(EURm)	2017	2018E	2019E	2020E
NFP Beginning of Period	32.29	40.54	43.04	35.14
Group Net Profit	3.90	7.31	7.41	8.68
Minorities	0.00	0.00	0.00	0.00
D&A	24.00	29.04	29.19	29.85
Change in Funds & TFR	0.00	0.00	0.00	0.00
Gross Cash Flow	27.90	36.35	36.60	38.53
Change In Working Capital	1.20	-0.39	-0.12	-0.10
Other	0.00	0.00	0.00	0.00
Operating Cash Flow	29.10	35.96	36.48	38.43
Net Capex	-33.63	-36.00	-24.00	-22.00
Other Investments	0.00	0.00	0.00	0.00
Free Cash Flow	-4.53	-0.04	12.48	16.43
Dividends Paid	-1.26	0.00	-2.11	-2.82
Other & Chg in Consolid. Area	-2.46	-2.46	-2.46	-2.46
Chg in Net Worth & Capital Incr.	0.00	0.00	0.00	0.00
Change in NFP	-8.25	-2.50	7.90	11.16
NFP End of Period	40.54	43.04	35.14	23.98

Source: Company data, UBI Banca estimates

Financial Ratios

(%)	2017	2018E	2019E	2020E
ROE	10.9%	17.0%	15.3%	16.0%
ROI	5.1%	11.1%	10.4%	12.2%
Net Fin. Debt/Equity (x)	1.1	1.0	0.7	0.4
Net Fin. Debt/EBITDA (x)	1.4	1.0	0.8	0.5
Interest Coverage	1.9	5.5	6.3	8.2
NWC/Sales	1.2%	1.4%	1.4%	1.4%
Capex/Sales	28.7%	27.8%	17.6%	15.2%
Pay Out Ratio	0.0%	28.9%	38.1%	32.5%

Source: Company data, UBI Banca estimates

Per Share Data

(EUR)	2017	2018E	2019E	2020E
EPS	0.28	0.52	0.53	0.62
DPS	0.00	0.15	0.20	0.00
Op. CFPS	2.07	2.55	2.59	2.73
Free CFPS	-0.32	0.00	0.89	1.17
BVPS	2.54	3.06	3.43	3.85

Source: Company data, UBI Banca estimates

Stock Market Ratios

(x)	2017 *	2018E	2019E	2020E
P/E	15.5	9.7	9.6	8.2
P/OpCFPS	2.1	2.0	2.0	1.9
P/BV	1.7	1.7	1.5	1.3
Dividend Yield (%)	0.0%	3.0%	4.0%	4.0%
Free Cash Flow Yield (%)	-7.5%	nm	17.5%	23.1%
EV (EURm)	101.44	114.61	106.73	95.60
EV/Sales	0.9	0.9	0.8	0.7
EV/EBITDA	3.4	2.7	2.5	2.1
EV/EBIT	18.7	8.6	8.1	6.5
EV/Capital Employed	1.3	1.3	1.3	1.2

Source: Company data, UBI Banca estimates

* Based on 2017 average price

Growth Rates

(%)	2017	2018E	2019E	2020E
Growth Group Net Sales	96.1%	10.4%	5.6%	6.1%
Growth EBITDA	25.1%	44.0%	-0.1%	5.4%
Growth EBIT	83.0%	146.1%	-1.5%	12.4%
Growth Net Profit	114.7%	87.3%	1.3%	17.2%

Source: Company data, UBI Banca estimates

Disclaimer

Analyst Declaration

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Equity rating dispersion in the past 12 months

Buy	Hold	Sell	No Rating
81.6%	10.5%	0.0%	7.9%

Proportion on issuers to which UBI Banca has supplied investment banking services relating to the last 12 months

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

For further information regarding yearly and quarterly rating statistics and descriptions, please refer to www.ubibanca.com/equity-research.

Historical ratings and target prices

Date	Rating	Target Price (EUR)	Market Price (EUR)
10 May 2017	Buy	5.16	4.64
4 October 2017	Buy	5.55	5.00
14 February 2018	Buy	6.34	5.55