

DREAMWORKS ANIMATION

STOCK VALUATION

Siede Coleman, David Ferialdi, Chris Ramirez, Chinvee Lim, Isaac Rosales

WHY DREAMWORKS REPORT NET LOSS?

- Movie industry is volatile.
- There is no prediction of a film's success.
- A majority of a film's revenue comes from weekend box office releases. Competitive environment or low turnout can greatly make a negative difference in gross revenue.
- Piracy is common overseas and in United States.
- Family film successes are dependent on franchises well known stories will attract larger audiences than original stories if marketed incorrectly.
- DreamWorks subsidizes meals for their employees at the Studio, which Katzenberg refuses to decrease even in times of shrinking budgets

WHY PRODUCT COST DECLINE?

- Their earnings report states that DreamWorks will adopt a new technology that will reduce their costs by \$ 120 million per movie.
- In partnering with Twentieth Century Fox distribution, DreamWorks has also limited it's release slate to 3 films per year, whereas the company aimed for 4 films in 2013 and 2014 before the partnership.

STOCK VALUATION WORKSHEET


1. MorningStar Stock Analysts

- Sales growth rate from MorningStar, we believe this worksheet is more pragmatic.

2. Bloomberg

- Sales growth rate from Bloomberg terminal.
- Although the share price is higher, it is not consistent with stock analysts prediction.
- Sales growth rate is too fluctuate.

FUTURE FORECAST OF CASH FLOWS

- \$17.40 based on the future forecast of cash flow.
- Sales growth to average 1% annually for the next five years.
- Cost of sales as 80%, product cost will decrease.
- Produce more movies every year.
- Release at least one sequels film every year (less risky, increase profit through home video sales, merchandising, and licensing) 
- Average operating profit margin increase to 20% for the next 5 years because of increase in film release.
- Cash conversion cycle should be decrease as the days of inventory is very high, if cash conversion cycle decreases, stock price will increase.

FUTURE CASH FLOWS ANALYSIS

- Fair value estimates is \$17 per share, as they think that the company's revenue will be more stable than in the past.
- Revenue growth to average 1% annually for the next 5 years.
- Sales ↑ 4% in 2013.
- Average operating profit margin decrease to 15% for the next five years because of the decline in the home video market drag on profitability.

Upside case

- \$26 per share fair value
- 7% average annual growth
- 21% average operating margins

Downside case

- \$14 per share fair value
- 2% average annual sales decrease
- 14% average operating margins

DWA SHARE PRICE CONSISTENT WITH STOCK ANALYSTS PREDICTION

- DWA's share price is consistent with Stock analysts prediction
- The uncertain transition from DVDs to digital distribution drag on profitability. Number of DVDs sales ↓
- The film's library of content and franchises could make it an attractive takeover target.
- Reshaped the business by creating more films per year.
- Release at least one sequel film every year. For example, 2 films in 2013, 3 films in 2014, 4 films in 2015 and 3 films in 2016.

DWA SHARE PRICE CONSISTENT WITH STOCK ANALYSTS PREDICTION

- Partnership with a Russian Theme Park maker to license their characters for a theme park. DWA doesn't have expense, only revenue.
- Inventory decrease, carrying the cost of The Croods and Turbo.
- Popularity of cheap rental options from Netflix and Redbox. However, partnership with Netflix is to release an animated show based on Turbo exclusively for Netflix.
- The computer generated animation technologies lower the entry barriers.

HOW TO MAXIMIZE DWA'S SHARE PRICE?

- Increase total revenue, to not have high dependency on DVD sales and penetrate the digital media market. For instance, DreamWorks acquired YouTube channel Awesomeness TV on May 1st, 2013 that successfully enter to next generation media platform. DreamWorks has further entered this platform with its partnership with Netflix to create original content based on "Turbo", an emerging DreamWorks franchise.
- DreamWorks can outsource portions of their production to decrease the time to produce an animated film.
- Outsourcing production to other countries can also provide a cheaper alternative to productions costs.

HOW TO MAXIMIZE DWA'S SHARE PRICE?

- Increase company debt financing. DreamWorks Animation is highly funding the company by using Equity financing; however, DreamWorks definitely should balance their cost of capital by increasing their debt financing to decrease Weighted Average Cost of Capital (WACC).
- Decrease the cash conversion cycle days by decreasing the inventory. After DreamWorks launches a new film, it takes around three years to write off the inventories. Thus, finding a way for DreamWorks to return the cash faster than three years.