

13 October 2016

Consumer Cyclical | Entertainment

## Spackman Entertainment Group

**Buy**

Target Price: SGD0.22  
 Price: SGD0.11  
 Market Cap: USD33.6m  
 Bloomberg Ticker: SEG SP

### A Hallyu Star At Its Inflection Point

We initiate coverage on Spackman, a top-tier South Korean movie producer with a BUY and a TP of SGD0.22, based on a 15x FY17F P/E. The group, probably in the best health since its IPO, is primed for a strong turnaround due to a few key near-term catalysts:

1. Its upcoming movie, *Master*, to be released in December;
2. A 27.2% share stake in SMG likely worth ~USD45m;
3. It can sell SMG to raise cash for special dividends/share buybacks;
4. Divestment of loss-making Opus Pictures cuts SG&A costs by 70%.

**Potential blockbuster movie, *Master*, to turn Spackman Entertainment Group (Spackman) profitable.** *Master* – a crime action drama starring A-list actors Gang Dong-won, Lee Byung-hun and Kim Woo-bin – hits cinema screens in December. The first trailer for *Master* generated a remarkable interest from viewers when it was released over the recent holidays in South Korea. Our expectation of 7.5m in ticket sales would yield Spackman profits of USD5.6m and bring it back into the black.

**Spackman Media Group (SMG) a hidden gem.** Spackman owns 27.2% of SMG, the largest entertainment talent agency in South Korea. SMG manages >60 artistes, including A-listers such as Son Ye-Jin, Song Hye Kyo and Yoo Ah-in. We estimate Spackman's stake in SMG to be worth ~USD45m which is higher than its current market cap from a peer comparison, coupled with recent deals completed. Cash raised from any stake sale of SMG shares to potential content provider partners could likely be used to fund movies in FY17, as well as share buy-backs or a potential special dividend.

**Loss-making Opus Pictures LLC divested, SG&A costs cut by ~70%.** With the divestment of loss-making Opus Pictures significantly reducing the SG&A costs, this event would likely be an additional drive to bounce Spackman back into profitability. Its other production house, Zip Cinema Co Ltd, has a good track record and aims to make 1-2 movies pa which, coupled with Spackman's joint ventures to make additional movies, could spur the growth going forward.

**Significant Chinese interest and potential partnerships.** Chinese firms sank >USD870m in South Korean content providers in 2010-2015. These include behemoths Dalian Wanda Group, Alibaba and Huayi Brothers Media Corp (Huayi Brothers). This strong interest is likely to pave the way for more partnerships/collaborations for Spackman, like the one with Alibaba Pictures.

**Trading at a huge discount to peers.** Spackman's overseas peers are trading at an average of 46x, while local peers are trading at a 32x average. The counter is currently trading at just 7.5x FY17F P/E. We initiate coverage with a BUY call and a SGD0.22 TP derived through a 15x FY17F P/E multiple.

**Key risks:** Lack of earnings visibility due to the inherent nature of the business; for more description of key risks, see page 12.

#### Share Data

|                              |             |
|------------------------------|-------------|
| Avg Daily Turnover (SGD/USD) | 2.05m/1.51m |
| 52-wk Price low/high (SGD)   | 0.05 - 0.16 |
| Free Float (%)               | 27          |
| Shares outstanding (m)       | 399         |
| Estimated Return             | 95%         |

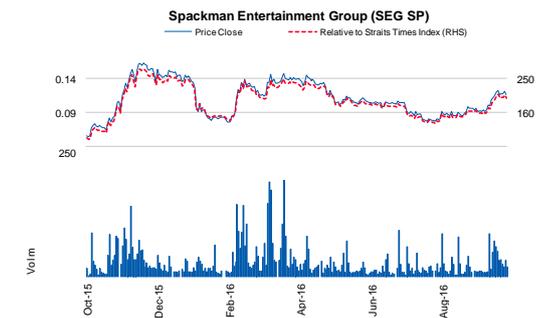
#### Shareholders (%)

|                                    |      |
|------------------------------------|------|
| Spackman Equities Group            | 38.8 |
| Lee Yoo Jin                        | 5.8  |
| Havenport Asset Management Ptd Ltd | 3.6  |

#### Share Performance (%)

|          | YTD    | 1m   | 3m   | 6m     | 12m   |
|----------|--------|------|------|--------|-------|
| Absolute | (20.0) | 20.8 | 10.5 | (16.6) | 114.8 |
| Relative | (19.1) | 21.4 | 11.2 | (18.3) | 119.6 |

Source: Bloomberg



Source: Bloomberg

#### Spackman's Top 3 movies and artistes



Source: Korean Film Biz Zone (KoBiz)

| Forecasts and Valuations        | Dec-13   | Dec-14   | Dec-15   | Dec-16F  | Dec-17F  |
|---------------------------------|----------|----------|----------|----------|----------|
| Total turnover (USDm)           | 11.9     | 15.6     | 17.8     | 21.0     | 35.5     |
| Reported net profit (USDm)      | 2.61     | (8.08)   | (1.27)   | 0.55     | 4.47     |
| Recurring net profit (USDm)     | 2.61     | (8.08)   | (1.62)   | 0.55     | 4.47     |
| Recurring net profit growth (%) | 0.0      | (410.0)  | (80.0)   | 0.0      | 714.8    |
| Recurring EPS (USD)             | 0.01     | (0.02)   | (0.00)   | 0.00     | 0.01     |
| DPS (USD)                       | na       | na       | na       | 0.000    | 0.003    |
| Recurring P/E (x)               | 12.8     | na       | na       | 61.2     | 7.5      |
| P/B (x)                         | 3.72     | 2.07     | 2.23     | 2.17     | 1.81     |
| P/CF (x)                        | 8.2      | na       | na       | 4.0      | 10.9     |
| Dividend Yield (%)              | na       | na       | na       | 0.5      | 4.0      |
| EV/EBITDA (x)                   | 7.1      | na       | na       | 15.3     | 3.0      |
| Return on average equity (%)    | 40.8     | (64.3)   | (8.1)    | 3.6      | 26.3     |
| Net debt to equity              | net cash |
| Our vs consensus EPS (adjusted) |          |          |          |          |          |

Source: Company data, RHB

#### Analyst

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## Financial Exhibits

Financial model updated on: 2016-09-30.

|                                                                                                                                                                                                                                                                                                                |                                     |               |               |               |                |                |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------|---------------|---------------|---------------|----------------|----------------|
| Asia                                                                                                                                                                                                                                                                                                           | <b>Financial summary</b>            | <b>Dec-13</b> | <b>Dec-14</b> | <b>Dec-15</b> | <b>Dec-16F</b> | <b>Dec-17F</b> |
| Singapore                                                                                                                                                                                                                                                                                                      | Recurring EPS (USD)                 | 0.01          | (0.02)        | (0.00)        | 0.00           | 0.01           |
| Consumer Cyclical                                                                                                                                                                                                                                                                                              | EPS (USD)                           | 0.01          | (0.02)        | (0.00)        | 0.00           | 0.01           |
| <b>Spackman</b>                                                                                                                                                                                                                                                                                                | DPS (USD)                           | 0.000         | 0.000         | 0.000         | 0.000          | 0.003          |
| Bloomberg                                                                                                                                                                                                                                                                                                      | BVPS (USD)                          | 0.02          | 0.04          | 0.04          | 0.04           | 0.05           |
| SEG SP                                                                                                                                                                                                                                                                                                         | Weighted avg adjusted shares (m)    | 395           | 399           | 399           | 399            | 399            |
| <b>Buy</b>                                                                                                                                                                                                                                                                                                     |                                     |               |               |               |                |                |
| <b>Valuation basis</b>                                                                                                                                                                                                                                                                                         | <b>Valuation metrics</b>            | <b>Dec-13</b> | <b>Dec-14</b> | <b>Dec-15</b> | <b>Dec-16F</b> | <b>Dec-17F</b> |
| 15x FY17F P/E.                                                                                                                                                                                                                                                                                                 | Recurring P/E (x)                   | 12.8          | na            | na            | 61.2           | 7.5            |
|                                                                                                                                                                                                                                                                                                                | P/E (x)                             | 12.8          | na            | na            | 61.2           | 7.5            |
| <b>Key drivers</b>                                                                                                                                                                                                                                                                                             | P/B (x)                             | 3.72          | 2.07          | 2.23          | 2.17           | 1.81           |
| Success on upcoming movies, partnership deals.                                                                                                                                                                                                                                                                 | FCF Yield (%)                       | 12.0          | (36.1)        | (57.6)        | 22.1           | 6.2            |
|                                                                                                                                                                                                                                                                                                                | Dividend Yield (%)                  | 0.0           | 0.0           | 0.0           | 0.5            | 4.0            |
| <b>Key risks</b>                                                                                                                                                                                                                                                                                               | EV/EBITDA (x)                       | 7.1           | na            | na            | 15.3           | 3.0            |
| reception of movies produced directly linking to ticket sales.                                                                                                                                                                                                                                                 | EV/EBIT (x)                         | 7.2           | na            | na            | 18.4           | 3.2            |
|                                                                                                                                                                                                                                                                                                                |                                     |               |               |               |                |                |
| <b>Company Profile</b>                                                                                                                                                                                                                                                                                         | <b>Income statement (USDm)</b>      | <b>Dec-13</b> | <b>Dec-14</b> | <b>Dec-15</b> | <b>Dec-16F</b> | <b>Dec-17F</b> |
| Spackman Entertainment Group's businesses span theatrical motion pictures, documentaries, talent management as well as studio photography. With three film production labels at the core operations of the business, the company is primarily involved in producing, presenting and distributing motion films. | Total turnover                      | 11.9          | 15.6          | 17.8          | 21.0           | 35.5           |
|                                                                                                                                                                                                                                                                                                                | Gross profit                        | 5.5           | 0.0           | 7.8           | 6.7            | 8.0            |
|                                                                                                                                                                                                                                                                                                                | EBITDA                              | 3.5           | (7.3)         | (0.9)         | 1.2            | 6.1            |
|                                                                                                                                                                                                                                                                                                                | Depreciation and amortisation       | (0.1)         | (0.1)         | (0.1)         | (0.2)          | (0.2)          |
|                                                                                                                                                                                                                                                                                                                | Operating profit                    | 3.4           | (7.4)         | (1.0)         | 1.0            | 5.8            |
|                                                                                                                                                                                                                                                                                                                | Net interest                        | (0.1)         | (0.1)         | (0.1)         | (0.4)          | (0.4)          |
|                                                                                                                                                                                                                                                                                                                | Exceptional income - net            | 0.0           | 0.0           | 0.2           | 0.0            | 0.0            |
|                                                                                                                                                                                                                                                                                                                | Pre-tax profit                      | 3.2           | (7.5)         | (0.9)         | 0.7            | 5.4            |
|                                                                                                                                                                                                                                                                                                                | Taxation                            | (0.6)         | (0.6)         | (0.4)         | (0.1)          | (1.0)          |
|                                                                                                                                                                                                                                                                                                                | Recurring net profit                | 2.6           | (8.1)         | (1.6)         | 0.5            | 4.5            |
|                                                                                                                                                                                                                                                                                                                |                                     |               |               |               |                |                |
|                                                                                                                                                                                                                                                                                                                | <b>Cash flow (USDm)</b>             | <b>Dec-13</b> | <b>Dec-14</b> | <b>Dec-15</b> | <b>Dec-16F</b> | <b>Dec-17F</b> |
|                                                                                                                                                                                                                                                                                                                | Change in working capital           | 1.25          | (4.16)        | (19.66)       | 7.30           | (1.98)         |
|                                                                                                                                                                                                                                                                                                                | Cash flow from operations           | 4.04          | (11.80)       | (16.56)       | 8.41           | 3.09           |
|                                                                                                                                                                                                                                                                                                                | Capex                               | (0.04)        | (0.31)        | (2.78)        | (1.00)         | (1.00)         |
|                                                                                                                                                                                                                                                                                                                | Cash flow from investing activities | (3.44)        | (0.67)        | (7.90)        | (1.00)         | (1.00)         |
|                                                                                                                                                                                                                                                                                                                | Proceeds from issue of shares       | 3.74          | 14.14         | 0.00          | 0.00           | 0.00           |
|                                                                                                                                                                                                                                                                                                                | Dividends paid                      | 0.00          | 0.00          | 0.00          | (0.16)         | (1.34)         |
|                                                                                                                                                                                                                                                                                                                | Cash flow from financing activities | 5.26          | 15.72         | 16.73         | (0.52)         | (1.70)         |
|                                                                                                                                                                                                                                                                                                                | Cash at beginning of period         | 3.32          | 9.21          | 12.18         | 4.11           | 11.00          |
|                                                                                                                                                                                                                                                                                                                | Net change in cash                  | 5.85          | 3.25          | (7.73)        | 6.89           | 0.39           |
|                                                                                                                                                                                                                                                                                                                | Ending balance cash                 | 9.21          | 12.18         | 4.11          | 11.00          | 11.39          |
|                                                                                                                                                                                                                                                                                                                |                                     |               |               |               |                |                |
|                                                                                                                                                                                                                                                                                                                | <b>Balance sheet (USDm)</b>         | <b>Dec-13</b> | <b>Dec-14</b> | <b>Dec-15</b> | <b>Dec-16F</b> | <b>Dec-17F</b> |
|                                                                                                                                                                                                                                                                                                                | Total cash and equivalents          | 11.5          | 15.7          | 11.0          | 17.9           | 18.3           |
|                                                                                                                                                                                                                                                                                                                | Tangible fixed assets               | 0.7           | 0.9           | 3.3           | 4.1            | 4.9            |
|                                                                                                                                                                                                                                                                                                                | Intangible assets                   | 0.1           | 3.4           | 0.8           | 0.8            | 0.8            |
|                                                                                                                                                                                                                                                                                                                | Total investments                   | 0.0           | 0.0           | 3.6           | 3.6            | 3.6            |
|                                                                                                                                                                                                                                                                                                                | Total other assets                  | 5.5           | 2.0           | 1.8           | 1.8            | 1.8            |
|                                                                                                                                                                                                                                                                                                                | Total assets                        | 25.8          | 31.9          | 57.3          | 56.3           | 72.6           |
|                                                                                                                                                                                                                                                                                                                | Short-term debt                     | 1.3           | 1.2           | 3.1           | 3.1            | 3.1            |
|                                                                                                                                                                                                                                                                                                                | Total long-term debt                | 1.3           | 0.0           | 2.0           | 2.0            | 2.0            |
|                                                                                                                                                                                                                                                                                                                | Other liabilities                   | 0.0           | 0.0           | 0.0           | 0.0            | 0.0            |
|                                                                                                                                                                                                                                                                                                                | Total liabilities                   | 16.8          | 14.6          | 40.6          | 39.3           | 52.4           |
|                                                                                                                                                                                                                                                                                                                | Shareholders' equity                | 8.9           | 16.2          | 15.1          | 15.4           | 18.6           |
|                                                                                                                                                                                                                                                                                                                | Minority interests                  | 0.0           | 1.1           | 1.6           | 1.6            | 1.6            |
|                                                                                                                                                                                                                                                                                                                | Total equity                        | 9.0           | 17.3          | 16.7          | 17.1           | 20.2           |
|                                                                                                                                                                                                                                                                                                                | Net debt                            | (9.0)         | (14.4)        | (5.9)         | (12.8)         | (13.2)         |
|                                                                                                                                                                                                                                                                                                                | Total liabilities & equity          | 25.8          | 31.9          | 57.3          | 56.3           | 72.6           |
|                                                                                                                                                                                                                                                                                                                |                                     |               |               |               |                |                |
|                                                                                                                                                                                                                                                                                                                | <b>Key metrics</b>                  | <b>Dec-13</b> | <b>Dec-14</b> | <b>Dec-15</b> | <b>Dec-16F</b> | <b>Dec-17F</b> |
|                                                                                                                                                                                                                                                                                                                | Revenue growth (%)                  | 170.1         | 31.2          | 13.9          | 18.4           | 68.9           |
|                                                                                                                                                                                                                                                                                                                | Recurrent EPS growth (%)            | 0.0           | (407.3)       | (80.0)        | 0.0            | 714.8          |
|                                                                                                                                                                                                                                                                                                                | Gross margin (%)                    | 46.6          | 0.3           | 44.1          | 31.8           | 22.6           |
|                                                                                                                                                                                                                                                                                                                | Operating EBITDA margin (%)         | 29.0          | (46.9)        | (5.1)         | 5.8            | 17.0           |
|                                                                                                                                                                                                                                                                                                                | Net profit margin (%)               | 21.9          | (51.8)        | (7.2)         | 2.6            | 12.6           |
|                                                                                                                                                                                                                                                                                                                | Capex/sales (%)                     | 0.4           | 2.0           | 15.7          | 4.8            | 2.8            |
|                                                                                                                                                                                                                                                                                                                | Interest cover (x)                  | 24.7          | (70.7)        | (13.7)        | 2.9            | 16.3           |

Source: Company data, RHB

## Investment Merits

**Movie-maker turning around with the disposal of loss-making production arm.** In August, Spackman disposed 100% of its equity interest in loss-making Opus Pictures. This ought to greatly reduce fixed overheads and opex by about 70%. As announced by the group, the full-year impact of the disposal is likely to net a NPAT difference of about USD2m for FY16, which would turn Spackman profitable.

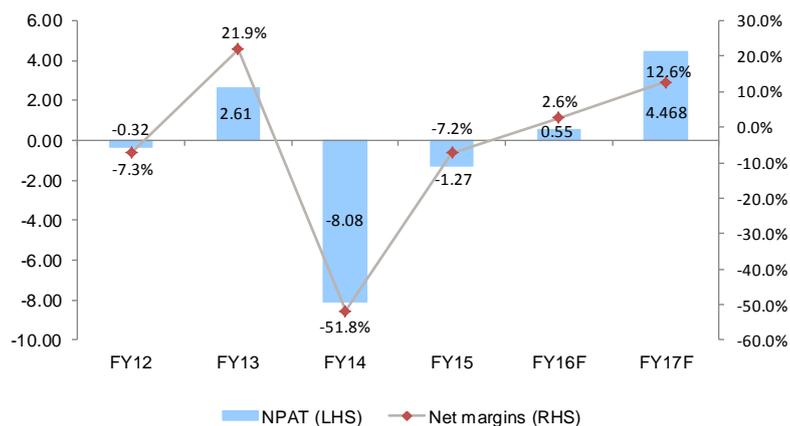
In addition, the loss-making Opus Pictures recorded an aggregate loss of KRW10.7bn (USD9m), with a negative 50% rate of return to investors for the six films it has produced since FY14.

With a much lower operating cost structure, coupled by a stronger track record held by its other production arm Zip Cinema, we believe that Spackman's 2H16 is likely to be a profitable period. In addition, *Master*, produced by Zip Cinema (which also filmed the hit movie *The Priests*), is also set to be released in December.

All in all, we expect Spackman to return to the black by the end of FY16. It should do even better in FY17. This is with the full cost savings from the Opus Pictures disposal booked, coupled with the launch of more new movies during the same period.

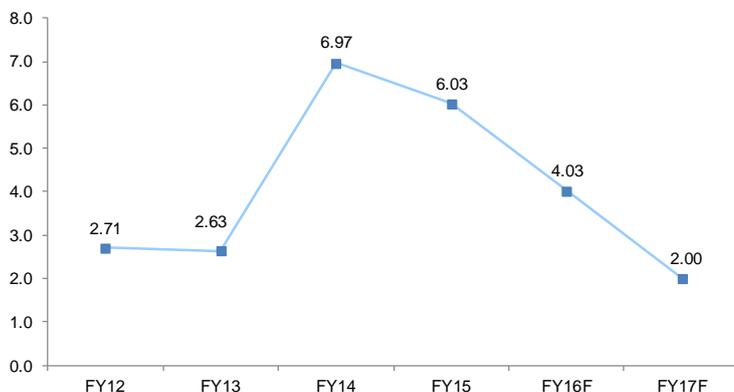
Based on our estimates, we believe that the addition of *Master* and *Life Risking Romance* into Spackman's portfolio of movies ought to yield a positive NPAT of USD870,000 and USD4.53m in FY16 and FY17 respectively. The estimates are being offset by loss-making movies, ie *Musudan* and *Chasing*, which are both being distributed by Opus Pictures. NPMs are also set to improve and turn positive.

Figure 1: Spackman's net profits and net margins



Source: Company data, RHB

Figure 2: Spackman's selling and administrative expenses



Source: Company data, RHB

Figure 3: Opus Pictures' past productions

|                                               | <i>For The Emperor</i> | <i>Confession</i> | <i>Big Match</i> | <i>Wonders</i> | <i>Chasing</i> | <i>Musudan</i> | Total         |
|-----------------------------------------------|------------------------|-------------------|------------------|----------------|----------------|----------------|---------------|
| Producer                                      | Opus Pictures          | Opus Pictures     | BK Pictures      | TPS Company    | The Queen D&M  | Golden Tide    |               |
| Presenter                                     | Opus Pictures          | United Pictures   | Opus Pictures    | Opus Pictures  | Opus Pictures  | Opus Pictures  |               |
| Distributor                                   | United Pictures        | CJ E&M            | NEW              | Opus Pictures  | Opus Pictures  | Opus Pictures  |               |
| Date of release                               | 11 Jun 2014            | 10 Jun 2014       | 27 Nov 2014      | 2 Apr 2015     | 7 Jan 2016     | 3 Mar 2016     |               |
| <b>Project Total Revenue (KRWbn) (A)</b>      | <b>3.84</b>            | <b>2.18</b>       | <b>5.26</b>      | <b>0.21</b>    | <b>0.55</b>    | <b>0.39</b>    | <b>12.43</b>  |
| Total Production cost (KRW bn) (B)            | 4.03                   | 4.61              | 8                | 0.43           | 2.1            | 2.2            | 21.37         |
| Total Distribution expenses (KRW Bn) (C)      | 0.35                   | 0.33              | 0.87             | 0.03           | 0.08           | 0.08           | 1.74          |
| <b>Total Cost (D = B + C)</b>                 | <b>4.38</b>            | <b>4.94</b>       | <b>8.87</b>      | <b>0.46</b>    | <b>2.18</b>    | <b>2.28</b>    | <b>23.11</b>  |
| <b>Loss from films (KRWbn) (A - D)</b>        | <b>-0.54</b>           | <b>-2.76</b>      | <b>-3.61</b>     | <b>-0.25</b>   | <b>-1.63</b>   | <b>-1.89</b>   | <b>-10.68</b> |
| <b>Rate of return from film (KRWbn) (D/B)</b> | <b>-13%</b>            | <b>-60%</b>       | <b>-45%</b>      | <b>-58%</b>    | <b>-78%</b>    | <b>-86%</b>    | <b>-50%</b>   |

Source: Company data, RHB

**World-class South Korean movie producer with a proven track record.** Spackman has produced many movie blockbusters. Its early successes were attributed to top-grossing movies such as *Woochi*. The latter sold over 6.1m tickets (gross revenue of USD40.5m) at the South Korean box office.

Another early hit was *All About My Wife*, which opened at the top of the South Korean box office when it was released in May 2012. The firm sold 4.6m tickets, which amounted to approximately USD31.4m in gross revenue and offered a rate of return of approximately 128% to investors.

The firm's most recent hit was *The Priests*, which opened at No. 1 at the domestic box office and sold over 5.4m tickets (gross revenue of USD38m). It had a high rate of 78% return to investors. An upcoming movie, *Master*, is to feature some of Korea's top artistes, namely Gang Dong-won, Lee Byung-hun and Kim Woo-bin. *Master* is set to be released in December.

Over the years, Spackman has proven that it can deliver world-class entertainment, as evidenced by its portfolio of movies.

Figure 4: Spackman's portfolio of past productions

| Title                    | Release    | Producer   | Presenter                      | Gross revenue (USDm) | Cost of production (m) | Net profit (m) | Rate of return to investors (%) |
|--------------------------|------------|------------|--------------------------------|----------------------|------------------------|----------------|---------------------------------|
| <i>The Priests</i>       | 5/11/2015  | Zip cinema | United Pictures                | 38                   | 5.9                    | 32.1           | 78%                             |
| <i>Cold Eyes</i>         | 3/7/2013   | Zip cinema | Next Entertainment World (NEW) | 36.1                 | 6.2                    | 29.9           | 89%                             |
| <i>All About My Wife</i> | 17/5/2012  | Zip cinema | United Pictures                | 31.4                 | 4.4                    | 27             | 128%                            |
| <i>Haunters</i>          | 10/11/2011 | Zip cinema | United Pictures                | 14.1                 | 5                      | 9.1            | 24%                             |
| <i>Woochi</i>            | 23/12/2009 | Zip cinema | CJ Entertainment               | 40.5                 | 14                     | 26.5           | 13%                             |
| <i>Closer To Heaven</i>  | 24/9/2009  | Zip cinema | CJ Entertainment               | 14.3                 | 5.1                    | 9.2            | 16%                             |

Source: Company data, RHB

Figure 5: Movie posters of past productions



Source: Company data

The upcoming movie *Master* is set to be the key catalyst. We conducted a scenario analysis for *Master* to paint a clearer picture of what revenue contributions can be expected in FY17 (Figure 6). The movie is set to be released in end-2016, and features some of South Korea's biggest movie stars. Following the success of *The Priests*, our estimates show that base case tickets sold are at 7.5m, yielding gross sales of approximately USD51.4m. Of this, USD16.7m is to be booked as revenue for Spackman. The group's net profit after deduction of cost of production would be USD5.6m.

In the worst case scenario, *Master* may sell 5m tickets. Even at that level, Spackman is still able to yield a positive net profit of USD2.3m. In our best case scenario, we expect 10m tickets to be sold. This would imply record-breaking sales if the film is able to reach that target. At this level, gross sales would amount to USD68.5m, of which USD20.1m would go to Spackman as revenue (implying earnings of USD9m).

Given the unpredictability of the movie industry, the success of a film ultimately depends on the taste and preferences of the audience. This is almost impossible to forecast. However, with Spackman's proven track record of movies, coupled with a talented cast and a renowned movie producer, we expect *Master* to minimally hit the base case estimates. In turn, this would contribute significantly to the group's FY17 NPAT.

Figure 6: Scenario analysis for *Master*

|       | Ticket sales (m) | Gross sales (USDm) | Spackman's revenue (USDm) | Spackman's costs (USDm) | Spackman's net profit (USDm) |
|-------|------------------|--------------------|---------------------------|-------------------------|------------------------------|
| Worst | 5.0              | 34.3               | 13.4                      | 11.1                    | 2.3                          |
| Base  | 7.5              | 51.4               | 16.7                      | 11.1                    | 5.6                          |
| Best  | 10.0             | 68.5               | 20.1                      | 11.1                    | 9                            |

Source: RHB

Figure 7: *Master* features Gang Dong-won, Lee Byung-hun and Kim Woo-bin



|                                                                                                                                                                                                                                                                                                                                                                                                                                         |                                                                                                                                                                                                                                                                                                                                  |                                                                                                                                                                                                                                                                 |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><b>Lee Byung Hun</b><br/>CHAIRMAN JIN</p> <p>A notorious conman, smooth criminal protagonist.</p> <p>A charming, charismatic silver-tongued hustler who always gets a way out.</p> <p>President of the biggest fraud organization called ONE Network.</p> <p>A skilled scammer and meticulous planner, perfect networker for the largest scale fraud ever.</p> <p>Undoubtedly, the mastermind for a massive con, whatever it is.</p> | <p><b>Kang Dong Won</b><br/>KIM JAE MYUNG</p> <p>Experienced team leader of the intellectual crime investigative unit.</p> <p>An adventurous cool cop with strong stance against his enemies.</p> <p>A charismatic detective Highly determined and daring in solving hard cases.</p> <p>His mission to capture Chairman Jin.</p> | <p><b>Kim Woo Bin</b><br/>PARK JANG GUN</p> <p>The brain behind Chairman Jin and operations at ONE Network.</p> <p>Known as "Gen. Park," Chairman Jin's faithful and right-hand man.</p> <p>Loyal but later conflicted between the police or President Jin.</p> |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

Source: EverythingLBH.Com

**Stake in SMG worth approximately USD45m, ie more than its current market cap.** To paint a clearer picture on the valuations of what a Chinese company is willing to invest, we use the example of Sohu.com, a Chinese Internet firm. The latter invested in Keyeast, a company that manages and recruits new and top actors. This talent management agency represents a number of famous actors, including Kim Soo Hyun, Han Ji-hye, Kim Hyun Joong and Bae Yong Joon. It has a total of 44 artists with a P/E ratio of 140x. A total of USD15m was invested, making Sohu.com the second-largest shareholder with 6.4%.

Furthermore, as shown in the peer comparison below, talent management agencies in South Korea are trading at an average P/E of 56x. SMG is the largest talent management agency, with its stable of renowned top-tier artistes like Soo Ye-jin, Song Hye Kyo and Yoo Ah-in.

We believe that it should also trade at a premium, if not at a comparable level, despite being a private entity. We understand that Spackman's management is in talks to sell part of its stake to renowned overseas content providers for partnership purposes. We also understand that the group is likely to use the cash to fund projects in FY17, as well as engage in share buy-backs and dish out a potential special dividend. Spackman also has a healthy balance sheet and is presently in a net cash position

**Figure 8: Chinese companies' investing into talent management agencies**

| Acquirer                | Investment        | Market Value (USDm) | Stake | Amount (USDm) | Total artists |
|-------------------------|-------------------|---------------------|-------|---------------|---------------|
| DMG Entertainment China | Chorokbaem Media  | 84.1                | 25.6% | 21.5          | 13            |
| Huayi Brothers          | SIM Entertainment | 75.0                | 26.0% | 19.5          | 31            |
| Sohu.com                | Keyeast           | 234.4               | 6.4%  | 15            | 44            |

Source: Company data, RHB

**Figure 9: SMG's peers**

| SMG Peer Comparison             |                |               |               |                     |            |                 |             |  |
|---------------------------------|----------------|---------------|---------------|---------------------|------------|-----------------|-------------|--|
| Company name                    | Mkt Cap (SGDm) | P/E (30/9/16) | P/B (30/9/16) | Dvd Ind Yld - Gross | ROE        | Net Gearing (%) | Ex-cash P/E |  |
| Wilhelmina International Inc    | 68.9           | 35.7          | 1.7           | N/A                 | 5.1        | (16.4)          | 29.8        |  |
| eSun Holdings Limited           | 177.9          | 3.0           | 0.1           | N/A                 | 3.6        | 21.4            | N/A         |  |
| AMUSE Inc                       | 451.9          | 13.6          | 1.5           | 1.3                 | 11.1       | (73.0)          | 3.7         |  |
| Zhejiang Huace film & TV Co Ltd | 4,884.2        | 55.3          | 3.9           | 0.2                 | 10.7       | (19.0)          | 44.8        |  |
| Zhejiang Talent Television      | 2,132.1        | 89.1          | 12.0          | 0.1                 | 18.5       | (2.8)           | 86.6        |  |
| Keyeast Co Ltd                  | 269.8          | 140.3         | 4.0           | N/A                 | 3.2        | (47.0)          | 74.4        |  |
| IHQ Inc                         | 387.8          | N/A           | 1.4           | N/A                 | (0.6)      | (20.6)          | N/A         |  |
| Huayi Brothers Co Ltd           | 272.8          | N/A           | 4.7           | N/A                 | (23.5)     | (51.8)          | N/A         |  |
| Chorokbaem Media Co Ltd         | 177.4          | N/A           | 2.2           | N/A                 | (7.7)      | (9.5)           | N/A         |  |
| Imagine Asia Co Ltd             | 47.1           | N/A           | 1.7           | N/A                 | (3.1)      | 19.0            | N/A         |  |
| <b>Average</b>                  |                | <b>56.2</b>   | <b>3.3</b>    | <b>0.6</b>          | <b>1.7</b> | <b>(20.0)</b>   | <b>47.9</b> |  |

Source: RHB

**Largest talent management agency in South Korea.** Spackman has a 27.2% stake in SMG, a company incorporated in Hong Kong. Together with its subsidiaries, they form one of the largest entertainment talent agencies in South Korea in terms of the number of artistes under management through six renowned agencies (Figure 10).

**Figure 10: SMG's agencies**

| Talent agencies                        | Description                                                                                                                        |
|----------------------------------------|------------------------------------------------------------------------------------------------------------------------------------|
| MS Team Entertainment Co Ltd (MS Team) | MS Team represents three artistes including respected film stars Son Ye-jin, Lee Min-jung and Wi Ha-jun                            |
| UAA & Co Inc (UAA)                     | Manages two of the most recognised names, Song Hye Kyo and Yoo Ah-in                                                               |
| Fiftyone K Inc (Fiftyone K)            | Represents a total of five artistes, led by So Ji-seob                                                                             |
| UL Entertainment Co Ltd (UL)           | Newly-established by the company, currently has 19 artistes under management, including Kim Sung-soo, Jung Tae-woo and Hwang Bo-ra |
| SBD Entertainment (SBD)                | Manages and represents 20 artistes, including Bae Doo-na and Go Won-hee                                                            |
| Kook Entertainment Co Ltd (Kook)       | Represents a total of 12 artistes, including Kim Sang-kyung and Park Sun-young                                                     |

Source: Company

Spackman has managed to produce some of the top-tier award-winning artistes in South Korea, grooming and guiding them through their professional careers in many different areas.

The six artistes pictured below are just some of the popular names in the country's show business. Spackman does not only engage these artistes purely for acting purposes, but also invests and nurtures them so as to win their loyalty. The latter is an important aspect in the fragmented entertainment industry in South Korea.

**Figure 11: Soo Ye-jin**



Source: KoBiz

**Figure 12: Song Hye Kyo**



Source: KoBiz

**Figure 13: So Ji-sub**



Source: KoBiz

**Figure 14: Yoo Ah-in**



Source: KoBiz

**Figure 15: Bae Doo-na**



Source: KoBiz

**Figure 16: Lee Min-jung**



Source: KoBiz

**SMG artists provide an access for potential investment opportunities.** In August, MS Team Entertainment Co Ltd (MS Team) was the co-presenter of *The Last Princess*, which debuted on top of the South Korean box office and took in over KRW44.4bn in ticket sales (ie well over 5.6m admissions). This was made possible by the draw of the main cast, which include MS Team artiste Son Ye-jin.

With a stable of highly sought-after artistes under SMG's talent agencies, this could potentially provide tremendous opportunities for Spackman. This is as such actors could star in future blockbuster movies. Moving forward, we can expect SMG to take part in future content projects as well (Figure 17).

**Figure 17: Future content projects**

| Future Content Project          | Expected release date | Main cast under SMGL                                 |
|---------------------------------|-----------------------|------------------------------------------------------|
| <i>Those Guys</i>               | 1H17                  | So Ji Seob (Fiftyone K),<br>Lee Hyo-jae (Fiftyone K) |
| <i>The Heart To Tell Others</i> | 2018                  | So Ji Seob (Fiftyone K)                              |
| <i>Villa 401</i>                | 2H18                  | To be determined                                     |
| <i>Can't Help But Go Crazy</i>  | 1H17                  | To be determined                                     |
| <i>Masterpiece</i>              | 2H17                  | So Ji Seob (Fiftyone K)                              |

Source: Company

**Variety shows may potentially enhance Spackman's presence in the China.** SMG is establishing a division that produces and supplies variety shows and unscripted content to the broadcast, cable, digital and first-run syndication platforms. This division is to be led by the former production team of Delmedia Co Ltd, which was known for producing some of South Korea's top variety shows for Munhwa Broadcasting Corp (MBC) like *I Am a Singer*, *MBC Star Audition: The Great Birth* and *Infinite Girls*.

The division is to focus on developing and producing unscripted variety programmes for the Chinese market. This is given the increasing popularity of South Korean-style variety shows in China. Since 2015, the foundation has been laid with a collaborative agreement with a Chinese broadcasting network, Liaoning TV, for programmes such as *A Song For You* and *The Best Gift*.

Going forward, we can expect more collaborative projects with Chinese companies as Spackman expands its reach into the market there. Furthermore, following the success of high-grossing drama series *Descendants Of The Sun*, the Chinese market may anticipate the entry of more South Korean TV dramas. SMG is poised to leverage on this tremendous opportunity.

**Potential partnerships with giant Chinese peers.** Having a similar culture and social values could be possible reasons why South Korean content is naturally accepted by Chinese audiences. This, in turn, allows such content to smash record-breaking views.

*My Love From Another Star* is an example of a successful South Korean drama series in China. The drama series received well over 14.5bn views since its debut, with over 2m views daily. The most recent drama series that successfully broke into China was *Descendants Of The Sun*. The USD11m production costs incurred by Next World Entertainment (NEW) were quickly recouped due to the overwhelming response from China and other countries. In the former alone, it was reported that episodes of the drama were downloaded over 2bn times by Chinese viewers.

**Significant investments surging from China.** Over the past two years, there has been a significant increase in interest in South Korean companies. Across all sectors, Chinese investments in such firms rocketed 119% in 2015 to USD1.9bn, according to *Bloomberg*. South Korean content providers – specifically in the areas of entertainment, film and gaming – subsequently attracted investments from China of over USD870m between 2010 and 2015.

In 2011, China's investment into the South Korean entertainment industry stood at USD6m. This surged to USD86m in 2015, a staggering 1,333% increase.

Many of these Chinese companies include behemoths like Dalian Wanda, Alibaba and Huayi Brothers. The influx of Chinese investments into South Korea has resulted in inflating costs for distribution rights, potentially increasing the distribution revenue for South Korean entertainment companies.

**Figure 18: China's major investments into South Korea's entertainment industry**

| Investor                                     | Investment                     | Price (KRWbn) | Stake                      |
|----------------------------------------------|--------------------------------|---------------|----------------------------|
| Alibaba                                      | SM Entertainment               | 35.5          | Shareholder                |
| Hauche Media                                 | Next Entertainment World (NEW) | 53.5          | Second largest shareholder |
| Suning Universal                             | Redrover                       | 45.3          | Largest shareholder        |
| Suning Universal                             | FNC Entertainment              | 33.6          | Second largest shareholder |
| DMG Entertainment and Media                  | Chorokbaem                     | 25            | Largest shareholder        |
| Huayi Brothers                               | SIM Entertainment              | 22.8          | Largest shareholder        |
| Spearhead Integrated Marketing Communication | Signal Entertainment           | 21.4          | Largest shareholder        |

Source: Company data, RHB

With Chinese giants snapping up premium content providers with rich valuations, especially in South Korea, we think that Spackman – with its good track record and its current undervalued state – may likely be a target.

In July, Alibaba Pictures purchased the distribution rights for the film *Life Risking Romance* in China. This Spackman and Alibaba collaboration provides a clear path into the country to reach a wider audience. Previously, the firm's films were limited to only theatrical releases.

With the advent of the Internet, Spackman is now able to leverage on an integrated platform by combining both traditional theatre and the Internet to provide greater exposure for its films. The rise of online and mobile platforms in China is also set to benefit.

Figure 19: Alibaba Pictures (left) and *Life Risking Romance* (right)



Source: KoBiz

**Excellent filmmakers – Eugene Lee and Suk Young Jung.** Zip Cinema is a South Korean production film founded by veteran film producer Eugene Lee, who was named as one of the world’s “10 producers to watch” in 2007. Some of the successful movies produced by Ms Lee are *Woochi*, *Haunters* and *All About My Wife*. The latter of the three was a romantic comedy that opened at No. 1 at the domestic box office. It sold well over 4.6m tickets and grossed USD31.4m, becoming one of South Korea’s highest-grossing romantic comedies of all time.

On Nov 2015, Zip Cinema managed to produce yet another movie blockbuster *The Priests*. The film achieved a record-breaking performance by being the fastest movie to reach four million tickets at the local box office that month. Zip Cinema’s upcoming movie *Master*, which is set to be released in December, is expected to match the success of *The Priests*.

Novus Mediacorp Co Ltd, founded by Suk Young Jung, is a renowned investor, presenter and ancillary distributor for South Korean theatrical films. Since 2009, the group has been the investor, presenter or distributor for a total of 55 films, including box office hits *Secretly, Greatly* and *All About My Wife*. The two filmmakers have recorded reputable accolades over the years, spearheading successful projects, and ensuring success and quality in every film.

Figure 20: Eugene Lee

Figure 21: Suk Young Jung



Source: Company

Source: Company

Figure 22: Further details about filmmakers Lee and Suk

| Name           | Role                                                                   | Background                                                                                                                                                                                                                                                                                                 | Success                                                                                                                                                                                                                                                                                                                                        |
|----------------|------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Eugene Lee     | Chief producer at Spackman                                             | Was a marketing director with major South Korean film label Bom Film Productions and worked as an advertising executive with Korad Advertising, a leading advertising agency. She graduated with a Bachelor of Arts degree from Ehwa Women’s University                                                    | Produced some of South Korea’s biggest box office hits. This included: <ul style="list-style-type: none"> <li>• <i>Woochi</i> (6.1m tickets sold)</li> <li>• <i>Haunters</i> (2.1m tickets sold)</li> <li>• <i>All About My Wife</i> (4.6m tickets sold)</li> </ul> Lee was named one of the 10 <i>Producers To Watch</i> in the world in 2007 |
| Suk Young Jung | Founder and CEO of Novus Mediacorp, and executive director of Spackman | Former co-founder and executive director of Vantage Holdings – a leading South Korean film investment company. Vantage invested in <i>The Chaser</i> , the No. 2 box office hit in 2008. Suk graduated with a Bachelor of Arts from Pennsylvania State University in the US, where he majored in Economics | Suk distributed four of the Top 20 films of 2013 in South Korea: <ul style="list-style-type: none"> <li>• <i>Secretly, Greatly</i></li> <li>• <i>Friend: The Great Legacy</i></li> <li>• <i>Hope</i></li> <li>• <i>Very Ordinary Couple</i></li> </ul>                                                                                         |

Source: Company

## Valuation

### Peer comparison

**Trading at a significant discount to overseas peers.** Spackman's foreign peers are currently trading at an average of 46.6x while its local peers are trading at a 32.4x average. Due to the catalysts in place, we expect the group to turn around in FY17.

We have decided to ascribe 67% and 53% discounts to its foreign and local peers' averages respectively. This is due to Spackman's relatively smaller scale when compared with its foreign peers, as well as the high degree of uncertainty when it comes to the success of a movie.

As such, we arrive at a 15x FY17F P/E multiple for a premium South Korean movie producer. Despite such a huge discount to its local and listed peers, our SGD0.22 TP represents a potential upside of c.97% from its current trading price.

**More upside can be expected.** We can expect more upside with the sale of Spackman's stake in SMG, which is worth more than its current market cap. SMG's listing in Hong Kong would further increase the value of the group's holdings in its associate, if successful.

In addition, our FY17 estimates are premised on a conservative base case scenario for ticket sales. If Spackman's movies perform better, its NPAT could further increase significantly.

**Figure 23: Peers comparison**

| Company name                                              | Mkt Cap (SGDm) | P/E<br>(30/9/16) | P/B<br>(30/9/16) | Dvd Ind Yld -<br>Gross | ROE         | Net Gearing<br>(%) | Ex-cash<br>P/E |
|-----------------------------------------------------------|----------------|------------------|------------------|------------------------|-------------|--------------------|----------------|
| Spackman Entertainment Group (FY17F)                      | 48.6           | 7.3              | 2.6              | N/A                    | (8.4)       | (35.4)             | 4.7            |
| mm2 Asia Ltd                                              | 432.1          | 34.9             | 9.7              | N/A                    | N/A         | (3.2)              | 33.8           |
| Cityneon Holdings Ltd                                     | 233.6          | 29.9             | 3.5              | 1.1                    | 14.3        | (25.9)             | 22.2           |
| <b>Average with Spackman Entertainment Group</b>          |                | <b>24.0</b>      | <b>5.3</b>       | <b>1.1</b>             | <b>3.0</b>  | <b>(21.5)</b>      | <b>20.2</b>    |
| <b>Average w/o Spackman Entertainment Group</b>           |                | <b>32.4</b>      | <b>6.6</b>       | <b>1.1</b>             | <b>14.3</b> | <b>(14.5)</b>      | <b>28.0</b>    |
| Spackman Entertainment Group (FY17F)                      | 48.6           | 7.3              | 2.6              | N/A                    | (8.4)       | (35.4)             | 4.7            |
| Lions Gate Entertainment Corp                             | 4,215.7        | 50.4             | 3.4              | N/A                    | 6.9         | 148.2              | N/A            |
| Zee Entertainment Enterprise                              | 11,149.0       | 57.9             | 12.1             | 0.4                    | 23.3        | (27.4)             | 42.0           |
| Alibaba Pictures Group Ltd                                | 7,220.2        | 70.7             | 2.3              | N/A                    | 1.0         | (61.1)             | 91.4           |
| Shenghua Entertainment Communication Co Ltd               | 85.3           | 25.8             | 2.4              | 1.9                    | 9.3         | 28.9               | N/A            |
| Huayi Brothers Media Corp                                 | 7,066.7        | 43.2             | 3.6              | 0.4                    | 10.1        | 1.0                | N/A            |
| China Film Co Ltd                                         | 10,341.3       | 43.1             | 7.8              | N/A                    | 20.0        | (62.8)             | 16.0           |
| Omnijoi Media Corp                                        | 2,263.3        | 79.9             | 6.7              | N/A                    | 8.7         | (25.0)             | 59.9           |
| Showbox Corp                                              | 490.6          | 25.2             | 3.3              | 0.8                    | 13.9        | (105.1)            | N/A            |
| CJ E&M Corp                                               | 3,617.5        | 30.2             | 1.8              | 0.3                    | 0.4         | (8.5)              | 27.6           |
| Seoul Broadcasting System                                 | 554.4          | 48.0             | 0.8              | 3.0                    | 1.8         | (12.9)             | 41.8           |
| Shochiku Co Ltd                                           | 2,268.3        | 38.4             | 2.0              | 0.3                    | 5.7         | 67.3               | N/A            |
| <b>Average with Spackman Entertainment Group</b>          |                | <b>43.3</b>      | <b>4.1</b>       | <b>1.0</b>             | <b>7.7</b>  | <b>(7.7)</b>       | <b>40.5</b>    |
| <b>Average w/o Spackman Entertainment Group</b>           |                | <b>46.6</b>      | <b>4.2</b>       | <b>1.0</b>             | <b>9.2</b>  | <b>(5.2)</b>       | <b>46.5</b>    |
| <b>Foreign and local w/o Spackman Entertainment Group</b> |                | <b>44.4</b>      | <b>4.6</b>       | <b>1.0</b>             | <b>9.6</b>  | <b>(6.6)</b>       | <b>41.8</b>    |

Source: Company data, RHB

## Key Risks

**Lack of earnings visibility due to the inherent nature of the business.** Operating in the film industry comes with a relatively high degree of uncertainty. The success of a film depends greatly on the timing of the movie's release as well as the response from the audience. The latter can be hard to predict and understand. In addition, casting for roles in a movie is subject to rapid shifts in popularity or fame of actors and actresses. Hence, the sentiment of the audience and general acceptance largely determine if a movie is a box office hit or miss.

**Large fluctuations in financial performance.** Due to the large initial capital outlay for a movie production, the success or failure of a film would most likely have a material impact on a company's financials. The number of films in the pipeline is also dependent on the general trend in the entertainment industry. Higher interest from investors and commercial demand from the public spells more films being made in the future. These fluctuations make it challenging to forecast the future profitability of films, since a track record of previous commercial successes does not directly translate into future box office successes.

**Lack of financing options.** As Spackman invests its own capital in films, it is likely to seek other investors to finance film productions. Management has stated that the group does not engage in long-term agreements with regards to film financing. Hence, the terms of agreement rely on general market conditions and investors' expectations. Therefore, Spackman may have to accept less-than-ideal terms or even give up producing specific films if it is not able to secure financing for such movies.

**Erosion of market share from larger players.** Given the competitiveness of the entertainment industry in South Korea, many of the market leaders are in a much better position to enjoy higher margins and exposure to the general market. The scope and breadth of services would undoubtedly eat into Spackman's market share.

Moreover, an oversupply situation in the film industry would lead to much lower box office receipts. This is as the public usually selects – at most – a few films to watch at any given time. As Spackman is involved in the production of domestic films, it would also have to compete with a high volume of films made by other companies during local holiday seasons and festivals.

**Highly dependent on filmmakers.** Spackman's impressive portfolio of movies thus far is largely attributed to filmmakers Lee and Suk. Their continual efforts in spearheading the films have proven to be vital for the group.

Being veterans in the industry, the success of Spackman's films would largely depend on the two filmmakers' judgments on various factors. These include deciding which artistes should take the role and determining the date of release of a movie, just to name a few. Hence, it is crucial to retain their services, as the risk of their being poached by other film companies is rather high.

## Industry Outlook

**Influential position of the South Korean film industry.** South Korean movies and dramas have been at the forefront of the entertainment sector, gaining widespread popularity across international borders. This is especially the case in Asia, where the country's movies and TV shows largely cater to a Japanese audience.

After benefiting from the Korean Wave phenomenon several years back, South Korea's entertainment industry has boomed as overseas marketing expanded concurrently. Looking forward, China is poised to drive further demand and appetite for South Korean culture due to the recent success of movies such as *Assassination*, which booked more than 12m viewers.

**Stronger tie-ups with China.** According to South Korea's Ministry of Trade, Industry & Energy, Chinese investment in the country's services sector has risen by almost 10x in four years to USD940m (2014) from 2010's USD100m.

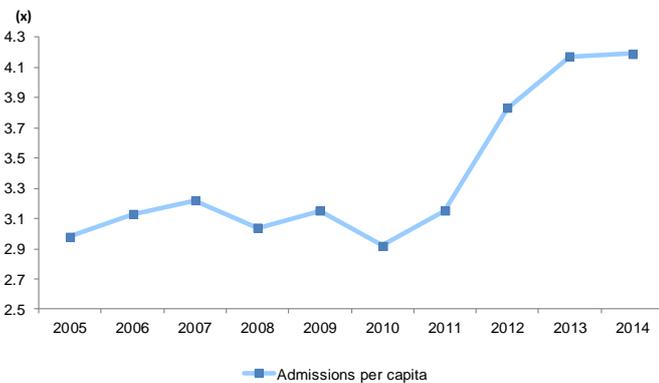
A large part of these investments flowed into the media and entertainment industry. Chinese companies like Zhejiang Huace Film & TV Group (Huace) have been acquiring stakes in South Korean companies, while Alibaba has invested a significant amount into the country's films, most recently in *Real*.

These have been made possible partly thanks improved cooperation between Chinese and South Korean filmmakers. As such, there are now clearer film production and copyright terms as well as co-production agreements to skirt China's import quota limits.

**Steady increase in admissions per capita.** A key benchmark of the South Korean film industry is based on admissions. The country has one of the highest film admissions rates in the world, at 4.19 per capita in 2015. Capital city Seoul on its own managed to hit a high of 5.89 that year. This is much higher than Singapore's 4.15 and the US' 3.83.

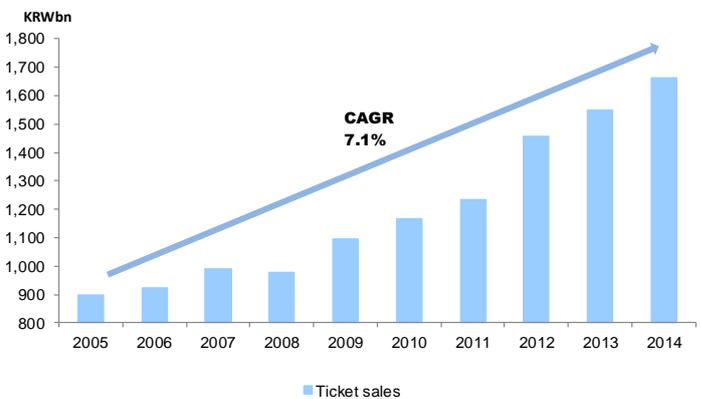
At present, South Korea has the second-highest annual admissions per capita in the world. Its movie industry is constantly investing in newer production technologies and making innovations in the development of films. As such, it is in a strong position to capture a wider regional target audience while enjoying robust domestic demand.

Figure 24: Admissions per capita surged after 2010



Source: Korean Film Council

Figure 25: Ticket sales have been growing since 2005



Source: Korean Film Council

**Leading the growth of Asia's movie market.** Box offices for China, Japan, India, South Korea, Taiwan and Indonesia overtook North America for the first time in 2014. This was driven by China's exponential growth in box office receipts in the range of 30-50% YoY.

South Korea remains a regional leader in the industry. The rise in production and distribution costs due to strong demand has been slightly offset by higher ticket prices. Despite that, the market share for films is likely to continue growing in South Korea. Domestically, ticket sales have increased at a CAGR of 7.1% since 2005, while average ticket prices have risen 25% over the same period.

These positive factors are likely to continue attracting and sustaining producers and distributors as they strive to translate market share into improved profitability.

**The rise in the popularity of domestic films.** Four of the Top 5-highest grossing films since Dec 2014 have been locally-made films. They raked in a total of USD279m and had a combined market share of 20.9%. Furthermore, although the number of foreign films released and screened in 2014 dwarfed that of domestic films (70-80% of the total), locally-made movies still garnered a market share of 50.1%. This reflects the general appeal and the high fundamental quality of such films.

Figure 26: Latest domestic top-grossing box office movies



Source: KoBiz

Figure 27: Domestic and international films comparison (2014)

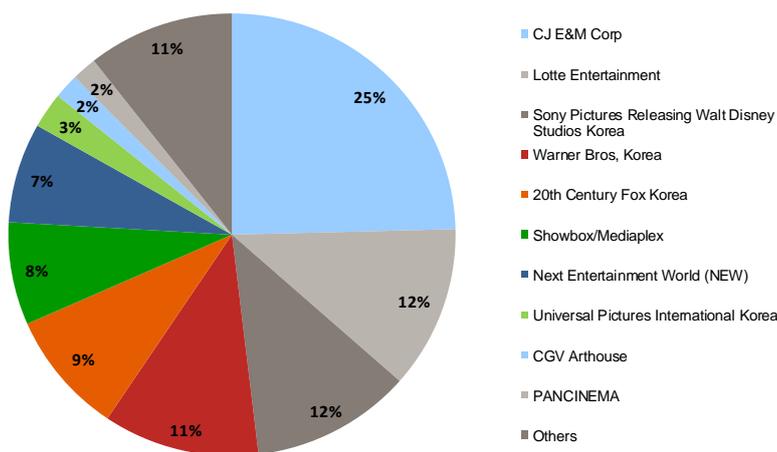
|                       | Korean | % of total | Foreign | % of total | Total |
|-----------------------|--------|------------|---------|------------|-------|
| Total admissions (m)  | 107.7  | 50.1%      | 107.4   | 49.9%      | 215.1 |
| No. of films released | 217    | 19.8%      | 878     | 80.2%      | 1095  |
| No. of films screened | 1147   | 30.0%      | 2681    | 70.0%      | 3828  |

Source: Korean Film Council

**Resilience of local producers and distributors.** South Korean and Hollywood movies made up a huge segment of the domestic industry, about 96.2% of the revenue share for movies released in 2014.

However, local distributors like CJ E&M Corp and Lotte Entertainment continue to exert dominance in the market. The number of releases and sales revenue topped that of foreign distributors like Sony Pictures and Warner Bros, with CJ E&M being the most prominent player in the local industry.

Figure 28: Revenue shares of distributors in 2014



Source: RHB

**Great potential for talent management services.** The boom in the entertainment industry, as a whole, has widened the media and advertising market. Talent management agencies also support a broad range of professional services for movie casts, music artistes and celebrities. This includes music videos, photography, commercials and product sponsorships.

Earlier this year, LVMH Moët Hennessey Louis Vuitton’s (LVMH) private equity arm invested between USD60-80m in YG Entertainment Inc, one of the largest talent management and music production group in South Korea. Similarly, Chinese firm

Sohu.com also offered USD15m for Keyeast, which managed Kim Soo Hyun, the famed co-star of hit drama *My Love From The Star*.

Looking forward, talent management agencies and other supporting operations – such as studio photography and media advertising – are key to capturing value higher up the chain in the entertainment industry. Having said that, having a portfolio of high-profile celebrities and proven track record of contract successes is likely to be crucial in gaining a foothold in these other services segments.

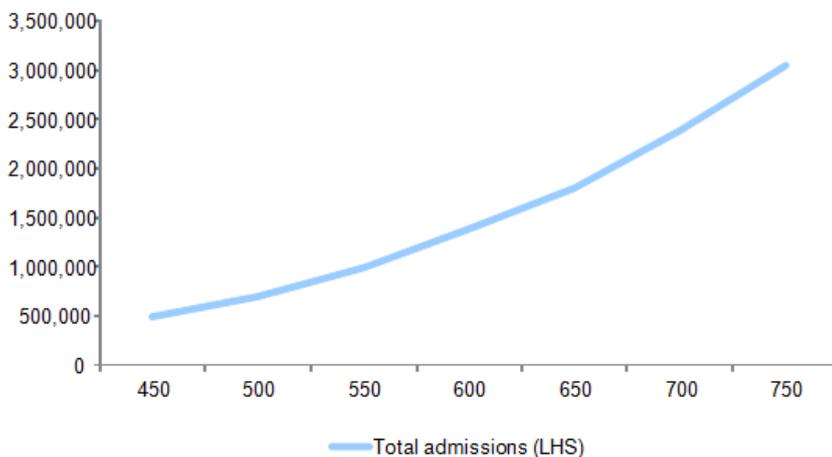
**Opening number of screens is a key determining factor of total box office admissions.** The movie industry is a challenging place to be in. Profits are solely dependent on total box office admissions, which can be very challenging to predict. Furthermore, gains or losses can only be realised after the movie is screened in theatres. In other words, movie producers are not able to control any variables in order to change the final outcome, ie total box office admissions.

We have discovered that the opening number of screens for a movie can play a vital role in terms of total box office admissions. To reduce the limitations of time factor, the variables adopted were “opening night number of screens” vs “total admissions”. Aggregating all the data from 2013 -2015, a regression analysis was formed to determine the correlation.

**Results of our discovery.** The regression line crosses over the 2m total admissions mark at 670 opening screens:

- i. **Less than 670 opening screens:** 82% chance of receiving less than 2m in total admissions;
- ii. **More than 670 opening screens:** 23% chance of receiving less than 2m in total admissions;
- iii. **More than 800 opening screens:** 87% chance of receiving 2m or more in terms of total admissions.

**Figure 29: Total admissions vs opening number of screens**



Source: Company data, RHB

## Financial Forecasts

### Revenue breakdown

**Bulk is from production and distribution of films.** Over the years, the production and distribution of films have been the major source of Spackman's total revenue, accounting for well over 95% of turnover. Spearheaded by filmmakers Lee and Suk, the group has seen tremendous success in previous films such as *The Priests*, *My Brilliant Life* and *Cold Eyes*. Going forward, given the much-anticipated line-up of films ahead (such as *Master*), we expect revenue growth to improve steadily into FY17.

Figure 30: Revenue breakdown (%)

| Revenue segments (%)                 | FY12  | FY13  | FY14  | FY15  | FY16F | FY17F |
|--------------------------------------|-------|-------|-------|-------|-------|-------|
| Production and distribution of films | 99.8% | 95.5% | 97.9% | 97.2% | 97.6% | 98.6% |
| Other                                | 0.2%  | 4.5%  | 2.1%  | 2.8%  | 2.4%  | 1.4%  |

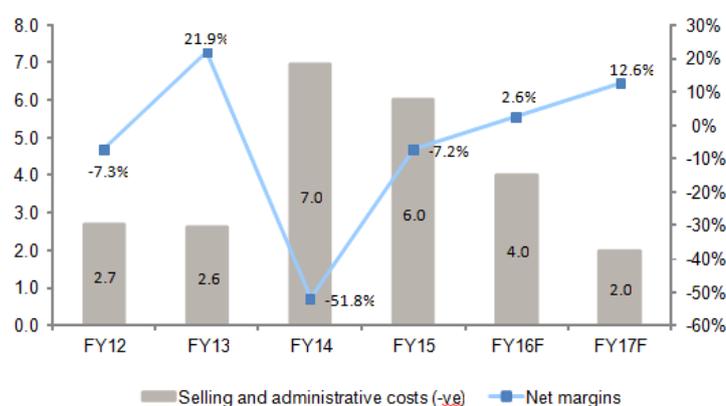
Source: Company data, RHB

### Margins

**We expect net margins to increase steadily.** The disposal of Opus Pictures ought to improve Spackman's net margins significantly. As mentioned before, Opus Pictures accounted for nearly 70% of the group's total general and administrative expenses for 1Q16.

As shown in Figure 33, we expect total selling and administrative costs to be reduced to SGD2m by 2017. This may improve net margins significantly to 12.6% in FY17 from 2.6% in FY16, ie turning the group profitable.

Figure 31: Net margins, selling and administrative costs



Source: RHB

## Company Background

**Leading entertainment production group in South Korea.** Listed on the SGX on 22 Jul 2014, Spackman is a leading entertainment production group that is primarily engaged in independent productions, presentations and the financing of theatrical motion pictures in South Korea.

Figure 32: Spackman's diversified subsidiaries



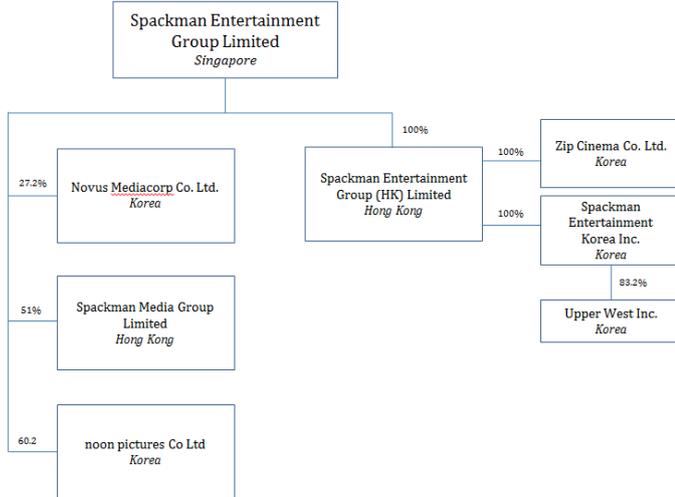
Source: Company

Figure 33: Spackman's key milestones

| Date   | Event                                                                                              |
|--------|----------------------------------------------------------------------------------------------------|
| Jul-14 | Listed on the SGX Catalist Board                                                                   |
| Nov-14 | Acquired 60.2% of Noon Pictures                                                                    |
| Jan-15 | Acquired Novus MediCorp and UAA Korea for 51% and 51.4% respectively                               |
| Apr-15 | Incorporated associated company Spackman Media Group Pte Ltd (SMG)                                 |
| Jun-15 | Acquired 99% of Delmedia, one of South Korea's leading producers of variety shows                  |
| Sep-15 | Acquired 51% of BreakfastFilm Co Ltd                                                               |
| Nov-15 | Opening of Zip Cinema's production, <i>The Priests</i> , which sold a record-breaking 5.4m tickets |
| Dec-15 | Proposed share swap of SMG                                                                         |
| Apr-16 | Proposed disposal of loss-making subsidiary, Opus pictures                                         |
| May-16 | Completed share swap of its 45.8% interest in SMG for 27.4% in Spackman Media Group Ltd (SMGL)     |
| Jul-16 | Alibaba Pictures purchases distribution rights for <i>Life Risking Romance</i> in China            |
| Aug-16 | EGM on disposal of loss-making subsidiary Opus pictures                                            |

Source: Company data, RHB

Figure 34: Units complementing the group's core operations



Source: RHB

Subsidiaries

**Zip Cinema.** A South Korean movie production firm founded by experienced veteran film producer Lee. She was named one of the world's "10 Producers to Watch" by leading Hollywood trade journal *Variety* in 2007. Zip Cinema engages in the development and production of theatrical motion pictures. Its goal is to provide original content to moviegoers from the most creative domestic filmmakers.

Since its establishment, Zip Cinema has racked up many accolades, and achieved box office successes and record-breaking ticket sales. Some of its successful movies are *All About My Wife* and *The Priests*, which sold well over 4.6m and 5.4m tickets respectively and topped the Korean box office chart.

Figure 35: Zip Cinema's productions – *The Priests* and *All About My Wife*



Source: Company

**Novus Mediacorp.** A renowned investor, presenter and ancillary distributor of South Korean theatrical films. Since 2009, Novus Mediacorp has invested, presented and/or been the ancillary producer of 55 films. This includes box office hits like *Secretly, Greatly* and *All About My Wife*. Novus also has a whollyowned subsidiary, Novus Entertainment Co Ltd, which is currently producing three major theatrical films, *Life Risking Love*, *Chong Hee – The Emperor's Love* and *Korean Gangster*.

Figure 36: Novus Mediacorp's films, *Life Risking Romance* and *All About My Wife*



Source: Company

**Spackman Media Group (SMG).** A company incorporated in Hong Kong. Together with its subsidiaries, SMG is one of the largest entertainment talent agencies in South Korea in terms of the number of artistes under management.

This Spackman subsidiary manages over 50 artistes and operates its talent management business via renowned agencies such as SBD Entertainment Inc and MS Team, just to name a few. Some of the popular artistes are Yoo Ah-in, Bae Doo-na and Gang Dong-won.

**Spackman Entertainment Group Korea (SEKI).** SEKI is a wholly-owned subsidiary, established on 3 Aug 2012. SEKI is a film investment company that makes early-stage investments into films developed and produced by Zip Cinema and Opus Pictures. The firm invests in films developed and produced by the group’s companies through special contractual arrangements, ie investment and profit distribution agreements.

Given that it is an affiliate of Spackman’s film production companies, SEKI generally enjoys more favourable investment terms than that of non-affiliated investors.

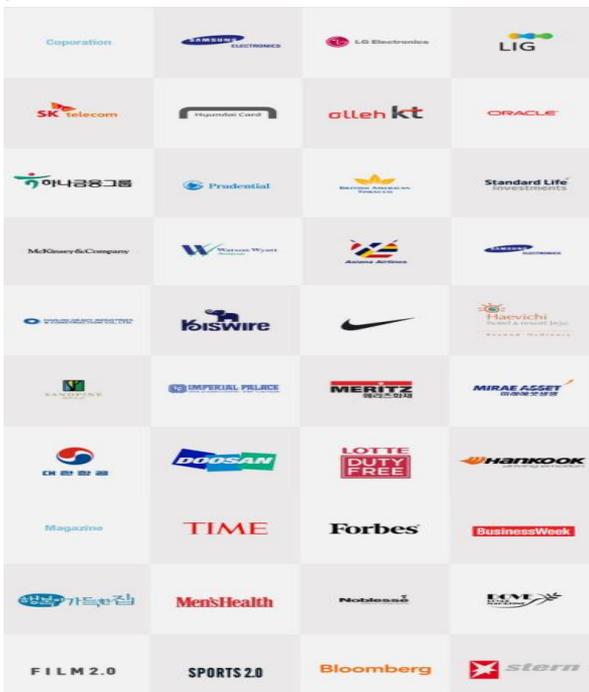
Figure 37: SMG and SEKI are different companies within the group



Source: Company

**Other businesses.** Spackman also has a café and lounge business, Upper West, which is located in Seoul’s Gangnam district. Another business, Noon Pictures, operates a professional photography studio and also offers in-house high-end photography services.

Figure 38: Noon Pictures’ established clientele (left side) and the Upper West logo



Source: Company

**Experienced management team with diverse experience.** The management team is led by Charles Spackman and Richard Lee. With a combined 40 years of experience in the entertainment industry, the team boasts deep knowledge in their respective fields. More notably are Suk and Lee, who have extensive knowledge in film production and development as founders of Novus Mediacorp and Zip Cinema respectively.

**Figure 39: Spackman's key management team**

|                    |                                     |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |
|--------------------|-------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Charles C Spackman | Executive chairman                  | Mr Spackman is the executive chairman of the group and is a member of the nominating committee. He is currently the chairman and chief executive officer of Spackman Equities Group Inc, a company listed on the TSX Venture Exchange in Canada. Mr Spackman is also the chairman, chief executive officer and founder of Spackman Group Ltd, a Hong Kong-based diversified investment company. He has about 18 years of experience in financing, analysing, investing in, and developing the businesses of public and private companies                                                                                                                       |
| Suk Young Jung     | Executive director                  | Mr Jung is the executive director of the group. He is responsible for overseeing and managing film production, development, presentation and financing of the group's films. Mr Jung was a former co-founder and executive director of Vantage Holdings, a leading South Korean film investment company that presented The Chaser. He graduated with a BA from Pennsylvania State University, majoring in economics in the US                                                                                                                                                                                                                                  |
| Richard Lee        | Director                            | Mr Lee was appointed the head of business development of the group in Oct 2013. He has now stepped down from this post and is currently the director of SMGL. Prior to joining the group, Mr Lee has worked in areas such as fund management, private equity, equity sales & research, and M&As for HSBC Private Equity, CIMB Securities, BNP Paribas Securities and CLSA Securities. Prior to this, and as one of the founding members of the Spackman Group, he served in various positions within the organisation. Mr Lee graduated with a BA from Harvard College                                                                                         |
| Kyoungwon Na       | CFO                                 | Mr Na was appointed as the CFO of the group in Sept 2013. He is responsible for managing and overseeing the financial related activities of Spackman, including accounting, financing and taxation matters. Prior to joining the group, Mr Na worked with KPMG Korea and KPMG Singapore, providing audit, tax and advisory services to many private and public companies over a period of nine years                                                                                                                                                                                                                                                           |
| Eugene Lee         | CEO and head producer of Zip Cinema | Ms Lee is the executive director and chief producer of the group. She is the founder, chief executive officer and head producer of Zip Cinema. Ms Lee commenced her film career in 2000 as the marketing director of BOM Film Production Co Ltd, a South Korean film production company. She also worked as an advertising executive at KORAD, a Seoul-based advertising agency. Ms Lee was named as one of the "10 Producers to Watch" in the world in 2007 by Variety magazine. She graduated with a BA from Ehwa Woman's University in South Korea                                                                                                          |
| Jasmine Leong      | Senior manager                      | Ms Leong is the senior manager of the group. She is responsible for overseeing its corporate actions, investor relations and operational matters. Ms Leong has several years of experience in handling investor relations and corporate communications of listed companies on the SGX. Previously, she was the investor relations manager at Accordia Golf Trust and worked at Financial PR as an investor relations consultant. Ms Leong started her career with Eurotronic Group, where she was based in China. Ms Leong graduated with a Masters in Communication Management and has a Bachelor in Business Management from Singapore Management University |

Source: Company

## Business Analysis

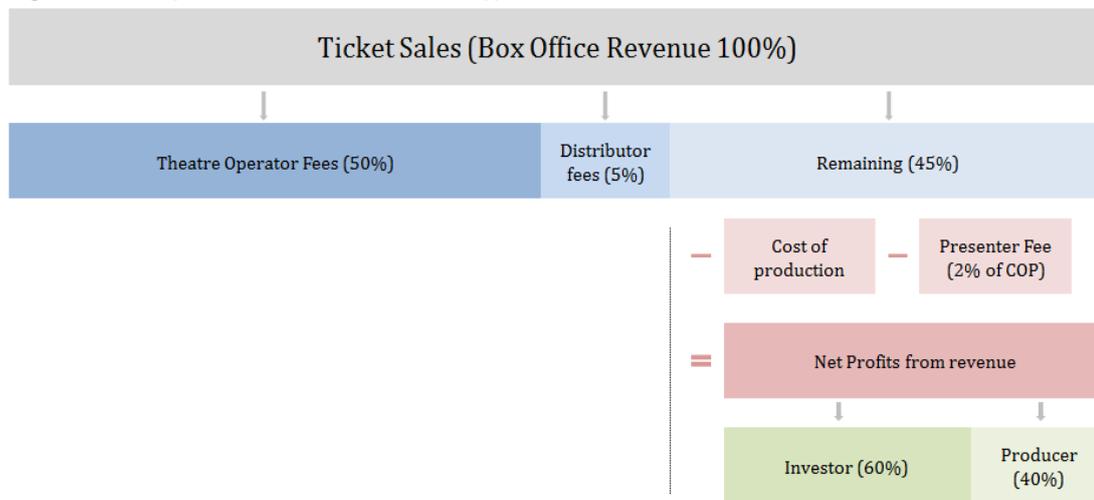
### Motion pictures

**Spackman's primary business is in producing, presenting, distributing and investing in theatrical films.** From the release of a film, half of the proceeds first flow to the cinema, while another 5% and 1% go to the distributor and presenter respectively. What is left is paid out to the film producers and investors after deducting a film's production costs.

As a producer, typical fees are around a 40% cut of the film's profits, whereas as co-producers, it is proportionally half of the 40%.

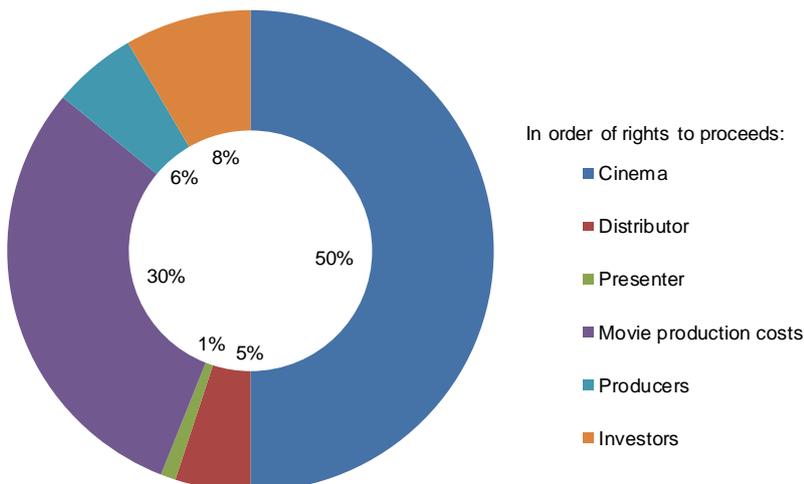
For investors, returns comprise a percentage of the film's profits after the producer's fees are paid. Spackman derives most of its revenue from this profit-sharing structure. Outside of these two operations, the group also handles the distribution of mainly foreign films through theatres, and internet protocol TV (IPTV) and video on demand (VOD) channels.

Figure 40: Respective share of film sales (I)



Source: RHB

Figure 41: Respective share of film sales (II)



Source: RHB

**Figure 42: Film segment activities**

**Producer**

- Originating and developing the screenplay
- Procuring the screenwriters, directors, cast and crew, and post production companies
- Selecting the presenter of the film (assuming Spackman does not act as the presenter of the film) and negotiating the profit-sharing arrangements with the presenter and film investors in the group's role as the producer
- Overseeing and managing the actual filming activities
- Managing the post-production process
- Developing and devising the marketing strategies for the film
- Licensing and/or selling the films to the overseas market

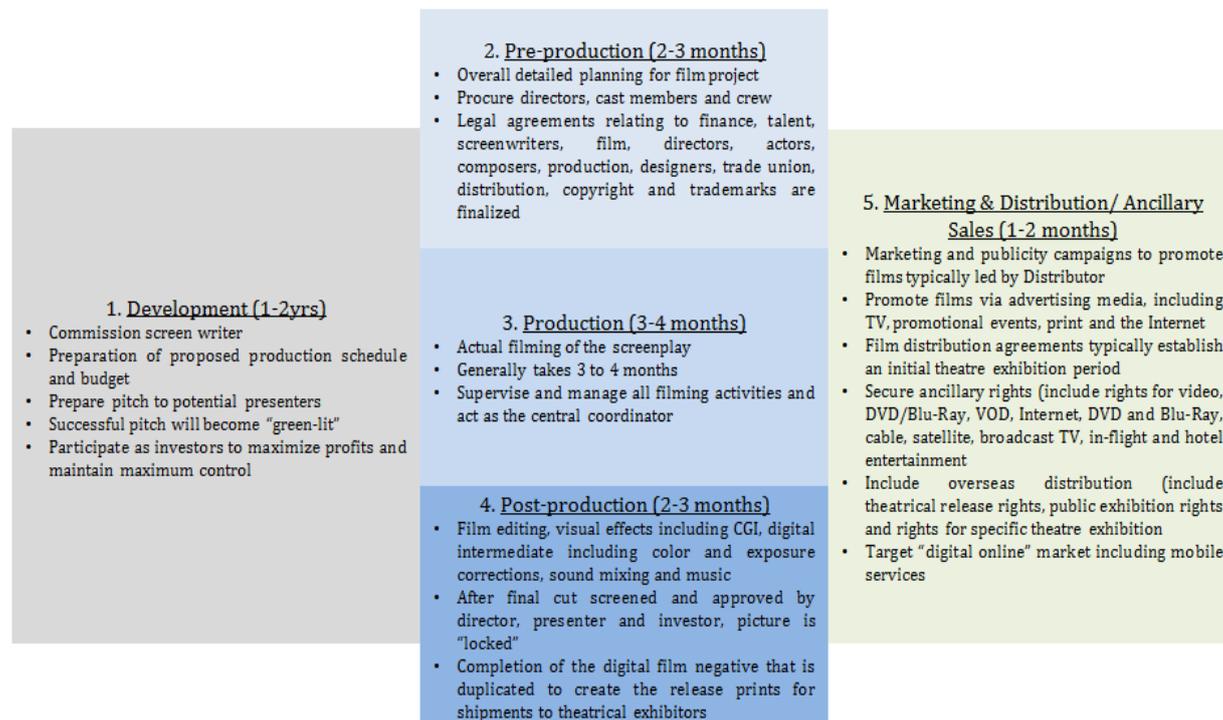
**Presenter**

- Raises the financing for a film's total production budget to the extent that the producer of the film does not finance the movie
- Entering into an agreement with a distributor to distribute the film in theatres in South Korea
- Entering into agreements for the distribution of the film overseas
- Entering into agreements for the ancillary distribution of the film
- Administering the expenses of the production, distribution and marketing of the film
- Settling and distributing the revenue from the film

Source: Company data

**Production process.** Typically, the entire production process (from pre-production to post production) takes approximately 7-10 months to complete. The filming takes approximately 1-2 months. After this, the marketing and distribution/ancillary sales takes another 1-2 months to finalise.

**Figure 43: The process of making and marketing a film**

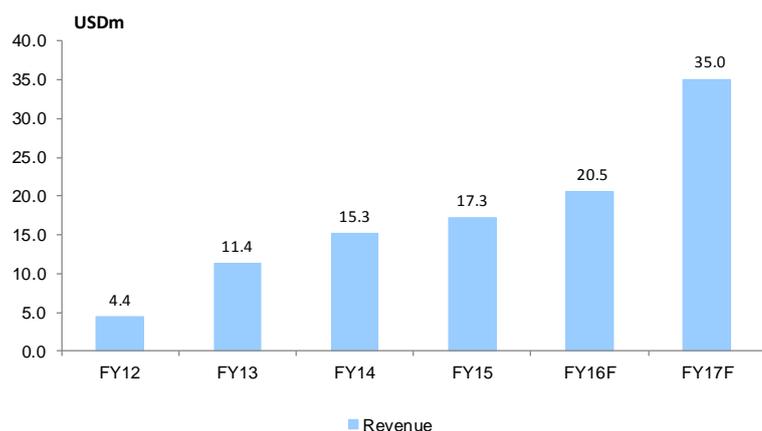


Source: Company

**Strengthening core capabilities.** Given the uncertain nature of the film business, Spackman acquired Novus Mediacorp to grow its business in the motion picture segment. This helps expand its presence and build on a more visible income stream. This is by taking on more movies and getting involved in different stages of a film's production, presentation and distribution processes.

Over the years, Spackman has seen a steady growth in its revenue. This is a testament to the popular films it has made over the years, which have also enjoyed being at the top spot in the box office charts. On top of that, the ancillary market continues to drive more post movie theatre revenue for Spackman, with more films in the pipeline.

**Figure 44: Revenue from film-related activities**



**Figure 45: Market players in 2014**

|                                                   | No. of releases | Sales revenue (KRWm) | Revenue share | Admissions | Admissions share |
|---------------------------------------------------|-----------------|----------------------|---------------|------------|------------------|
| CJ E&M Corp                                       | 31              | 408,252              | 25%           | 53,148,905 | 25%              |
| Lotte Entertainment                               | 30.5            | 197,781              | 12%           | 25,898,156 | 12%              |
| Sony Pictures Releasing Walt Disney Studios Korea | 16              | 193,007              | 12%           | 24,074,441 | 11%              |
| Warner Bros, Korea                                | 12              | 187,262              | 11%           | 23,143,012 | 11%              |
| 20th Century Fox Korea                            | 14              | 149,541              | 9%            | 19,085,692 | 9%               |
| Showbox/Mediaplex                                 | 9.5             | 124,513              | 8%            | 16,070,120 | 8%               |
| Next Entertainment World (NEW)                    | 16              | 120,288              | 7%            | 15,994,672 | 8%               |
| Universal Pictures International Korea            | 17              | 42,374               | 3%            | 5,254,204  | 3%               |
| CGV Arthouse                                      | 15.5            | 30,499               | 2%            | 4,031,659  | 2%               |
| PANCINEMA                                         | 11.5            | 30,514               | 2%            | 3,890,344  | 2%               |
| Others                                            | 1015            | 174,655              | 11%           | 23,281,846 | 11%              |

Source: Korean Film Council

**Photography**

**In-house high-end photography work.** Noon Pictures is one of the group's strategic acquisitions to further capture value in the broader entertainment industry. An established portfolio of corporate clients and international celebrities boosts the quality capabilities of its studio services. It also serves as an alternative avenue for Spackman to manage its non-core services.

**Figure 46: Noon Pictures' office**



Source: Noon Pictures

**Figure 47: Noon Pictures' office and samples of its work portfolio**



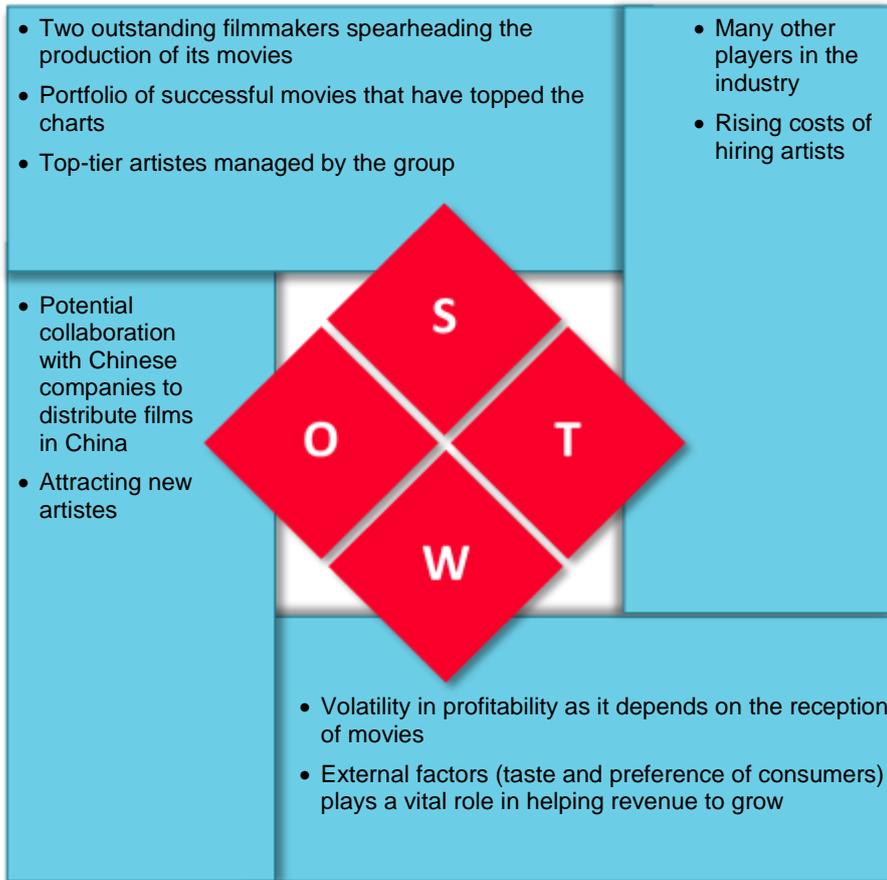
Source: Noon Pictures

**Figure 48: Poster of a drama made in collaboration with Seoul Broadcasting System**



Source: Noon Pictures

## SWOT Analysis



## Recommendation Chart



Source: RHB, Bloomberg

| Date       | Recommendation | Target Price | Price |
|------------|----------------|--------------|-------|
| 2016-10-12 |                |              |       |

Source: RHB, Bloomberg

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a) -

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a) -

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a) -

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a) -

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3. Affiliation between 2 companies whereby one or more member of the Board of Directors or the Commissioners are the same;
4. Affiliation between the Company and the parties, both directly or indirectly, controlling or being controlled by the Company;
5. Affiliation between 2 companies which are controlled, directly or indirectly, by the same party; or
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- b. a substantial shareholder of an Issuer or Public Company;
- c. an individual, who because of his position or profession, or because of a business relationship with an Issuer or Public Company, has access to inside information; and
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- (a) -

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- (a) -

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- (a) -

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