ILBE Spa

Sector: Media content production

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Return less visible, but stock now at deep value

Iervolino & Lady Bacardi Entertainment (ILBE) is an Italian cinema, TV and web content production company with an international footprint and strong focus on OTTs contents, listed on Euronext Growth Milan and Paris. It produces diversified contents for global distribution, focused on production and IP ownership.

FY22 revenues +6%, lower margins on faster D&A + tough comp

FY2022 production deliveries were in line with expectations (revenues of €161mn (+6% y/y), but EBIT was down to €9.8mn from €23.5mn of FY2021 and below €21.6mn expected, due to 1) accelerated D&A of family movies; 2) lack of sizeable revenues from one-off deals on IPs (€30.2mn in FY21); 3) high service costs for Metaverso contents. The bulk of revenues (72%) came from animations (production, executive production and IPs), with executive production of *Puffin: impossible* finally running at full speed (€30.3mn revenues), while the delivery of *Muti* accounted for €17mn.

Net debt better than expected, backlog supportive

Dec 2022 net debt was down to €25.8mn from €29.3mn of Dec 2021, also due to a better than expected NWC (smarter management of fiscal credits) and lower investment in contents/distribution rights (€95mn). As for updated backlog and target value of projects, management indicated €173mn (2023-24) and €311mn (2023-25) respectively, slightly below the last release, but enough to fully support our revenues forecasts.

Revenues up, EBIT unchanged, net debt peaking in FY23

Our revised model factors the updated backlog and projects targeted, a faster D&A policy and higher cost of debt, and now includes FY25E. The new 2023E-24E forecasts show slightly higher top line, broadly unchanged EBIT, despite lower margins (avg 11.2% vs previous 12.4%), and lower cash generation (cumulated €-0.6mn vs previous €0.6mn). Yet, we see as a negative take-away the FCF expected for FY25E, as it comes below our original medium term expectations, due to the deterioration of competitive outlook and recent industry dynamics, driven by OTTs.

Fair value adj. for higher rates & lower M/T free cash flow

The stock has performed poorly over the last months in absolute and relative terms and now it trades at even deeper discount to peers: 2023E EV/EBIT of 3.5x vs peers' 10.7x. On the back of three methodologies - relative peers' multiples, EFCF yield analysis and DCF (WACC to 10.6% from 9.3%) – we reduce our fair value from €3.10 to €2.25, and despite we do not see a trigger in the short term, we reckon the stock offers deep value on any metric.

Fair Value (€)	**2.25**
Market Price (€)	**0.91**
Market Cap. (€m)	**32.1**

KEY FINANCIALS	2022A	2023E	2024E
REVENUES	161.0	166.9	174.5
EBITDA	129.6	133.0	138.7
EBIT	9.8	18.1	20.5
NET PROFIT	3.5	11.8	14.1
EQUITY	89.4	101.4	115.4
NET FIN. POS.	-25.8	-30.5	-26.4
EPS ADJ. (€)	0.16	0.33	0.40
DPS (€)	0.00	0.00	0.00

Source: Company (historical figures), Value Track (2022A-24E estimates)

RATIOS & MULTIPLES	2022A	2023E	2024E
EBITDA MARGIN (%)	80.5	79.7	79.5
EBIT MARGIN (%)	6.1	10.8	11.7
NET DEBT / EBIT (x)	2.6	1.7	1.3
NET DEBT / EQUITY (x)	0.3	0.3	0.2
EV/SALES (x)	0.4	0.4	0.3
EV/EBITDA (x)	0.4	0.5	0.4
EV/EBIT (x).	6.0	3.5	2.9
P/E ADJ. (x)	5.7	2.7	2.3

Source: Company (historical figures), Value Track (2022A-24E estimates)

STOCK DATA	
FAIR VALUE (€)	2.3
MARKET PRICE (€)	0.9
SHS. OUT. (m)	35.3
MARKET CAP. (€m)	32.1
FREE FLOAT (%)	21.7
AVG. -20D VOL.	16,206
RIC / BBG	IE.MI / IE IM
52 WK RANGE	0.83-1.99

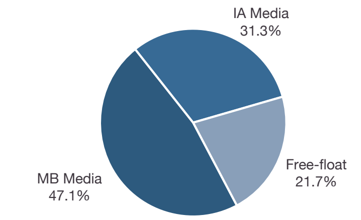
Source: Stock Market Data

Business Description

ILBE (Iervolino & Lady Bacardi Entertainment, ex Iervolino Entertainment) is an Italian cinematographic production company with a global footprint that, through its headquarters in Rome and thanks to its founder and CEO's relationships and experience in the world of Cinema, is able to produce "Hollywood Style" movies and web series. It produces diversified contents for an international audience, focusing on the core production phases and IP ownership and exploitation.

The company is listed since August 2019 on Euronext Growth Milan (and Paris since 2022) and the IPO proceeds were used for funding the accelerating growth in high quality and innovative contents for cinema, TV and streaming platforms.

Shareholders Structure



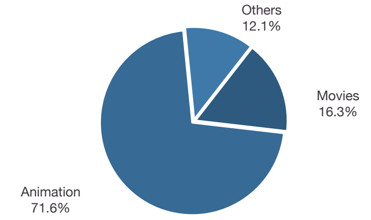
Source: ILBE

Key Financials

€'000	2022A	2023E	2024E	2025E
Total Revenues (VoP)	**161.0**	**166.9**	**174.5**	**184.3**
Chg. % YoY	5.6%	3.7%	4.6%	5.6%
EBITDA	**129.6**	**133.0**	**138.7**	**145.9**
EBITDA Margin (% of VoP)	80.5%	79.7%	79.5%	79.2%
EBIT	**9.8**	**18.1**	**20.5**	**21.0**
EBIT Margin (% of VoP)	6.1%	10.8%	11.7%	11.4%
Net Profit	**3.5**	**11.8**	**14.1**	**15.0**
Chg. % YoY	-80.9%	nm	19.6%	6.7%
Net Fin. Position	**-25.8**	**-30.5**	**-26.4**	**-19.2**
Net Fin. Pos. / EBITDA (x)	0.2	0.2	0.2	0.1
Capex	-99.4	-115.1	-118.4	-127.3
OpFCF b.t.	**8.2**	**1.3**	**10.6**	**13.2**
OpFCF b.t. as % of EBITDA	6.4%	1.0%	7.6%	9.0%

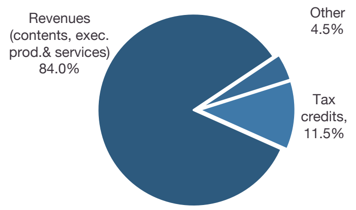
Source: ILBE (historical figures), Value Track (estimates)

VoP 2022 by production type



Source: ILBE

VoP 2022 by type



Source: ILBE

Investment Case

Strengths / Opportunities

- ILBE is set to benefit from the rising global demand for audio-visual contents, as it produces contents with international appeal, ranging from movies to animation;
- The company has recently focused on short contents, i.e. short animation contents for web series with hundreds of episodes (of 5-8') and time horizon of many years;
- ILBE focuses on the core production phases and IP ownership and exploitation, with a risk-adverse approach: it gets funding of new productions ahead of kick-off.

Weaknesses / Risks

- In the content production industry, the FCF lags behind the revenues recognition. This implies a small and fast growing producer faces material ST funding needs;
- The Company is highly dependent upon its founder, CEO and Chairman Mr Iervolino, given the lean structure and his key relationships in the industry;
- The OTTs boom have challenged the media & content industry driven by box office and ad spending and is questioning the video content long term returns/life spam.

Stock multiples @ €2.25 Fair Value

	2023E	2024E
EV / SALES (x)	0.7	0.6
EV / EBIT (x)	6.1	5.2
EV / CAP.EMP. (x)	0.8	0.7
OpFCF Yield (%)	1.2	10.0
P / E (x)	6.8	5.6
P / BV (x)	0.8	0.7
Div. Yield. (%)	0.0	0.0

Source: Value Track

Key recent events & backlog

Recent events

During 2022 ILBE closed a small acquisition, a number of new production and distribution contracts and undertook a few funding decisions. All this is summarised below:

1. Acquisition of SoBe Sport

In **February** the company has signed an agreement to acquire a 60% stake in **SoBe Sport**:

- it is a sports communication and marketing company for professional athletes and coaches, with 2021 Revenues of €2.0mn and EBITDA of €0.7mn;
- ILBE indicated a **€658k** payment in **cash** for 31.4% of share capital and the issue of 244.8k **new ILBE shares** for a total value of **€514k** (valued at €2.1 per share, i.e. the share price at the acquisition time) for the remaining 28.6% stake;
- the deal also contains **call & put** options for ILBE and the seller for the acquisition of the remaining 40% share, for a total value of €1mn, to be activated by March 2024 (in July-Sept 2023 by the seller), equally covered by a mix of a cash (40%) and paper (60%) issued at market price;
- the cash position of SoBe Sport at acquisition was €230k and we calculate an acquisition multiple of ca **0.9x EV/Sales and 4x EV/EBIT** (2022), including the put & call.

2. New production, executive production and distribution agreements

Following the release of interim results, the following new contracts were announced:

- Between November 2022 and February 2023, ILBE worked at the executive production of ***Verona*** a musical based on the *Romeo and Juliet* by W. Shakespeare, starring Rupert Everett, Rebel Wilson, Jason Isaacs, Clara Rugaard, Jamie Ward and produced in the Veneto and Emilia Romagna regions. The movie is in post-production and should contribute to revenues in 1H2023;
- In December 2023 ILBE signed a distribution agreement with Wonder Capital LLC and WWPS for the movie ***Paradox Effect***, due for delivery in 1H 2023, with a Minimum Granted of €4mn;
- ILBE announced in March 2023 the production of the movie "***Maserati: a racing life***", the history of Ettore and Ernesto Maserati, founders of the renown Italian automotive company. The title is still in early development phase and hence there are no additional details.

3. New loans, rising rates and Shares buy-back programme

During FY2022 ILBE secured **additional funding** from major Italian and international banks (Banca Intesa, BPM. Mediocredito Centrale, Deutsche Bank), for around €9.2mn, with a 2/5 years' loan duration and rates at Euribor 3M + 2.30% / 2.75% Spread. As of December 2022 ILBE reported a gross debt of ca €56.4mn – including €2.7mn or leasing (IFRS 16) - with a cash & financial assets position of €30.6mn, including €9.5mn invested in mutual funds, which have caused a €1mn non cash loss in the P&L, and €6.5m of financial credits towards clients (bearing interest rates).

According to debt repayment schedule, ca. €9.4m or 17% of gross debt is due in FY2023, but the high net cash available should represent a reassuring element and ease the company's refinancing pressure. In terms of funding cost, however, FY 2023 will face **rising interest charges**, as almost 70% of gross debt bear variable rates and this will bring additional costs for ca. €1mn, according to management.

Between May and December 2022 ILBE purchased 150k shares on Euronext Growth Milano at a weighted average price of €1.5 (€225k) and additional shares were purchased on Euronext Growth Paris, for a total amount of €232k in the year.; while over the period Jan-April 2023 additional 3k shares were purchased on EGP. We estimate that as of today, value of **treasury shares equals ca €140k** i.e. 157k shares at a price of €0.9p.s. and equivalent to the 0.4% of the share capital, while the cost was around €240k.

Backlog

The contracted production backlog for delivery over 2023-2024 was equal to **€172.9mn** as of December 2022, compared to €224.9mn as of June 2022. Of these, we estimate ca. €96mn are related to activities in the FY2023.

The **backlog** is composed as follows:

- New sequel to the animated series Arctic Friends and Puffins, titled ***Baby Puffins & Bunny*** consisting of 405 episodes, each lasting 5 minutes, of which 135 episodes were produced in FY22 as *animatics*. The backlog of the new animated production is **€91.9mn,** with a production plan spread between 2023 and 2024;
- **3 Puffins animated series** (*Mini Puffins Wonder, Swifty, Super Impossible*) of 100 episodes each in the new "short" format, lasting 60 seconds. In FY22, €13.5 were realized while **€5.3mn** are expected in the first half of 2023;
- **Executive production of the *Puffins Impossible* animated series**, and related service activities including IP exploitation licenses, consisting of 270 episodes. The backlog of executive production and licensing on IP is **€62.3mn**, (€20.6mn were produced in 2H22) with a production plan spread between fiscal years 2023 and 2024;
- Production of the film ***In the Fire*** for **€4.5mn**, initially planned for FY2022 and then postponed and scheduled for delivery in the 1H23;
- Residual Backlog of **€4.9mn** related to the production of **3 Animation Films** (85' each), based on Puffins / Artic Friends / Puffins Impossible's characters, after having delivered €18.1mn in 2H22 in *animatics* format;
- Production of the film ***Paradox Effect*** for **€4.0mn**, scheduled for delivery in the 1H23.

Management provided also the updated 3-year slate of **target projects for the period 2023-2025E**, for a total value of **€311mn**, compared to the €395mn value provided in June 2022 (for deliveries over 2022-2024E). This target includes ca. 56 projects which should be split as follows in terms of contribution to revenues:

- Ca.€234mn in new **productions**, which include animations, movies and other scripted and unscripted contents in various stage of development;
- Ca. €26mn of revenues from **service** activities (including executive production, digital delivery – Arte Video - and concession of IPs);
- Ca. €52mn of revenues from projects of **celebrity management and digital ADV** (Red Carpet, SobeSport).

On top of these projects, summarized in the table below, the executive production business continues with production like **Ferrari** and the US-produced movie ***"Verona"***, described above. We remind that these projects would be recognised by ILBE only in terms of net fee in the P&L, with a limited top line contribution, but with a potential attractive contribution in terms of EBIT and cash flow, according to management plans.

ILBE: Backlog and Target Projects Value 2023-2025E

(€mn)	Type	Delivery 2023-2025	o/w FY23	o/w FY24	Episodes (#)
Baby Puffins & Bunny	Series	91.9	45.9	45.9	405
3 "Shorts" Series	Short Series	5.3	5.3		300
Puffins Impossible (Servicing)	Web Series	62.3	31.2	31.2	270
In the Fire	Film	4.5	4.5		
Animation Films (3 x 85')	Film	4.9	4.9		
Paradox Effect	Film	4	4		
Total Contracted Backlog (2023-24E)		**172.9**	**95.8**	**77.1**	
Animation productions		114.9			19 projects
Audiovisual productions		22.6			9 projects
Films		74.7			12 projects
Unscripted Projects		21.6			16 projects
Total Production under development		**233.7**			
Servicing & Licensing (incl. Arte Video)		25.9			-
Celebrity Mngt, Digital ADV (Red Carpet. Sobe Sport)		51.8			-
Total Target Projects Value (2023-25E)		**311.2**			

Source: Value Track Analysis

Sector overview

The content industry is currently facing a series of structural changes, combined with macro challenges and the impact of Covid-19 pandemic, not fully recognised in its long term yet. The combines effect of a) rising demand of content volumes by streaming platform (OTTs), b) flattening pace of growth in penetration of the large global players (like Netflix) with rising competition and rising attention on costs and returns, c) slower than expected recovery of box office revenues in the post-pandemic, among the major sector drivers, rises a few questions on the medium/long term impact for content providers' business model and returns.

These question marks, already outlined in our latest reports, have more recently triggered a few write-offs in the value of smaller players' IPs libraries (e.g. Mondo TV, Xilam) - in line with the "accelerated" write-off decided by ILBE - as the expected returns of contents seem to polarise around stronger contents at the expenses of mid tear ones.

2022 Box Office revenues on the rise, but pre-Covid levels not even at sight yet

Worldwide, **global box office revenues were at USD25.9bn**, according to Gower Street Analytics, of which USD18.4bn were collected outside the US. This is a **27% increase over 2021**, but it is still **35% below the average** of the three-year period **2017-2019**: there are still about USD14bn missing. In addition, it should be kept in mind that China before the pandemic competed with the United States to become the number one global film market, and now finds itself far behind, because i) the zero contagion policy caused the closure of many cinemas for much of 2022 and ii) a substantial embargo on international films that accounted for a good percentage of receipts before the pandemic hit the business. In more details:

- the **US** market remains the leading one with 2022 revenues around USD7.6bn, jumping from USD4.5bn of 2021, but still one third lower than pre-Covid;
- the **EMEA** region collected USD7.1bn, +52% y/y and -31% compared to the pre-pandemic three-year period;
- the **Asia/Pacific** region (excluding China) raised USD5.2bn (+49% y/y, -26% vs pre-pandemic);
- **China** closed 2022 at USD4.3bn, i.e. 35% below 2021 and 49% below the average three-year pre-pandemic period;
- the **Latin American** region raised USD1.8bn (+87%/-30%), while **Russia** saw the steepest drop, mainly due to the embargo: only USD 310m was raised in 2022, a drop of 43% compared to 2021 and almost 60% compared to pre-pandemic levels.

Gower Street forecasts for 2023E global Box Office **revenues at a value of USD29bn or +12%** vs USD25.9bn of 2022 and still USD11bn below the pre-pandemic levels.

OTTs revenues and penetration are already huge and keep growing

Over-the-top video (OTT video) refers to the transmission and sale of video content over the internet. Users can access OTT content via networked devices such as PCs, laptops, tablets, mobile phones and set-top boxes and game consoles. By controlling the IP address, content can be restricted to specific countries.

This includes

- all advertising-financed contents, from premium to user-generated (OTT Video Advertising);
- Video-on-Demand (VoD) services, with three fee-based business models, often combined in hybrid models: i) time-limited individual rentals (transactional VoD or TVoD), ii) the

subscription to a video streaming service (such as Netflix or Amazon Prime Video) with unlimited access to the content offered for the duration of the subscription (subscription VoD or SVoD) and iii) individual purchases of films or series as direct downloads, analogous to the purchase of a DVD or Blu-Ray (electronic sell-through or EST) or live events (PPV).

These streaming and sale platforms keep growing, with

- Revenue in the **OTT Video segment seen at USD316.1bn in 2023E,** with the largest segment being OTT Video Advertising with a market volume of US$205.1bn in 2023E**;**
- Revenue expected to show an **annual growth rate (CAGR 2023-2027) of 10%**, resulting in a projected market volume of USD462.9bn by 2027;
- The **VOD** market representing the residual **USD111bn revenues, still almost 4x the box office** market;
- Most revenue generated in the US (US$137.8bn in 2023E, or 43% of total);
- In the OTT Video segment, the number of users expected at 4.22bn by 2027E, with a user penetration growing from 45.7% in 2023E to 53.0% by 2027;
- Average 2023E revenue per user (ARPU) in the OTT Video segment at US$90.

…but competition heats up

Under the above consideration, there is no surprise that the OTT streaming platform are those driving the media industry at the moment, and in this respect ccompetition is increasing and is expected to heat up in the coming years. For the first time in a decade, Netflix, Inc. lost subscribers in the first half of 2022 (in Europe and US): inflation, the Russia-Ukraine conflict and fierce competition were a few reasons behind this loss, according to the company's statement, but nevertheless this is a reflection of changing landscape in the OTT streaming industry.

Netflix, started as a disruptor in the entertainment industry, but has being turning over the years into another content provider, as Disney+ and HBO Max and others have diverse portfolios including consumer products, theatrical services, etc. This changing landscape has also forced the company to rethink its strategy and diversify its source of generating revenue, by pushing advertising-supported content, which management had previously opposed.

The increasing pressure on users' acquisition and retention and higher focus on bottom line and returns to shareholders are likely to put pressure on the whole media content value chain, where rising interest rates add a further hurdle for a "working capital intense" business.

All this seems to trigger a few trend in the industry, especially among the smaller players:

- pressure on margins, as bargaining power of tier 2 content producers or distributors is limited;
- shorter duration of contents (with limited backend revenues and virtually no long tail income);
- rising demand of international executive productions, but margins and payment terms are tight;
- the value of the IPs and distribution rights' library may be at risk and may require some "impairments" or change in their amortization rates (e.g. Mondo TV, Xilam and to some extent ILBE on 2022 results).

FY2022: higher D&A impacts bottom line

FY 2022 results' main outcomes are the following:

- **Total Revenues at €161.0mn** vs. €152.3mn of FY21 (+6% y/y), supported by i) animations' productions, (53% of total revenues, excluding executive productions); ii) three movies and two Amazon docufilms; iii) the concession of Puffins characters' IPs and other services (a €10.9mn, 7% of total revenues); iv) steadily growing executive production business (19% of total revenues) and some early revenues from distribution (€3.4mn);
- **EBIT at €9.8mn** vs. €23.5mn as of 31 December 2022 and broadly in line with 1H**,** as the 2H margin is weighed down by faster D&A related to the impairment of the Christmas/Family Movies' recoverable amount under the long term distribution contracts signed. According to management, the one-off adjusted EBIT stands at €20.8mn (-15% y/y), with margin at 12.9% (vs. 15.4% of FY21);
- **Net profit at €3.5mn** vs €19.4mn FY21, burdened by the above mentioned non-recurring amortizations as well as by increased financial charges (€5.2mn) linked to hiking interest rates and increased gross debt load, but also impacted by unrealised capital loss on financial assets (bonds) for €1mn and slightly higher exchange rates losses (€1.7mn vs €1.3mn of FY21);
- **Net Debt decreased to €25.8mn** from €29.3mn of Dec 2021, as cash flow fully funded investments in new productions and distribution rights as well as NWC requirements, while a smart executive production agreement, allowing a faster utilization of fiscal credits, reduced NWC and net debt by €6.5mn.

Overall the FY22 results are slightly below our expectations in terms of margins and net profit, with most of the difference being due to higher D&A and financial charges, while the free cash flow generation has been slightly better than expected due to a better NWC management.

ILBE: Key Financials

(€mn)	FY21A	FY22E	FY22A	Change YoY (%)
Total Revenues	152.3	158.9	161.0	*5.7%*
EBIT Adjusted	24.4	21.6	20.8	*-14.9%*
EBIT Reported	23.5	20.1	9.8	*-58.5%*
Net Profit	18.4	11.9	3.5	*-80.9%*
Group Equity	85.6	98.0	89.4	*4.4%*
Net Financial Position	-29.3	-28.4	-25.8	*nm*

Source: Value Track Analysis

Revenues increased with a more diversified but "poorer" mix

Group FY2022 revenues came from:

- **Productions & IPs equal to €135.2mn**, slightly increasing from €132.1mn in FY21 and marked by a more even distribution between animated productions (53%), movies (16%), animation services / executive production (28%) and licensing of animated characters and revenues from distribution (2% each);
- **Other Revenues lines** split in i) Celebrity Management, digital ADV (Red Carpet, Sobe Sport) and ii) Authoring & Digital Delivery (Arte Video) and with total revenues of **€7.3mn**, growing 36% y/y and supported by the consolidation of Sobe Sport from mid-March;
- Increasing amount of related **Tax Credits**, exceeding ca. **€18mn**.

ILBE: Total Revenues FY21A – FY22A

(€mn)	FY21A	FY22A	Change YoY (%)
Revenues from Productions & IPs , o/w	132.1	135.2	2%
Content Production	*81.9*	*89.9*	*10%*
Distribution	*0.0*	*3.4*	*nm*
Characters & Pipeline licensing	*37.1*	*3.0*	*nm*
Services (executive prod.)	*12.9*	*38.2*	*195%*
Celebrity Mgmt, casting & Digital ADV	4.2	5.7	36%
Authoring, Encoding & Digital delivery	1.0	1.4	40%
Revenues from Sales	**137.3**	**142.3**	**4%**
Other Revenues	0.2	0.1	nm
Tax Credits	14.8	18.6	+25%
Total Revenues	**152.3**	**161.0**	+6%

Source: ILBE, Value Track Analysis

Production & management of contents / IPs, i.e. the core business of ILBE, reported revenues of ca. €135mn out of a total €142.3 top line (before tax credits) and 95% of Group revenues including tax credits. The main contributors were:

#1 Content Production activities (€109mn incl. tax credits): higher diversification

As far as Content Production is concerned, the vast majority of revenues came from the *Puffins*-related pipeline (ca. 75%), split in 4 main projects. Another notable contribution was made by the film *Muti,* which accounted for 16% of revenues.

ILBE: Content production details FY21A – FY22A

(€mn)	FY21A	FY22A	Change YoY (%)
Arctic Friends	59.8	1.1	*-98%*
Waiting for the Barbarians	0.5	0.1	*-70%*
Puffin	37.9	20.6	*-46%*
Puffin Shorts	0.0	13.5	*nm*
Tell it like a Woman	2.6	0.4	*-84%*
Giving Back	0.0	3.5	*nm*
Paradox Production	1.2	3.9	*221%*
Muti	0.0	17.1	*nm*
WWPS/Universal	5.1		*-100%*
Baby Puffin & Bunny	0.0	29.5	*nm*
WW Productions	0.5		*-100%*
3 Animation Movies	0.0	18.1	*nm*
Amazon Documentaries	0.0	0.0	*nm*
Revenues from Content Productions (incl. tax credits)	**107.5**	**109.0**	***1%***

Source: ILBE, Value Track Analysis

The distribution of revenues within the content production and IPs business demonstrates a significant enhancement in the variety of projects undertaken.

ILBE: Revenues from Content Production breakdown in FY21 (left) and FY22 (right)

Source: Value Track analysis, (*) Including Tax Credits

#2 Services / Executive Production activities (€38.2mn) carried by Puffins Impossible

The second largest contributor is services (including executive productions) for €38.2mn in FY22, and here the bulk comes from **"Puffins: Impossible"** servicing, i.e. the executive production carried by Iervolino Studios (Serbia) with recognition of revenues for a total of €30.3mn vs €10.8mn in FY22.

#3 Licensing (€3.0mn): more volatile activities with tough comps

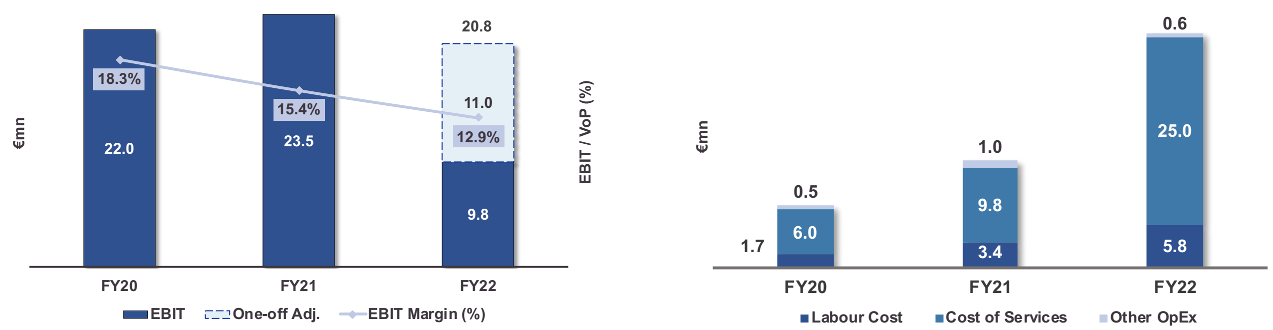
The FY22 revenues from concessions / licensing out of ILBE IPs (either characters, fonts or production pipeline) and other services, faced the tough comp of FY21 (€37.1mn), that benefitted from a one-off deal on concession of the production *Pipeline* & *font* license, worth €30.2mn.

EBIT and net result affected by higher service costs and much higher D&A

In terms of costs, margins and net profit the key elements are the followings:

- **EBIT Adjusted** in FY22 closed down to €20.8mn vs €24.4mn of FY21, with margin at ca. 12.9% or 310bsp below previous year;
- **Reported EBIT** (including the extraordinary costs) was €9.8mn, i.e. reported EBIT margin fall is ca. 680bps;

ILBE: FY2020-21-22: EBIT evolution (left) and Opex evolution (right)



Source: ILBE, Value Track Analysis

In terms of costs, the major swing y/y was witnessed by:

i) personnel costs (€5.8mn as of FY22 vs. €3.4mn FY21), due to Iervolino Studios hiring plan;

ii) other Opex (€25.6mn as of FY22 vs. €10.8mn FY21), with the difference mainly attributable to €9.3mn cost of outsourced services related also to animated content intended for the metaverse, as well as a general service costs increase;

iii) amortizations, burdened by an extra €9.5mn amortization (i.e. faster than initially expected) on the Family Movies' recoverable amount.

- **Net Profit** burdened also by increased Net financial charges (€5.2mn), reflecting a higher cost of debt, and by foreign exchange losses and adjustments on financial assets' value (€1.7mn and €1.0mn respectively).

ILBE: Income Statement (FY21-FY22)

€mn	2021A	2022A
Value of Production	**152.5**	**161.0**
Other Opex	-10.8	-25.6
Labour Cost	-3.4	-5.8
EBITDA	**138.2**	**129.6**
D&A	-114.8	-119.9
EBIT	**23.5**	**9.8**
EBIT margin (%)	***15.4%***	***6.1%***
Net Financial charges	-3.1	-5.2
Taxes	-1.9	-1.0
Net Profit	**18.4**	**3.5**

Source: ILBE, Value Track Analysis

Cash Flow & Balance Sheet

At Balance Sheet level we note:

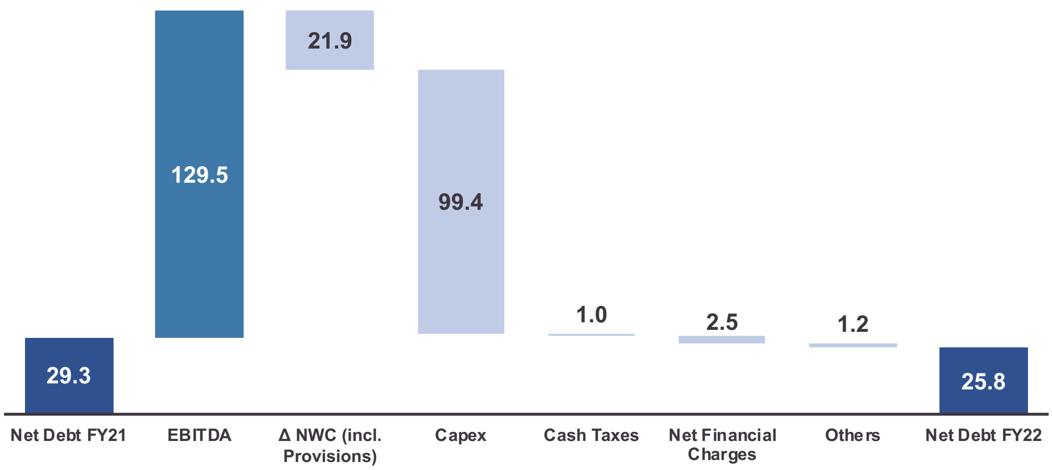
- **Net fixed assets** at €89.4mn, down by ca. €21.7mn attributable to reduction in capitalized production costs of products delivered and in progress, which stood at €96mn level;
- **Working capital** at €26.2mn (vs. €4.6mn in Dec 2021), driven by increased trade receivables related to key productions;
- **OpFCF$_{a.t.}$** back to positive for ca. €7.2mn on lower investments (€99.4mn), despite lower EBITDA and a €21.6mn Net Working Capital absorption, material but lower than expected;
- **Net Debt** stood at €25.8mn vs. €29.3mn as of Dec 2021, slightly improving due to smarter management of fiscal credits and lower investments, as said.

ILBE: Balance Sheet (FY21-FY22)

€mn	2021A	2022A
Working Capital	4.6	26.2
Net Fixed Assets	111.0	89.4
Provisions	0.7	0.4
Total Capital Employed	**114.9**	**115.2**
Group Net Equity	**85.6**	**89.4**
Net Fin. Position	**-29.3**	**-25.8**

Source: ILBE, Value Track Analysis

ILBE: FY21 – FY22 Cash Flow Statement



Source: ILBE, Value Track

Review of 2023-2025E forecasts

Following FY2022 results and recent news flow, we have update our model and expanded our forecast horizon to FY2025. Company's 2023-2024E forecasts compares to previous ones as follows:

- **Revenues slightly up**, to factor updated backlog and despite some changes in revenues mix;
- **Operating Profitability down**, with EBIT margins reduced by an average of 120bps;
- **Higher Net debt**, peaking in 2023 and then declining by ca. €6mn per year.

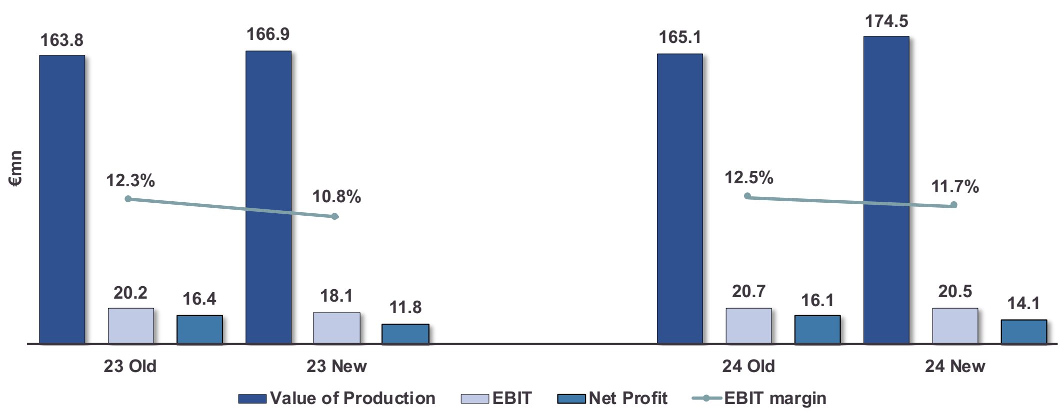
Yet, the current industry scenario is expected to impact ILBE's long run financial profile, i.e. a lower steady-state EBIT margin (ca.11.5%) and lower free cash flow generation capacity (€5-10mn per year over the next 5 years).

ILBE: Old vs. New Estimates 2023E-24E

	2023E			2024E		
€mn	Old	New	Δ	Old	New	Δ
Total Revenues	**163.8**	**166.9**	**2%**	**165.1**	**174.5**	**6%**
EBIT	**20.2**	**18.1**	**-10%**	**20.7**	**20.5**	**-1%**
EBIT Margin (%)	12.3%	10.8%	-148bps	12.5%	11.7%	-80bps
Net Profit	**16.4**	**11.8**	**-28%**	**16.1**	**14.1**	**-13%**
Net Fin. Position	**-28.0**	**-30.5**	**-2.5**	**-27.8**	**-26.4**	**1.5**
OpFCF after tax	**2.2**	**-1.6**	**nm**	**2.0**	**7.1**	**nm**

Source: Value Track Analysis

ILBE: Old vs. New Estimates 23E-25E (P&L)



Source: Value Track Analysis

Revenues up following Backlog update, EBIT margin converging towards 11.5%

The impact of our update on 2023E-25E financial forecasts can be summarized as follows:

- **Revenues** – slightly upward to factor higher tax credits and improved outlook for the minor businesses (Red Carpet, SoBe Sport), with some adjustments in revenue mix related to Christmas movies impairment, entirely offset by the additional deliveries factored in the updated Backlog;

- **EBIT margin** – 120bps average deterioration over the forecast period and henceforth expected to converge towards the 11.5% level. This comes as a result of: 1) **higher expected D&A** (avg. ca.€118mn over the period 2023-25E, vs. our previous assumption of ca. €81mn), due to a faster depreciation policy reflecting the structural shortening of the assets' useful life in accordance with the "*Film Forecast Computation Method*"; 2) **Increased labour cost** following the Group-wide recruitment plan (+€4.0mn in the forecast period compared to our last update); and despite 3) **lower cost of services** due to a rationalization and cost optimization of the executive production business in Serbia (including metaverse related costs);
- **Net Profit** –burdened by higher interest costs due to rising interest rates and to the new debt structure (+ ca.€1mn average cost per year, compared to our last update), yet more than offset by lack of losses on exchange rates and write-offs from marked-to-market of financial assets.

ILBE: 2022-2025E Profit & Loss

(€mn)	2022A	2023E	2024E	2025E
Revenues from Sales	135.2	138.2	138.8	145.8
Other Revenues	7.2	12.0	19.0	21.0
Tax credits	18.6	16.7	16.7	17.5
Total Revenues i.e. VoP	**161.0**	**166.9**	**174.5**	**184.3**
Cost of Sales	-25.6	-27.4	-28.9	-31.2
Labour Costs	-5.8	-6.5	-6.9	-7.1
EBITDA	**129.6**	**133.0**	**138.7**	**145.9**
Depreciation / Provisions	-2.9	-0.8	-1.2	-1.0
Amortization	-116.9	-114.2	-117.0	-123.9
EBIT	**9.8**	**18.1**	**20.5**	**21.0**
EBIT Margin (%)	**6.1%**	**10.8%**	**11.7%**	**11.4%**
Net Fin. charges & others	-5.2	-3.4	-2.9	-2.3
Pre-Tax Profit	4.5	14.7	17.6	18.8
Taxes	-1.0	-2.9	-3.5	-3.8
Net Profit	**3.5**	**11.8**	**14.1**	**15.0**

Source: Value Track Analysis

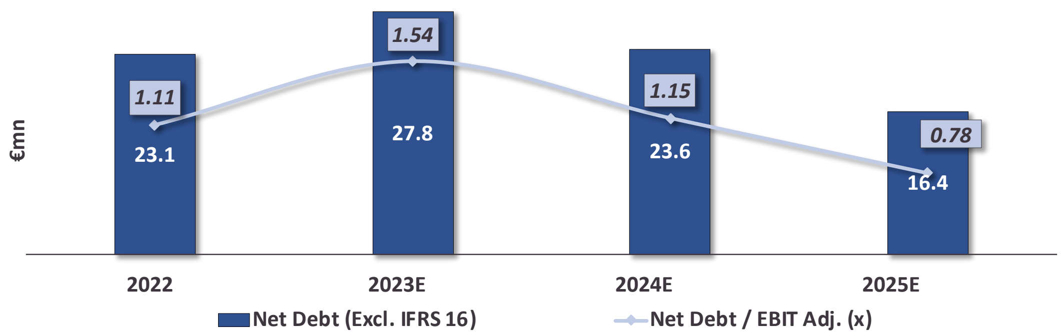
Net Debt peaking in 2023E, then some Cash Generation from 2024E

As for Balance sheet and Cash Flow, we expect:

- **Net Fixed Assets** to increase only mildly, coherently with investments in new productions and rights, up to ca. €92mn in 2025E, i.e. much below our previous assumptions, due to higher D&A and compensated by higher capital required in the production/distribution process (NWC);
- **Net Working Capital** gradually moving up to 38/40%, burdened by a structurally adverse trade receivables/payables dynamics related to cinema productions activities;
- **Investments in new productions and rights** (i.e. Capex) at average €120mn in 2023-25E, well above the 2022 level (€95.6mn) and still expected to absorb most of the cash generated;
- **Net Debt peaking in 2023E and then reducing gradually in following years**, where we expect a steady-state net cash generated from ILBE's business to be ca. €7mn per year (FY2025E). We forecast Net Debt/EBIT at ca. 1.69x in 2023E (1.54x excluding IFRS16), suggesting that ILBE will have to stick to a very disciplined strategy in terms of contents production and M&A or alternatively renegotiate the covenants.

In short we do not expect free cash flow to drive any visible de-leverage before 2025E, after which, cash generation will dependent on the evolution of size and quality of the backlog and productions.

ILBE: Adj. Net Debt (*) / EBIT 2022A-2025E



Source: Value Track Analysis, Net Debt adjusted for IFRS-16 elements

ILBE: 2022A-25E Balance Sheet

(€mn)	2022A	2023E	2024E	2025E
Net Working Capital	26.2	42.9	52.7	58.3
Net Fixed Assets	89.4	89.6	89.7	92.1
Provisions	0.4	0.6	0.7	0.8
Capital Employed	**115.2**	**131.9**	**141.8**	**149.6**
Group Net Equity	**89.4**	**101.4**	**115.4**	**130.4**
Net Fin. Position [i.e. Net Debt (-) Cash (+)]	**-25.8**	**-30.5**	**-26.4**	**-19.2**

Source: Value Track Analysis

ILBE: 2022A-25E Cash Flow Statement

(€mn)	2022A	2023E	2024E	2025E
EBITDA	**129.6**	**133.0**	**138.7**	**145.9**
Op. WC Requirements	-21.6	-16.7	-9.8	-5.6
Capex	-119.8	-115.1	-118.3	-127.3
Change in Provisions	-0.3	0.1	0.1	0.1
Cash Taxes	-1.0	-2.9	-3.5	-3.8
OpFCF a.t.	**7.2**	**-1.6**	**7.1**	**9.4**
Capital Injection	0.5	0.0	0.0	0.0
Other (Incl. Fin. Inv.)	-1.7	0.3	0.0	0.0
Net Financial Charges	-2.5	-3.4	-2.9	-2.3
Change in Net Fin. Position	**3.5**	**-4.8**	**4.2**	**7.2**

Source: Value Track Analysis

Valuation

As outlined in our last reports on ILBE, there are a few key points to consider in its investment case, and in particular we underline the following:

- As for ILBE top line, forecasts have been supported by a solid backlog over the past quarters and consensus has been relatively resilient as for revenues growth, however we acknowledge that Dec 2022 revenues closed up 6% y/y and that backlog has been reported slightly below Sept 2022 and in line with June 2022. This seems to confirm that **growth is expected to remain low single digit** in coming years;
- The lower growth is also driven by a combination of increasing capital needs (even more penalizing with rising interest rates), decreasing margins on productions and lower visibility on distribution revenues and timing. These are very much trends shared by a number of players of the content industry, which have suggested **longer pay-back periods**;
- The launch of a new business line focused on large **international executive production**s has not proven yet to be as profitable and capital light as expected, albeit we would give management some more time to provide more encouraging evidence about the actual potential of this business.

All the considerations above have lead us to revise down the free cash flow profile of ILBE in the medium term, with much more cautious assumptions about the sustainable return of the business. This is not visible in the short term from our forecasts, also because a more efficient use of fiscal credits reduced Dec 2022 net debt, and cannot be linked to the cash flow generation of a single year, as this may depend on the specific slate of production in that year. Yet, this affects the expected medium term free cash flow generation of the Group. In other words, the **low visibility about the actual returns of ILBE business model**, in the post-pandemic word driven by OTTs remains the key point, as already outlined in the past:

- **the stock seems to offer deep "value"** in absolute and relative terms, on undemanding multiples;
- but **the medium term/sustainable return of ILBE business seems to keep lowering,** despite the top line and EBIT consensus are relatively stable;
- hence the stock remains one of the worst performers among peers **(-29% YTD)** and it needs a **trigger for its rerating,** as deep value does not seem a trigger in itself;
- **the trigger** may come either from some evidence that **return on production is resuming and/or** that **FCF generation is turning positive**, i.e. in FY2025, according to our forecasts.

The corollary of this picture is that we increasingly focus on methodologies driven by FCF, and widen our valuation approach, averaging **EFCF yield, DCF and peers' multiples analysis**:

- the FCF driven methodologies imply more cautious valuations, driven by lower FCF forecasts, rising interest rates and higher equity risk premium compared to our last reports;
- on the other hand, peers' multiples provide more bullish outcomes, supported by relatively resilient stocks' performance, combined in a few cases with falling earning consensus, albeit these multiples remain relatively scattered around;
- combining the drivers above the **fair value of the stock goes from €3.1 p/s to €2.25 p/s**, still 147% above its current market value;
- at fair value ILBE would trade at EV/EBIT of 6.1x and P/E of 6.8x for 2023E, i.e. at ca. 25% discount to peers, justified by its slower growth and/or lower free cash flow and, in some cases, by its relatively lower scale.

ILBE: Sensitivity of implicit stock ratings at different stock prices

Share price (€)	EV / EBIT (x) 2023E	EV / EBIT (x) 2024E	P / E (x) 2023E	P / E (x) 2024E
€ 0.9	3.5	2.9	2.7	2.3
€ 1.4	4.3	3.6	4.0	3.4
€ 1.8	5.2	4.4	5.4	4.5
€ 2.3	**6.1**	**5.2**	**6.8**	**5.6**
€ 2.7	6.9	5.9	8.0	6.7
€ 3.2	7.8	6.7	9.4	7.8
€ 3.6	8.7	7.5	10.7	9.0

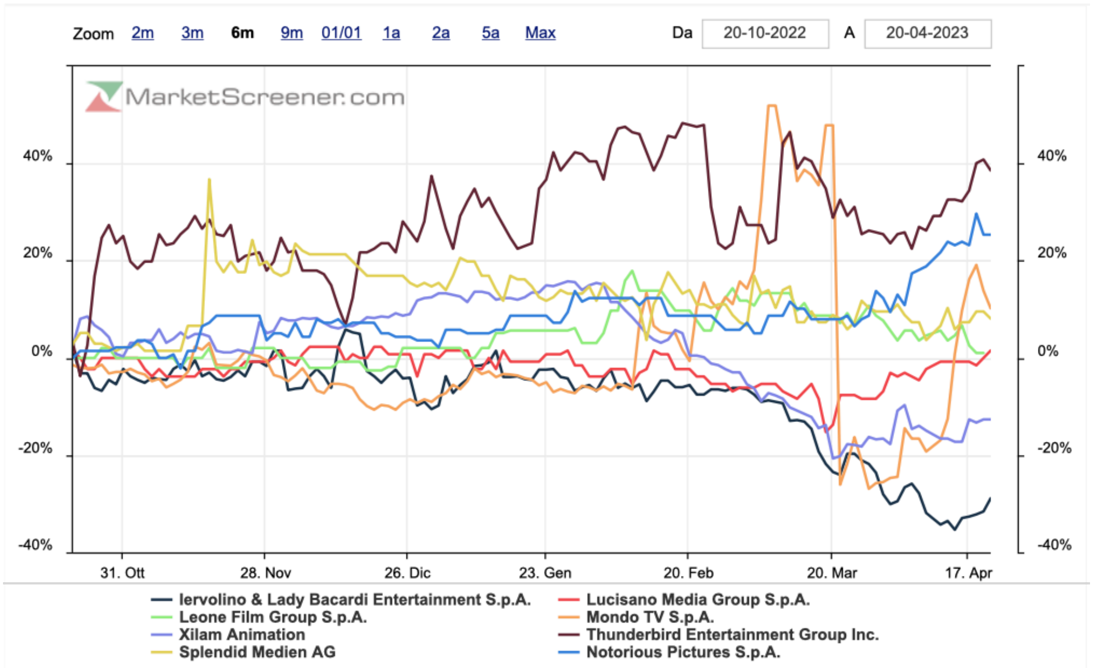
Source: Value Track Analysis

Peers Multiple Analysis

The stocks included in the peers' group have all performed well since our last update - and following a relatively weak performance over January-November 2022 - and have materially outperformed ILBE over the past six months.

The group of peers is broadly the same we used in the past, but we have taken out Mondo TV, due to the dramatic change in its client portfolio and strategy (and pending the release of a new Industrial Plan) and replaced with Splendid Mediem (Germany).

Comparables Stock Performance (last 6 months)



Source: Market Screener

Hence, not surprisingly ILBE trades at even deeper discount to domestic and international peers: still focusing on **EV/EBIT and P/E** (for 2023E and 2024E), the table below summarises the current ratings of the selected peers.

ILBE: Peers' stock trading multiples

Company	EV / EBIT (x)		P / E (x)	
	2023E	2024E	2023E	2024E
Notorious Pictures SpA	8.4	5.8	6.0	4.2
Leone Film Group SpA	11.4	9.4	7.3	5.6
Lucisano Media Group	10.0	7.8	8.2	5.0
Xilam Animation	11.5	8.9	14.4	11.8
Thunderbird Entertainment Group	11.9	8.2	nm	nm
Splendid Medien AG	4.4	4.2	8.6	7.7
Average	**9.6**	**7.4**	**8.9**	**6.9**
Median	**10.7**	**8.0**	**8.2**	**5.6**
ILBE	**3.5**	**2.9**	**2.7**	**2.3**

Source: Value Track Analysis

On the back of the above considerations we use the group's median value to set the fair EV/EBIT and P/E multiples for ILBE, as reported below, and get to a **fair equity value per share of €3.4, broadly in line with our last update.** ILBE's fair ratings fall in between those of the Italian players – much smaller, more exposed to the distribution and box-office business and hence more volatile - and those of the pure content producers, as Xilam and Thunderbird, whose premium ratings are supported by either higher growth and/or FCF prospects and/or size.

ILBE: Peers' stock trading multiples

	EV / EBIT (x)		P / E (x)	
	2023E	2024E	2023E	2024E
Total Peers' Average	9.6	7.4	8.9	6.9
Total Peers' Median	10.7	8.0	8.2	5.6
Fair Multiple ILBE (x)	**10.7**	**8.0**	**8.2**	**5.6**
Fair Equity ILBE (€mn)	162.5	136.7	96.3	79.4
Fair Value ILBE (€ p/sh.)	4.6	3.9	2.7	2.3
Average (€ p/sh.)		**3.37**		

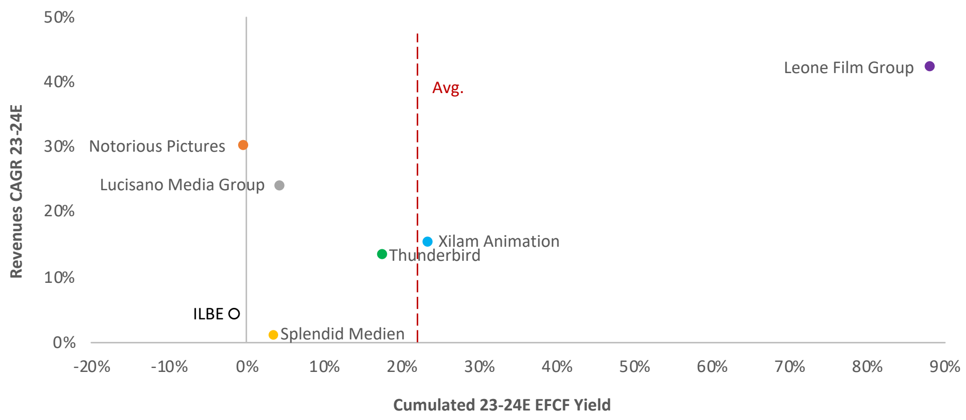
Source: Value Track Analysis

EFCF yield Analysis

While in the past we used the EFCF yield analysis only as a cross-check, we now introduce this as a valuation methodology, as we understand the decreasing return of the business has become a key issue and value driver, we believe, and as peers' positioning is less scattered around. Also, in a moment were the value of content library has become more uncertain and earnings become more volatile, it makes sense to move focus to cash flow.

The chart below shows the peers considered on the back of their cumulated EFCF yield over 2023-24E (2 years) and their expected top line growth over 2023-24E (2-yrs CAGR). The map confirms ILBE's weak positioning among comparables, which are expected to deliver on average stronger free cash flow generation and/or stronger top line growth. Peers offer on average an EFCF yield of ca.11.3% over the next two years, which is 300/400bp higher than in the past, consistently with higher interest rates and increased equity risk premium.

ILBE: EFCF Yield vs Revenue Growth



Source: Value Track Analysis, (*) LFG out of scale

This exercise has the limit of being focused over a very limited period of time, where a content provider may also face temporary effects from particularly light or demanding slate, however, it has the benefit of

- considering the actual return of the business, notwithstanding the accounting and capitalization policies;
- capturing the momentum of the industry in a phase of decreased visibility.

The model gives a current **fair equity value per share of €1.47.**

ILBE: Fair Value based on normalized EFCF yield

€mn	
Normalized ILBE EFCF (2025E)	7.2
Fair EFCF Yield (2023-24E of peers)	11.3%
ILBE target Equity (based on Medium Term potential, 2025E)	63.5
Target Equity Per Share (Medium Term, 2025E)	€1.80
Current Value (2023 NPV @ WACC)	**€1.47**

Source: Value Track Analysis

DCF model

Our DCF model provides a **fair equity value per share of €1.87** and is built on the back of the following assumptions:

- time horizon for explicit forecasts is 2023-28E;
- valuation date is December 2022 and net debt refers to FY2022;
- WACC is equal to 10.6% (see table below for its components);
- terminal value is based on PGR of 0% and implies an exit EV/EBIT of 7.8x (at slight premium to current peers' rating).

ILBE: WACC calculation

Risk free	2%
Risk Premium	8.1%
Credit spread	3%
Beta Levered	0.97
Small Cap Mkt Risk Premium	2.0%
Cost of Equity	11.8%
Cost of Debt a.t.	3.8%
D/D+E	15%
WACC	**10.6%**

Source: Value Track Analysis

ILBE: DCF valuation

	€mn
PV of future cash flows (2023-2028E)	23.2
PV of Terminal value	69.1
Fair Enterprise value	**92.3**
Fair Equity value	**66.1**
Shares (mn)	35.3
Fair Equity Value p.s. (€)	**1.87**

Source: Value Track Analysis

By averaging the fair value per share coming from the peer's analysis (€3.37 p/s), the DCF analysis (€1.87 p/s) and the EFCF Analysis (€1.47 p/s) we come up with a **fair value per share of €2.25.**

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