



# Cityneon Holdings Limited

(CITN SP/CNHL.SI)

## BUY - Maintain

Price as of 17 May 2018	1.00
12M target price (S\$)	1.54
Previous target price (S\$)	1.54
Upside, incl. div (%)	53.5

## Trading data

Mkt Cap (S\$m) / (US\$m)	245 / 182
Issued Shares (m)	245
Ave Daily Traded (3-Month) Vol / Val	0.7m / \$0.7m
52 week lo / hi	\$0.91 / \$1.26
Free Float	31.0%

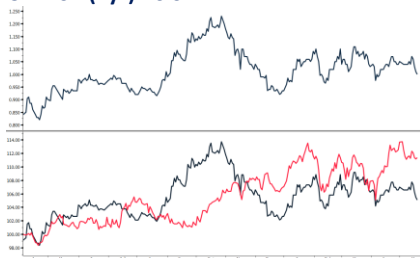
## Major Shareholders

Lucrum 1 Investment	69.0%
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## Previous Recommendations

Date	Rating	Share Price (S\$)	Target Price (S\$)
10-Nov-17	BUY	1.10	1.38
5-Mar-18	BUY	1.06	1.54

## CITN SP (1yr) VS STI



Source: Bloomberg

Nicholas Siew  
65 6202 1193  
nicholas.siew@kgi.com

See the last page for important disclosures.

## 1Q18 results in line; 4<sup>th</sup> IP update

### Event

Cityneon reported 1Q18 net profit of S\$4.0mn (+80.4% YoY), in line our expectations. This was mainly driven by the IP business segment, which accounted for about 80% of the bottom line. Traditional business segments remained flat, in line with our expectations as well. The Group has also strengthened its IP business segment with the acquisition of its 4<sup>th</sup> IP: The Hunger Games: The Exhibition (THG Exhibition).

### Impact

**1Q18 earnings in line with expectations.** 1Q18 earnings came as no surprise. The IP business segment, which typically commands higher margins as compared to the traditional business segments, now makes up 62% and about 80% of revenue and net profits, respectively. This led to improved overall gross and net margins of 69.8% and 16.8%, respectively, on the back of a positive shift in sales mix. Going by this trend, we expect the IP business segment to be the key driver of growth for the group as new IPs are announced.

**4<sup>th</sup> IP – THG Exhibition.** Cityneon has acquired its 4<sup>th</sup> IP, which will last for seven years, granting the Group the rights to the THG Exhibition and the creation and sale of the Hunger Games branded merchandise. The agreement allows Cityneon to exploit other IPs of Lionsgate such as, Twilight and Now You See Me etc, widening the range of movie franchises it can leverage on.

**2<sup>nd</sup> Jurassic World exhibition set.** Cityneon has also entered into an agreement with Universal to build a second Jurassic World exhibition set. This comes after successful tours in Australia and the US. The set will take about 9 months to build and should be completed by 2Q19 at the latest, enlarging Jurassic World's revenue stream. Universal Pictures has announced its plans to produce another instalment of the Jurassic World franchise in 2021 and would complement the Jurassic World exhibitions.

### Valuation & Action

**Maintained BUY with no change to our P/E based target price of S\$1.54 (FY2018F EPS: S\$0.11; FY2018F P/E: 14.0x).** Our investment thesis remains intact, with Cityneon's attractive growth prospects and low risk business model being the basis of our recommendation.

### Risks

Renewal of the various IP rights and a decline in the franchise popularity.

### Financials & Key Operating Statistics

YE Dec SGD mn	2016	2017	2018F	2019F	2020F
Revenue	96.8	116.7	138.0	159.3	166.3
PATMI	6.7	17.4	26.9	31.3	32.4
Core PATMI	6.7	17.4	26.9	31.3	32.4
Core EPS (SGD cents)	2.8	7.1	11.0	12.8	13.2
Core EPS grth (%)	302.6	151.1	54.5	16.5	3.4
Core P/E (x)	33.4	13.2	9.6	8.3	8.0
DPS (SGD cents)	0.0	0.0	0.0	0.0	0.0
Div Yield (%)	0.0	0.0	0.0	0.0	0.0
Net Margin (%)	6.9	14.9	19.5	19.7	19.5
Gearing (%)	26.3	54.7	47.7	41.5	36.6
Price / Book (x)	3.2	2.8	2.4	1.8	1.5
ROE (%)	11.2	22.9	27.9	24.9	20.5

Source: Company Data, KGI Research

### **A substantial portion of its US\$60mn war chest remains untapped**

Recall that the Group secured a US\$60mn (S\$79mn) credit facility in Feb-18 to scale its IP business segment. We understand that approximately 50% has been drawn down, with the remaining 50% ready to be deployed for future growth capex i.e. creative transformation efforts for the overall Group's positioning and additional IPs for the IP business segment, which we believe are actively being pursued by the management.

### **Demystifying the increasing operating and finance cost pressures**

Operating expenses have increased 46% YoY, mainly led by higher depreciation & amortisation charges (+135% YoY), marketing expenses (54% YoY) and staff costs (36% YoY). Finance costs surged (417% YoY) on the back of newly obtained loans to acquire JP Exhibitions and to build new exhibition sets.

While we do not rule out the possibility of the above costs continuing to trend on a YoY basis, bringing about liquidity concerns and potentially hurting margins, we do not see these as near-term concerns for the following reasons:

1. **Growth phase:** Cityneon is in the early stages of growth and expediting growth plans with leverage is commonplace. Given its high margin and low risk IP business segment, we believe its 1Q18 interest coverage ratio of 4.4x is still at a sustainable level, albeit much lower than in 4Q17 of 14.0x.
2. **Creative transformation:** The Group continues to transform and reposition itself as a creative and design brand. Higher costs associated with branding/marketing and hiring creative talent are expected in the near term, but not recurring in nature.

### **Jurassic World – Exploring a different business model**

The reception at the on-going Jurassic World exhibition (in Paris) is by far the leading exhibition by visitorship. Number of visitors at the exhibition is currently 4 – 5k/day, compared to the average visitorship of 1 – 2k at the other exhibitions of other IPs. We understand that the Group is considering a change in business model for the subsequent Jurassic World exhibition i.e. operate the exhibition set, without an operator, and bearing operational risk. Cityneon's revenue in this case will be subject to variability in visitorship. This arrangement will remain flexible and will depend on the management's prior projection of potential demand.

While the management's plans only pertain to Jurassic World at the moment, we do not rule out the possibility of this arrangement being implemented across its other IPs, especially for those exhibitions/locations that coincide with movie releases.

### **Reduction in earnings volatility as a result of changes in accounting policies**

Changes in revenue recognition policies now mandate that 50% of its license fees are to be recognised when the permit has been granted to the promoter of the exhibition, and the remaining 50% to be booked as revenues over the term of the agreement. This consequently removes the lumpiness in earnings.

### **Management guidance**

The Group currently has 7 exhibition sets, and guides for 9 – 10 by the end of the 2018, which would contribute to the top line from 2019 onwards.

### Lions Gate Exhibition (Lionsgate)

Lionsgate owns the rights to the THG Exhibition and belongs to the Lions Gate Entertainment Inc. Group (NYSE: LGF/A), which makes and distributes films, television shows and other entertainment content globally.

### Terms of the agreement

**7 + 7 year agreement:** Cityneon has entered into a license agreement with Lions Gate Exhibition (Lionsgate) to obtain an exclusive worldwide license of the rights to the THG Exhibition. The agreement will last for seven years and will not only grant Cityneon the rights to the THG Exhibition, but also the creation and sale of the Hunger Games branded merchandise.

**Widened opportunities:** The agreement may be renewed for a maximum of seven years and also grants Cityneon the right of first negotiation to (1) purchase any materials relating to the THG Exhibition in the event Lionsgate wishes to sell the same to an unaffiliated third party and (2) exploit other intellectual property of Lionsgate e.g. Twilight, Now You See Me etc. Cityneon does not own the exhibition set and hence, does not bear any depreciation charge for this.

### The Hunger Games: The Exhibition (THG Exhibition)

The THG Exhibition is not exactly what we expected, but nonetheless, fits the bill for an experiential exhibition. The new IP would allow Cityneon to expand its global reach and has successfully toured New York, San Francisco, Sydney, and Louisville. The agreement provides Cityneon with a first right to produce future travelling exhibits for the studio.

**Figure 1: How The Hunger Games stacks up against the other IPs – Worldwide Box Office sales**

Rank	Year	Title	Gross (US\$b)
4	2015	Jurassic World	1.70
5	2012	The Avengers	1.50
7	2012	Avengers: Age of Ultron	1.40
13	2011	Transformers: Dark of the Moon	1.10
16	2014	Transformers: Age of Extinction	1.10
57	2013	The Hunger Games: Catching Fire	0.86
85	2014	The Hunger Games: Mockingjay - Part 1	0.77
108	2012	The Hunger Games	0.68
120	2015	The Hunger Games: Mockingjay - Part 2	0.65

Source: The-numbers, KGI Research

## 1Q18 results review

**Figure 2: Results comparison**

FYE Dec (SGD m)	1Q18	1Q17	yoy % chg	FY19F	Comments
Revenue	23.5	16.9	38.4%	159.3	Driven by IP segment; Traditional business remained flat
Cost of sales	(7.1)	(6.6)	7.6%	(75.2)	
<b>Gross profit</b>	<b>16.4</b>	<b>10.3</b>	<b>58.1%</b>	<b>84.1</b>	<b>Driven by higher margin business</b>
<i>Gross margin (%)</i>	69.8	61.1		52.8	
Other operating income	0.3	0.1	114.8%	0.0	Mainly due to rental income from rented out units at new office premises
Operating expenses	(11.0)	(7.5)	45.8%	(45.5)	Driven by rebranding exercise and higher depreciation and amortisation
Finance costs	(1.3)	(0.2)	417.1%	(4.0)	Loans obtained to acquire JP Exhibitions and build new exhibition sets
Other expenses	0.0	(0.1)	-100.0%	0.0	
<b>Net profit/(loss) before tax</b>	<b>4.4</b>	<b>2.6</b>	<b>67.5%</b>	<b>34.8</b>	<b>Driven by higher margin business</b>
Income tax	(0.4)	(0.4)	0.9%	(3.5)	
<b>Total return after tax</b>	<b>4.0</b>	<b>2.2</b>	<b>80.4%</b>	<b>31.3</b>	
Minority interest	(0.0)	(0.0)	nm	0.0	
<b>PATMI</b>	<b>3.9</b>	<b>2.2</b>	<b>80.5%</b>	<b>31.3</b>	<b>In line with topline</b>
<b>EBITDA, adjusted</b>	<b>9.0</b>	<b>5.1</b>	<b>75.3%</b>	<b>47.1</b>	
EPS (cents)	1.6	0.9	79.4%	12.8	In line with topline

Source: Company, KGI Research

**Financials**

FYE 31 December

<b>INCOME STATEMENT (SGD mn)</b>	<b>2016</b>	<b>2017</b>	<b>2018F</b>	<b>2019F</b>	<b>2020F</b>
Revenue	96.8	116.7	138.0	159.3	166.3
Cost of Sales	(63.4)	(52.9)	(64.9)	(75.2)	(79.0)
<b>Gross Profit</b>	<b>33.3</b>	<b>63.8</b>	<b>73.1</b>	<b>84.1</b>	<b>87.3</b>
Operating Expense	(25.3)	(41.4)	(39.4)	(45.5)	(47.7)
Interest Expense	(0.6)	(2.1)	(4.0)	(4.0)	(4.0)
Interest Income	0.1	0.0	0.1	0.2	0.4
Other Gains/(Losses)	0.0	0.0	0.0	0.0	0.0
<b>Profit Before Tax</b>	<b>7.4</b>	<b>20.3</b>	<b>29.9</b>	<b>34.8</b>	<b>36.0</b>
Income Tax	(0.7)	(2.8)	(3.0)	(3.5)	(3.6)
Perpetual, Others etc.	(0.1)	(0.2)	0.0	0.0	0.0
<b>PATMI</b>	<b>6.7</b>	<b>17.4</b>	<b>26.9</b>	<b>31.3</b>	<b>32.4</b>
<b>BALANCE SHEET (SGD mn)</b>	<b>2016</b>	<b>2017</b>	<b>2018F</b>	<b>2019F</b>	<b>2020F</b>
Cash and Equivalents	23.8	17.9	32.2	50.5	73.9
Accounts Receivable	24.0	75.9	89.7	103.6	108.1
Other Current Assets	17.4	23.6	23.6	23.6	23.6
<b>Total Current Assets</b>	<b>65.9</b>	<b>118.1</b>	<b>146.4</b>	<b>178.6</b>	<b>206.7</b>
Net Property, Plant, and Equipment	43.4	80.2	90.8	100.4	109.8
Other Assets	10.6	39.4	37.8	36.1	34.5
<b>Total Assets</b>	<b>120.0</b>	<b>237.7</b>	<b>274.9</b>	<b>315.2</b>	<b>351.0</b>
Accounts Payable	19.6	45.0	55.2	64.0	67.2
Borrowings (Current)	24.7	66.5	66.5	66.5	66.5
Other Current Liabilities	5.2	1.1	1.1	1.1	1.1
<b>Total Current Liabilities</b>	<b>49.6</b>	<b>112.6</b>	<b>122.8</b>	<b>131.6</b>	<b>134.9</b>
LT Borrowings	0.0	33.7	33.7	33.7	33.7
Other Non-Current Liabilities	0.8	8.2	8.2	8.2	8.2
<b>Total Liabilities</b>	<b>50.4</b>	<b>154.5</b>	<b>164.7</b>	<b>173.5</b>	<b>176.7</b>
Shareholder's Equity	69.3	82.9	109.9	141.4	174.0
Minority Interest	0.3	0.3	0.3	0.3	0.3
<b>Total Equity</b>	<b>69.6</b>	<b>83.2</b>	<b>110.2</b>	<b>141.7</b>	<b>174.3</b>
<b>Total Liabilities and Equity</b>	<b>120.0</b>	<b>237.7</b>	<b>274.9</b>	<b>315.2</b>	<b>351.0</b>
<b>CASH FLOW STATEMENT (SGD mn)</b>	<b>2016</b>	<b>2017</b>	<b>2018F</b>	<b>2019F</b>	<b>2020F</b>
<b>Net Profit</b>	<b>6.6</b>	<b>17.4</b>	<b>26.9</b>	<b>31.3</b>	<b>32.4</b>
Depreciation	3.6	6.2	6.0	6.9	7.2
Amortisation	0.9	1.6	1.6	1.6	1.6
Other Non-Cash Adjustments	0.3	3.5	0.2	0.2	0.2
Changes in Working Capital	(7.7)	(43.4)	(3.8)	(5.2)	(1.4)
Deferred Taxes	0.3	1.8	0.0	0.0	0.0
<b>Cash from Operations</b>	<b>3.9</b>	<b>(12.9)</b>	<b>30.9</b>	<b>34.8</b>	<b>40.0</b>
Capex	(29.6)	(13.9)	(16.6)	(16.6)	(16.6)
Other Investing	(2.7)	(28.4)	0.0	0.0	0.0
<b>Cash in Investing</b>	<b>(32.3)</b>	<b>(42.3)</b>	<b>(16.6)</b>	<b>(16.6)</b>	<b>(16.6)</b>
Dividends Paid	0.0	0.0	0.0	0.0	0.0
Equity Raised / (Bought Back)	12.1	0.0	0.0	0.0	0.0
Borrowings Raised / (Repaid)	15.8	49.9	0.0	0.0	0.0
Other Financing	(0.2)	1.2	0.0	0.0	0.0
<b>Cash from Financing</b>	<b>27.7</b>	<b>51.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
FX Effects, Others	0.2	(1.0)	0.0	0.0	0.0
<b>Net Increase in Cash</b>	<b>(0.5)</b>	<b>(5.2)</b>	<b>14.3</b>	<b>18.2</b>	<b>23.4</b>
Beginning Cash	23.2	22.6	17.4	31.7	49.9
<b>Ending Cash (Incl. Pledged Cash)</b>	<b>23.8</b>	<b>17.9</b>	<b>32.2</b>	<b>50.5</b>	<b>73.9</b>
<b>KEY RATIOS</b>	<b>2016</b>	<b>2017</b>	<b>2018F</b>	<b>2019F</b>	<b>2020F</b>
Core EPS (SGD cents)	2.8	7.1	11.0	12.8	13.2
Core EPS Growth (%)	302.6	151.1	54.5	16.5	3.4
DPS (SGD cents)	0.0	0.0	0.0	0.0	0.0
Div Yield (%)	0.0	0.0	0.0	0.0	0.0
Price / Book	3.2	2.8	2.4	1.8	1.5
<b>Profitability (%)</b>					
Gross Margin	34.4	54.7	53.0	52.8	52.5
EBITDA Margin	12.9	25.9	30.0	29.6	29.2
Net Margin	6.9	14.9	19.5	19.7	19.5
Return on Equity	11.2	22.9	27.9	24.9	20.5
ROIC	16.6	21.1	19.8	20.8	20.0
<b>Financial Structure (x)</b>					
EBIT / Interest Expense	12.5	10.7	8.4	9.6	9.9
Debt / Capital	0.3	0.5	0.5	0.4	0.4

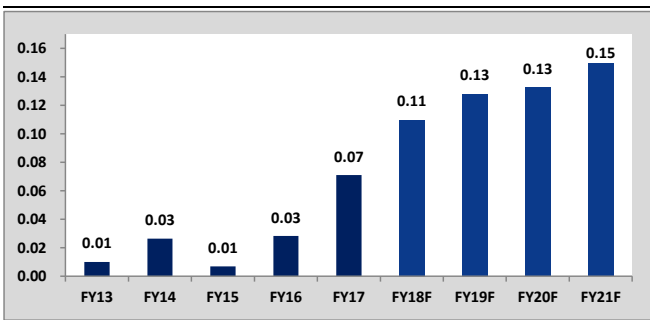
Source: Company Data, KGI Research

**Figure 3: Company profile**

Cityneon Holdings Ltd, through its subsidiaries is a turnkey service provider of creative solutions in the area of Interior Architecture, Events, Exhibitions and all manner of Experiential Environment through the actualization of creativity, production, execution and delivery. It also has very specialized expertise in the area of conceptualizing, designing and building Museums.

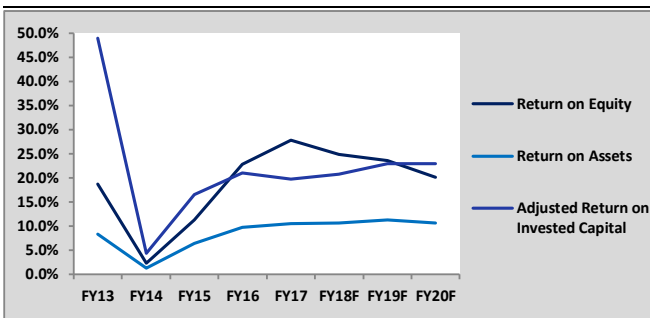
Source: Bloomberg

**Figure 5: Diluted EPS projections**



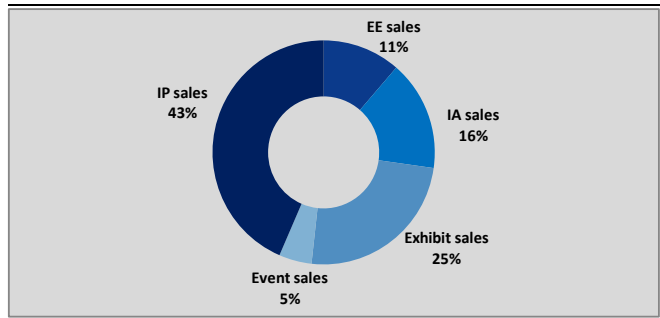
Source: Company Data, KGI Research

**Figure 7: ROE, ROA and ROIC**



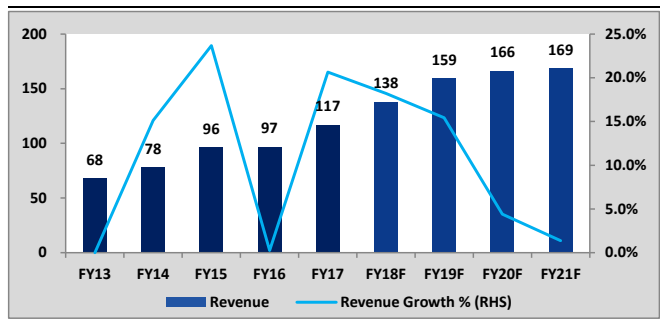
Source: Company Data, KGI Research

**Figure 4: FY17 Revenue contribution by segment**



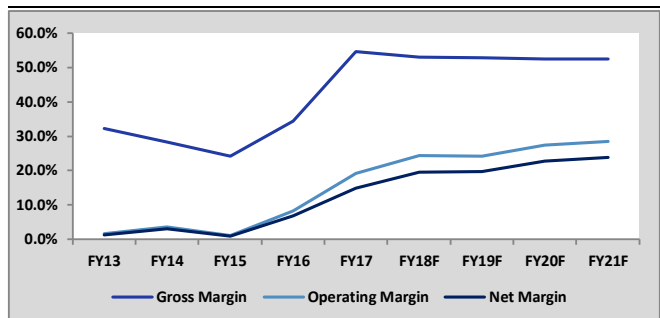
Source: Company Data, KGI Research

**Figure 6: Projected revenue and revenue growth**



Source: Company Data, KGI Research

**Figure 8: Gross margin, Operating margin and Net margin**



Source: Company Data, KGI Research

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	KGI Securities Research's recommendations are based on an Absolute Return rating system.
<b>BUY</b>	>10% total return over the next 12 months
<b>HOLD</b>	-10% to +10% total return over the next 12 months
<b>SELL</b>	<-10% total return over the next 12 months

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