

Lucisano Media Group

A 60-Year Journey in the Italian Film Industry

Lucisano Media Group - Key estimates and data					
Y/E December		2017A	2018E	2019E	2020E
Revenues	EUR M	38.39	38.87	46.85	50.92
EBITDA	EUR M	14.17	14.78	18.32	19.75
EBIT	EUR M	5.77	4.63	6.82	6.75
Net Income	EUR M	3.80	2.97	4.75	4.74
Dividend ord.	EUR	0.05	0.05	0.05	0.05
Adj. EPS	EUR	0.26	0.20	0.32	0.32
EV/EBITDA	x	4.7	3.7	2.9	2.6
Adj. P/E	x	9.2	9.1	5.7	5.7

A: actual; E: estimates; Source: Company data and Intesa Sanpaolo Research

- A leading fully vertically integrated player.** Founded in 1958 by Fulvio Lucisano, Lucisano Media Group is the oldest integrated Italian player active in the production, acquisition, distribution of film and TV products, and in the management of multiplexes. Over its history, Lucisano Media Group has produced over 150 films, has distributed approximately 500 foreign movies and can count on over 325 Italian and International films in its library to date. The group has also become the third-largest operator in the Italian multiplex circuit with 57 screens directly managed. In FY17A, revenues increased by 0.7% to EUR 38.4M, with revenues from services (production, distribution and multiplexes) down by 4.6% to EUR 28.1M and other revenues (grants and tax credit) up by 19% to EUR 10.2M. EBITDA was EUR 14.2M (-5.4% yoy), with a margin contraction of 240bps to 36.9%. Net income amounted to EUR 3.8M, -3.4% yoy.
- Positives.** We believe that Lucisano Media Group can leverage on some company-specific positives, including: i) a consistent line-up in terms of production and distribution; ii) a unique business model, in which activities are divided between film and television production, distribution of cinematographic works, and the management of multiplexes, thus implying a direct control over the entire value chain; iii) long-term relationships with young talented artists, thanks to the establishment of the IIF Factory; and iv) a capillary presence in the multiplex market in southern Italy, with future expansion plans in terms of number of cinemas owned and managed.
- Estimates and valuation.** We projected a broadly stable trend for multiplexes, while revenues from production and distribution should benefit from 4-5 movie releases per year, and an important TV series in FY19-20. We see the EBITDA margin in FY18E-20E ranging between 38% and 39%, slightly lower than the average of the last five years (around 40% in FY13A-17A). We expect a 2017A-20E EPS CAGR of around 8%. We valued Lucisano Media Group with a DCF model, which points to **a EUR 3.3/sh target price and we initiate coverage of the company with a BUY rating**. Lucisano trades at a 9-18% discount on EV/EBITDA in FY18E and FY19E, respectively, and a significant discount on FY19E P/E (38.5%).
- Key risks.** In our view, the key risks are: 1) film production is subject to many uncertainties that include possible delays/interruptions to the completion of the project for events of force majeure, which would result in an increase in the forecasted costs; 2) the strong seasonality of the Italian film market, with a concentration of film releases in a few months of the year; 3) credit risk due to a temporal difference between revenue and costs. The lack of a production's success could therefore compromise the company's overall profitability due to a misalignment of revenues and margins compared to the budget; and 4) increasing competitive pressure from online platforms on the multiplex side, which could cause a downsizing of the traditional cinematographic market.

See page 33 for full disclosures and analyst certification
Banca IMI is Specialist to Lucisano Media Group

21 September 2018: 8:16 CET
Date and time of production

BUY

Target Price: EUR 3.3

Italy/Media
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Price performance, -1Y

19/09/2018



Source: FactSet

Date and time of first circulation:
21 September 2018: 8:15 CET

Priced at market close on 19/09/2018*	
Target price (€)	3.3
Target upside (%)	81.80
Market price (€)	1.82
52Wk range (€)	2.98/1.79
Market cap (€ M)	27.00
No. of shares	14.88
Free float (%)	11.9
Major shr	Keimos
(%)	68.0
Reuters	LMG.MI
Bloomberg	LMG IM
FTSE IT All Sh	23576
Performance %	
Absolute	Rel. to FTSE IT All
-1M	-1.6 -1M
-3M	-12.7 -3M
-12M	-29.9 -12M
	-5.6
	-10.0
	-26.5

*unless otherwise indicated within report. Source: FactSet and Intesa Sanpaolo Research estimates

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Sebastiano Grisetti contributed to this report

Positives and Negatives

Positives

- **A fully vertically-integrated group:** the group has a unique business model, in which activities are divided between film and television production, distribution of cinematographic works, and the management of multiplexes, thus it has a direct control over the entire value chain. This model allows Lucisano Media Group (LMG or Lucisano) to reduce the risk characteristic of single platform companies, exploit the synergies between the various business units and thanks to technical and managerial know-how developed over time, combine an industrial approach with the creative needs typical of the sector. Moreover, thanks to the unified and centralised management of financial resources, the group is committed to balancing the flows of the collections from film production contracts and those deriving from the management of multiplexes (in part owned, in part rented), lightening the credit risk;
- **Leading independent Italian player in the multiplex market:** in the multiplex industry, according to management, the company ranks as the first independent player in southern Italy and the third-largest operator at a national level, with future expansion plans in terms of number of cinemas owned and managed. Looking at the number of viewers, the group's multiplexes are placed just behind big international players, such as UCI and The Space, positioning as the first independent Italian player in the market, with over 2M viewers per year. In this regard, in 2017 ANEC assigned the Golden Ticket award to the Andromeda multiplex in Brindisi, for scoring the highest number of spectators in the categories of multiplexes with 5 to 7 screens and in Italian municipalities with up to 200k inhabitants. The group is also committed to ongoing technological progress within its cinemas, and in particular we highlight the HAPPY auditorium equipped with IMAX technology and the Andromeda auditorium of Rome selected by DOLBY for the installation of the innovative DOLBY ATHMOS system;
- **Consistent line-up in terms of production and distribution:** in the next three years, the group is planning the release of important productions, both for cinema and television, including the high-budgeted series "Les Italiens" in co-production with Nicolas Winding Refn, acclaimed director of the film "Drive". These productions sustained considerable costs in 2016 and 2017, which are expected to be offset by increased revenues in the coming years when these films are released. Also on the distribution side, thanks to the agreements signed at the end of 2017 with M2 Pictures and Vision Distribution, numerous films have been purchased aiming to receive positive feedback at the box office once released, such as "Escape Plan 2" and "Georgetown", presented at the Cannes and Berlin festivals. Thanks to these acquisitions, the already extensive Library, which in 2017 comprised 324 films, is expanding, allowing the group to offer more titles to broadcasters;
- **"IIF Factory":** thanks to the creation of the "IIF Factory", the group has combined a group of young directors, actors and screenwriters led by Massimiliano Bruno, who produce high quality products with good commercial potential, like "Nessuno mi può giudicare", "Prima che la notte", and "Noi e la Giulia", which were awarded David di Donatello awards for the movie and actors. Due to the long-term contracts, the artists can forge strong bonds between themselves and with the group, to ensure greater stability in production times. With the entry into the shareholding structure of Alevi S.r.l., the group is also extending its focus to alternative content, such as documentaries and docufiction;
- **The new legislative framework for tax credit,** in force since 1 January 2017, will be fully implemented in the coming years as 2017 was still a transitional year. It provides tax incentives in the form of tax credits, automatic contributions, facilities for the film and audio-visual promotion, and a Plan for the upgrading of the halls¹. The benefits and contributions from the government are considerable and affect the entire value chain, from production to the management of multiplexes; thus, these incentives could underpin solid improvements in productivity and profitability.

¹ See Appendix for further explanations

Negatives

- **Credit risk:** between the drafting of the subject (i.e. the idea behind the film) and the theatrical release of the movie, the average time that elapses is about a year or two, during which costs are very high. Hence the temporal coordination is a crucial factor. While the first cash outflows already take place during the design phase, the generation of revenue commences well after the end of the production process. This credit risk concerns only the production and distribution activity, as in the case of multiplexes, almost all collections are immediate. The lack of success of one or more films produced or distributed by IIF could determine a misalignment of revenues and margins compared to the budget that can affect the group's overall profitability;
- **Online piracy:** online piracy continues to be a factor influencing the revenues of the film industry and in 2017 it has proved to still be a factor negatively affecting the group's performance. On this front, however, we highlight how the general decrease in Pay-Tv costs and the growth of low-cost legal platforms has allowed a slight reduction in the impact from piracy, with management expecting further improvements in the coming years;
- **Film production is subject to many uncertainties that include possible delays/interruptions** to the completion of the project due to events of force majeure including: creative differences between members of the cast and personnel, illness, disability or death of the main cast, technical complications with special effects or other aspects of production, lack of necessary equipment, damage to the recording equipment, as well as adverse weather conditions. Delays and interruptions can result in an increase in the forecasted costs;
- **Seasonality:** unlike other markets, such as the US, the Italian film market is characterised by strong seasonality with a concentration of film releases in a few months of the year. The postponement of a film release to a less 'favourable' moment of the year could jeopardise the collection at cinemas and, consequently, the overall commercial exploitation of the film by the group;
- **Increasing competitive pressure from online platforms:** On the multiplex side, the turnout of the public in the halls has been declining in recent years, and the classic dynamic of the film being distributed first in cinemas and then successively via other channels could undergo a fundamental change, with the release of movies simultaneously at cinemas and on streaming platforms, causing a downsizing of the traditional cinematographic market.

Valuation

We valued Lucisano Media Group with a DCF model and we cross-checked our result with a multiples comparison.

DCF model

DCF valuation

We ran a DCF model based on our estimates and on the following key assumptions:

- A 5.6% WACC, incorporating a 3.0% risk-free rate, an equity risk premium of 5.75% and a gearing of 49.2%;
- A 0% terminal value growth;
- LT EBIT is calculated starting from 2020E data.

Lucisano Media Group - WACC calculation	
%	
Gross debt rate	3.0
Tax rate	24
Net debt rate	2.3
Beta* levered (x)	1.00
Gearing	49.2
Beta* relevered (x)	1.00
Risk-free rate	3.00
Equity risk premium	5.75
WACC	5.6

Source: *FactSet, Intesa Sanpaolo Research estimates

Our model returns a target price at EUR 3.3/share. We initiate coverage on Lucisano Media Group with a BUY rating, given the around 80% upside at current price levels.

BUY; EUR 3.3/sh target price

Lucisano Media Group - DCF calculation (2018E-20E)				
EUR M	2018E	2019E	2020E	LT
EBIT	4.6	6.8	6.8	5.5
Tax	-0.8	-1.3	-1.3	-1.0
Depreciation	10.2	11.5	13.0	
NOPAT	14.0	17.0	18.5	4.5
WC	1.1	-3.2	-1.7	
Capex	-9.7	-11.7	-12.7	
FCF	5.4	2.1	4.0	4.5
Discounted FCF	5.4	2.0	3.6	3.8
WACC (%)	5.6			
TV growth (%)	0.0			
Sum	11			
TV	68			
EV	79			
Debt 2017A	30.9			
Equity	48			
Shares	14.9			
Target price (EUR/share)	3.3			

E: estimates; Source: Intesa Sanpaolo Research estimates

Multiples cross-check

We double-checked our DCF valuation with a peers' multiples comparison (Leone Film, Mondo TV, Notorious Pictures). We highlight that we consider the peers sample as not particularly meaningful, given the companies' different business models.

Multiples

Lucisano trades at a 9-18% discount on EV/EBITDA in FY18E and FY19E, respectively, and at a significant discount on FY19E P/E (38.5%).

Lucisano Media Group - Peers' EV/EBITDA and P/E						
x	Price	Mkt Cap	EV/EBITDA		P/E	
	(EUR/sh)	(EUR M)	FY18E	FY19E	FY18E	FY19E
Leone Film	4.8	68	3.7	3.3	10.5	8.9
Mondo TV	3.9	134	3.5	2.9	10.3	8.7
Notorious Pictures	2.8	64	5.0	4.5	10.6	10.1
Average			4.0	3.6	10.5	9.2
Lucisano	1.8	27	3.7	2.9	9.1	5.7
Discount vs. average %			-9.2	-17.9	-13.3	-38.5

Priced at market close on 19/09/2018; Source: FactSet and Intesa Sanpaolo Research estimates

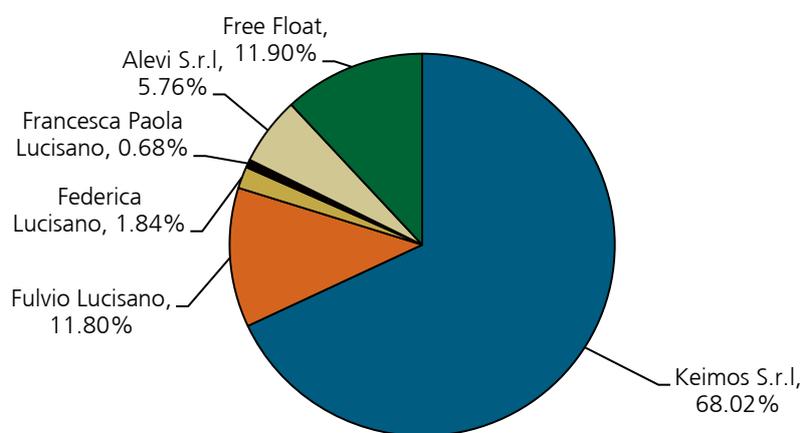
Shareholders' Structure

Lucisano Media Group shareholders' capital comprises 14.9M shares. The main shareholders are:

Main shareholders

- Keimos S.r.l: 68.02%
- Lucisano Fulvio: 11.80%
- Lucisano Federica: 1.84%
- Lucisano Paola Francesca: 0.68%
- Alevi S.r.l: 5.76%
- Free float: 11.90%

Lucisano Media Group - Shareholders' structure



Source: Company data

The free float comprises 1.77M shares, corresponding to 11.9% of the capital. Keimos S.r.l is the Lucisano family's holding company, which therefore controls the company both directly and indirectly. Fulvio Lucisano is the chairman, while his daughter Federica Lucisano is the CEO.

In July 2014, Lucisano Media Group was listed on the AIM segment of the Milan Stock Exchange, with the intention to expand its activities and gain visibility on the market. The company's current market cap is EUR 27M.

**Listed on the AIM segment
of the Milan Stock
Exchange**

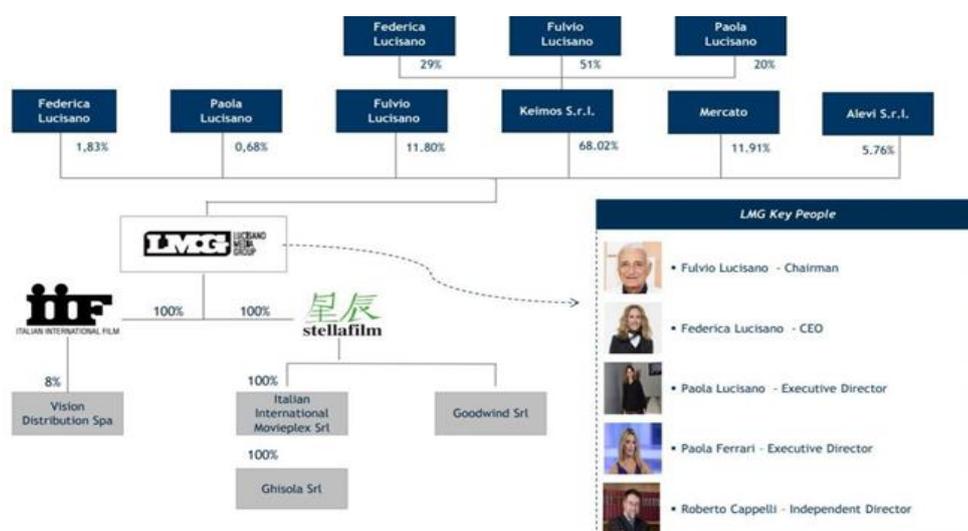
Group Profile

Lucisano Media Group is an Italian film production and distribution company, which is also active in the management of multiplexes. Through its sixty-year old subsidiary IIF, it is the oldest and most important player on the Italian market in the distribution and production of cinematographic and television works.

LMG: key player on Italian market in the distribution and production of cinema and TV works

Although the holding company (Lucisano Media Group S.p.A) performs the main functions as to strategic development of activities and management of financial services, 7 companies form the group structure, the most important of which are Italian International Film S.r.l (IIF) and Stella Film S.r.l. The former is active in film production and distribution, while the latter operates in the management of multiplexes.

Lucisano Media Group - Group structure



Source: Company data

Over its 60-year history in the movie industry, the group has produced more than 150 films, distributed approximately 500 foreign movies, and has a library of over 300 Italian and International films. The group is also active in the multiplex segment, and over the years has become the third-largest operator in the Italian multiplex circuit (first Italian independent player). According to management, the group's main success factors in the reference market are recognised as being the following:

Group key success factors

- **Technical and management know-how**, being in a position to supervise every aspect of the development and realisation of cinematographic works;
- **A successful track record**, represented by sixty years of experience in the sector during which it produced and distributed about 600 titles, including 2 Oscar winning and 12 Oscar nominated films;
- Ability to maintain a **stable market share**;
- Development of the **IIF Factory**, a group of talent coordinated by the director Massimiliano Bruno who, through the signing of exclusive and non-exclusive contracts, aims to establish and strengthen bonds with young directors, actors, writers and screenwriters, and create high-quality products with strong commercial potential;
- **High-quality Library**;
- **Unique business model**, characterised by a vertical integration of the value chain, from production to the distribution of the film product, diversifying the distribution models and dividing the risk through the management of multiplexes.

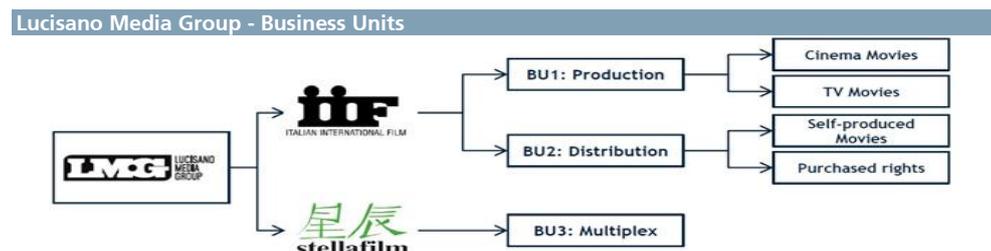
Business Model

The group's business model is structured into three Business Units:

- Movie and television production;
- Distribution of self-produced movies and purchased products;
- Management of multiplexes.

Three Business Units

Lucisano Media Group is the only vertically-integrated Italian player in the market and therefore active from the production (for Cinema and TV) to the distribution and full exploitation of the products. The various activities carried out by the Business Units are analysed in detail below.



Source: Company data

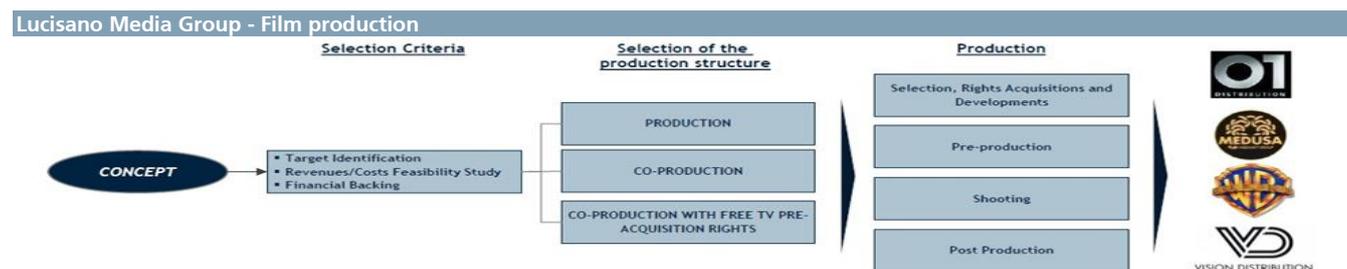
Production

Movie production

The process begins with the ideation and selection of the concept, following a market analysis of potential targets for the movie. Before starting production, however, two important decisions are taken: the first concerning the type of production (independent production or co-production), and the second concerning the financing resources needed to ensure the coverage of the budgeted costs. The latter can be implemented through pre-sale agreements, contracts with a minimum agreed revenue (the so-called "Minimum guarantee agreements"), underwriting of co-production agreements, as well as the exploitation of tax benefits (Tax Credit). Schematically, film production is divided into four phases:

- **Initial phase:** once the concept is determined, the writer will be hired to draft the screenplay or, if it has already been drafted, the screenplay will be purchased from the same screenwriter or from other writers;
- **Pre-production:** collection, from third parties, of the financial resources needed to cover the estimated costs of the production (filming does not begin until the budget is covered);
- **Filming:** IIF oversees every moment of production, as it is the most important phase of the entire production process;
- **Post-production:** is the final phase of the production process, in which the editing, the soundtrack, the dialogues, the synchronisation and the mixing are carried out, up to the final movie editing.

Upon completion of this process the promotion and launch period of the film commences, which are crucial for the success of the product.

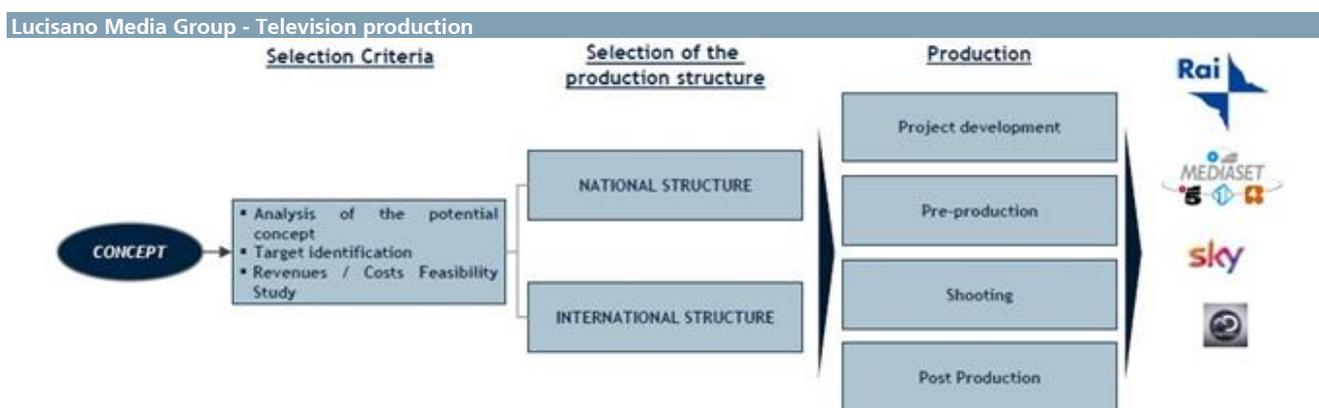


Source: Company data

Television production

TV production has a different business model, which operates through specific agreements with interested broadcasters, who actively collaborate in the selection and development of the concept. The works are therefore co-produced, but IIF generally retains a share up to 50% of the distribution rights in some channels, as well as being entitled to a producer's fee. The production differs according to the market for which the product is destined. Products destined to the local market are first presented to the TV broadcaster based on its editorial line and then produced under a co-production agreement with it. The cast is selected together with the broadcaster and the formats used are those of the Miniseries, TV Movies, Series, or Sit-com. On the other hand, the productions for the international markets are in English and in co-production with international partners, with a pre-purchase agreement with the Italian broadcaster. The most frequently used format is the TV Movie.

IIF's main partners in this segment are Rai and Mediaset: while the former has a more cinematographic approach, the latter is more focused on TV-specific comedies. This set-up allows the company to maintain a balanced production and greater choice.



Source: Company data

Acquisition of rights and distribution

Acquisition of distribution rights

This activity consists in assuring IIF the distribution licence for a given territory of cinematographic works. In this case, the concept selection and film production are carried out by third parties. Thanks to the company's strong relationships with major international studios and producers, it usually manages to receive the screenplays and the projects before official markets and festivals. The types of acquisition contract that are generally used by IIF are:

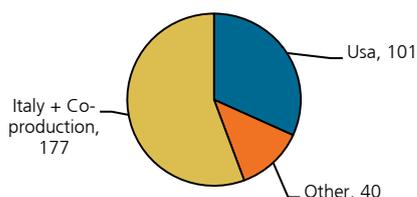
- "Minimum Guarantee Agreements", in which IIF pays the seller a minimum guaranteed amount against the proceeds that will be earned from the movie, and advances the expenses related to the distribution activities (prints and advertising, "P&A costs"). The company is entitled to a share of the proceeds as its fee for the distribution activities (the "distribution fee") and to retain the remaining portion of the proceeds until it has fully recovered its investment in minimum guarantee and P&A;
- Fixed-price licence contract, where IIF acquires the exploitation rights and all the proceeds deriving from the movie against the payment of a flat fee, also taking charge of all expenses.

The average length of the exploitation licence of the cinematographic work ranges between 20 and 25 years.

The Library

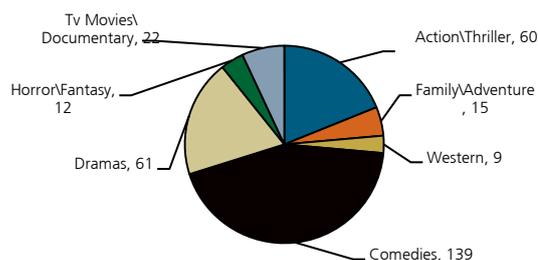
Thanks to its over sixty-year presence in the sector, IIF has one of the most valuable libraries in Italy. Its mixed composition allows IIF to adequately respond to the demands of the television and Home Entertainment market.

Lucisano Media Group - Breakdown by Nationality



Source: Company data

Lucisano Media Group - Breakdown by Genre



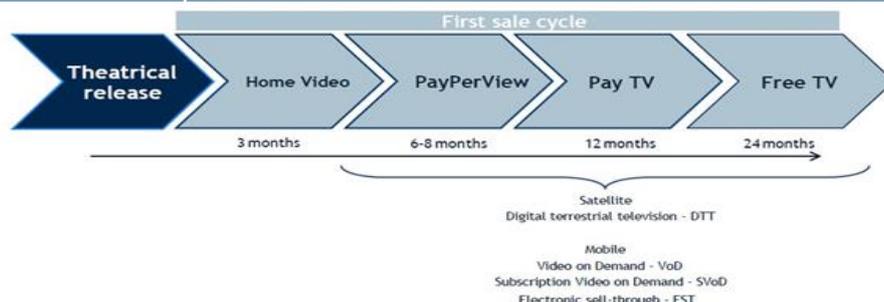
Source: Company data

Distribution

The company commercialises movies that it has produced directly and movies for which it has purchased the distribution rights. For the former, there is the possibility of exploiting other intellectual property rights, and this exploitation can be extended worldwide. The distribution activities are crucial and consist of both the printing of copies of the movies to be distributed in cinemas, and an intense marketing activity that is carried out through paid advertising on all media (TV, newspapers and magazines, internet, social media) and publicity (press screening and conferences, TV, radio and online interviews etc.). The different distribution channels through which the commercial exploitation of the film takes place are:

- **Theatrical channel:** this is the projection in cinemas, and represents the first phase of the film distribution process. In this phase the dubbing, printing of copies and advertising launch are discussed and it is the most important moment in the commercialisation of the product as the subsequent exploitation of the work will depend on the revenues obtained from the cinemas. To minimise the risks, IIF entrusts this stage to external partners such as O1 Distribution, Warner, Vision Distribution and Medusa Film. These agreements provide a commission to the distributor, the anticipation of launch costs by the distributor, a duration of 36 months and the right of approval by IIF on the methods used for distribution;
- **Home video channel:** this phase is entrusted to third parties, both in terms of rental and sale. In this case, IIF provides for authoring and duplication of the items requested by the distributor. Regarding the "newsstand" channel, the company operates through direct sales to publishing groups or through distribution mandates for film packages entrusted to third parties for long periods;
- **Television channel:** the sale of Pay TV and Free TV distribution rights is made through the sale of a library movie package. In this channel, the main commercial partners of the company are Rai, Mediaset, Sky Italia, Universal, Discovery and Viacom channels. DTT has greatly expanded the opportunity for exploitation of the Library films in recent years;
- **New channels:** the importance of distribution through IPTV, Mobile, VoD, SVoD is increasing annually. Players such as Netflix, TIM Vision, Infinity and Itunes, are becoming important partners for the group.

Lucisano Media Group - Distribution channel



Source: Company data

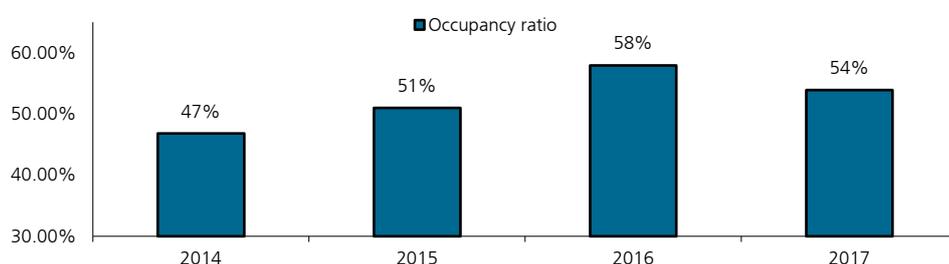
Management of Multiplexes

Through the subsidiary Stella S.r.l the group manages some multiplexes in Central and Southern Italy. The related activities consist of choosing the movies to be projected, the management and optimisation of the programming in the cinemas, the projection of movies and ancillary activities. The analysis of the type of movies and the identification of the target consumers are two important preliminary activities. The key factors for an optimal management of multiplexes is the steady presence of brand-new releases in the programming and the optimisation of the rotation of the movies in the multiplex rooms to ensure an adequate occupancy ratio.

Through the subsidiary Stella S.r.l the group manages some multiplexes

Another important feature in the management of a multiplex is the ability to purchase the film on consignment and with percentage modes allowing it not to have inventories in stock, risks related to the deterioration and theft of the goods, no financial exposure for the purchase of products, and variable costs based on collection.

Lucisano occupancy ratio (%)



Source: Intesa Sanpaolo Research elaboration on Company data

The group currently manages 57 screens (9,773 seats) and programmes in another 68 proprietary screens in southern Italy, and is the third-largest operator on the Italian market, with an occupancy rate that has increased in the last years (from 47% in 2014 to 58% in 2016, with a slight decrease in 2017 to 54%²). The characteristics of the multiplexes managed by Stella Film are the offer of high-quality services (in terms of reception, programming and technology), the high brand recognition, and the constant organisation of events and meetings with the protagonists of the evenings. Two examples of the group's efforts in technology development are the implementation of IMAX technology in the HAPPY auditorium (exclusive to Central-Southern Italy) and the installation of a DOLBY ATMOS audio system at the Andromeda in Rome.

Top 5 cinema player in Italy (FY17)

Rank	Company	Visitors (M)	Screens	Theatres
1	UCI	18.73	491	47
2	The Space Cinema	12.96	293	30
3	Stella Film	1.88	57	7
4	Ferrero Cinemas	1.65	47	10
5	Giometti Cinema	1.38	40	4

Source: Company data

² The ratio is computed dividing the annual attendance by 360 days and then by the number of seats managed by the group. We highlight that in the multiplex business, attendances are highly concentrated on weekends and holidays, and therefore the occupancy ratio reaches a high percentage (almost 90%) in these days despite other working days, where the ratio falls below 30%.

Strategy

The group's strategy aims to reduce the overall corporate risk and strengthen its competitive position in the various sectors in which it operates. Future strategies that the group will implement concern:

Strategy: to reduce the overall corporate risk and strengthen its competitive position in the various sectors

- **Strengthening its competitive position:** through the subsidiary IIF, the aim is to offer a more extensive and diversified product. To this mission, a Factory was created in which writers, directors and actors collaborate to create a synergy between themselves and between cinema and television productions. The goal is to intensify the number of agreements with directors, screenwriters and actors to increase productivity by investing in talented young people and in established authors and actors. It is thanks to the stipulation of multi-year contracts with the interested parties that the group can plan steady growth for the next few years;
- **Multiplex management activities** will expand on various fronts. Firstly, expansion works to the Brindisi and Benevento Multiplexes will be launched and feasibility studies were carried out to evaluate the acquisition of the management of other multiplexes, without requiring real estate investments. Secondly, the group intends to further pursue the process of technological innovation that will allow short-term personnel savings and an expansion in the range and number of projections. In this perspective, the number of halls with advanced technology and satellite connection are expected to grow, allowing the transmission of live events, already present in some cinemas, that could become an important source of revenues;
- **Increasing the number of cinematographic productions and international co-productions**, destined for the European and international markets. The entry of Alevi S.r.l (which purchased 5.76% of the share capital) into the shareholding structure was allowed so that the group could produce alternative and supplementary content to the core business, such as documentaries and docufiction, in order to diversify the production activity. The group also aims to increase the acquisition of foreign film rights, with new investments and new distribution partnership agreements, such as the arrangement reached at the end of 2017 with M2 Pictures and Vision Distribution;
- Trying to **exploit the benefits arising from the growing importance of streaming platforms**, such as Netflix and Amazon, which are substantially changing the entire cinematographic market. On the one hand, this transformation could radically change the theatrical market, which must adopt increasingly innovative and customised solutions to attract an audience that increasingly prefers the use of these platforms. On the other hand, however, the greater demand for such platforms, will oblige these providers to offer a broader range of cinematographic products, in order to stand out from competitors and attract the public: in this perspective, the group will try to finalise distribution and co-production agreements with these platforms to ensure the success of the works produced and distributed.

The Reference Market

When analysing the market in which the group operates, it is important to recall how Lucisano Media Group is the only vertically-integrated company in the Italian cinematographic market, from production to distribution. The main sectors in which the group operates are therefore film and television production and distribution and the multiplex market. In general, the main success drivers in the Film business are:

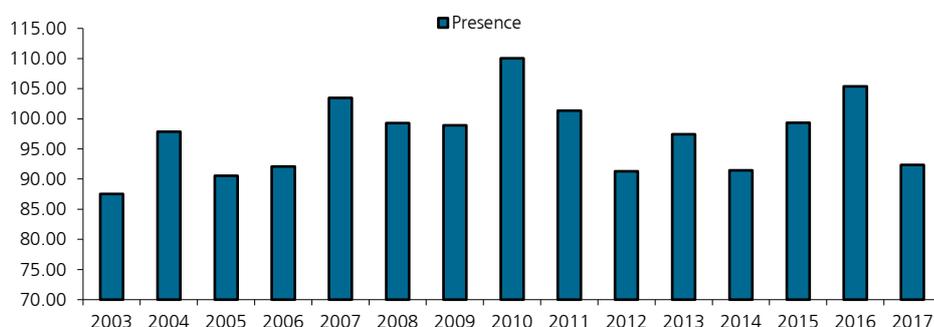
- Downstream revenues sharing generated by successful content: in order to ensure steady growth, it is important for a company to generate the maximum possible level of revenues from successful projects;
- Achieving diversified revenue streams: thereby creating a network of diversified activities across the Film business value chain, generating multiple sources of income;
- Ongoing relationships with successful talent: to succeed, the product needs to have the best available resources, and in the case of cinematographic works these are the actors, directors, and writers. The better the relationships, the greater the number of movies that could be produced together;
- International and corporate business relationships: especially in the field of distribution, it is important that the company has internationally recognised partners with large market shares;
- A supportive and consistent government policy.

Theatrical Market

2017 was a negative year for Italian cinema. Among the main factors that influenced this performance was the acceleration of the trend of the migration of consumer preferences towards alternative platforms (Netflix, Amazon Prime), the wide impact of online piracy, the transition period to Law n.220 (also called "Franceschini Law"), which affected planning and seasonality.

Theatrical Market

Presence in Italian cinemas since 2003 (M of visitors)



Source: Intesa Sanpaolo Research elaboration on ANICA data

Year-over-year change in admission and presence

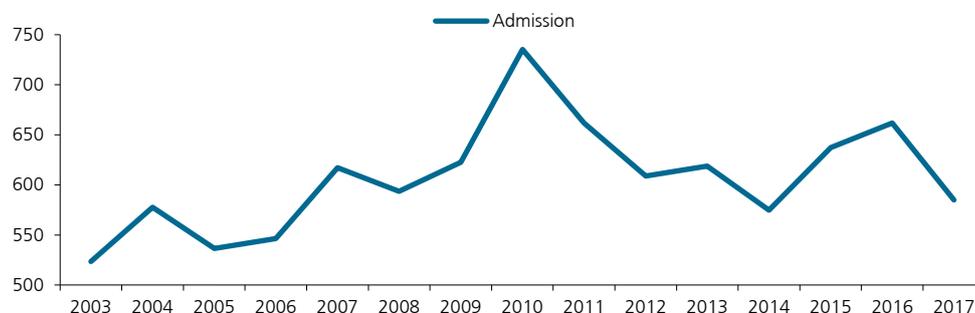
%	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Admission	10.3	-7.1	1.8	12.9	-3.8	4.9	18.1	-10.0	-8.0	1.6	-7.1	10.9	3.9	-11.6
Presence	11.8	-7.5	1.7	12.4	-4.1	-0.4	11.2	-7.9	-9.9	6.7	-6.1	8.6	6.1	-12.4

Source: Intesa Sanpaolo Research estimates

Looking at numbers, box office revenues fell by 11.63%, with a 12.38% decrease in presences in 2017. 536 films were distributed, including 218 of Italian production and co-production (up from 2016), with a market share that has risen to 40%. The 96 complementary distributed content (events, special editions, re-editions, and restored editions), despite the decrease in amount, recorded a 30.7% increase in revenues and 32.6% in attendance. Italian cinema saw a 46.35% decrease in revenues and 44.21% in tickets sold. The box office revenues depend on the fact that in 2016, the film "Quo Vado" alone corresponded to about 34% of receipts and 31% of

presences. Although 2017 was not a good year for Italian movies, American movies (programmed in Italian cinemas) performed better than 2016, recording a 5.24% increase in revenues and 3.37% in tickets sold. French cinema also had a substantial increase in revenues, about 112.11% more than 2016.

Box Office collections in Italian cinemas since 2003 (EUR M)



Source: Intesa Sanpaolo Research elaboration on Anica data

Given the market seasonality, the month with most collections was January, and the worst month was August, demonstrating how the summer represents a weak period for the Italian market. Compared to 2016, only 4 months had better performances (April, July, September, and December), while the best month (January) showed a decrease in revenues of 35.53%. The best box office film in 2017 was "Beauty and the Beast" with a collection of EUR 20.5M, the lowest amount for this figure since 2014.

Despite the negative years, in terms of revenues and tickets sold, cinema in Italy still attracts half of all spectators participating at live performances: alone it reaches a number equal to the sum of all the other sectors, from sports to theatre, from music to traveling entertainment. Even though the new ways of movie fruition, driven by technology, represent a limiting factor to theatrical distribution, they can also be turned into opportunities for the entire production chain. Thanks to its structure, which includes both distribution and film production, LMG can exploit this recent trend, managing to offset the lower productivity that could affect the distribution segment in the future.

The new Law n.220 came into effect at the end of 2016. 2017 was a transitional period, as considerable effort had been made in planning to make the most of this regulatory provision. The reform is fundamental for the sector as it brings new resources, cost savings and stimulates investments. This law also increases the tax credit, thus helping to underpin greater development.

European Theatrical Market

Looking at the situation in Europe, according to IHS Markit, the UK theatrical market had another record year with box office reaching a historical high of GBP 1,278M, a 4.1% yoy growth. 170.6M tickets were sold, slightly above the 2016 total. The result is particularly impressive given that 2016 was a 53-week year, while 2017 was a 52-week year.

In France, the cinema market has been stable over the past few years, and in 2017 only dropped slightly by 2% for both box office and admissions. Local titles "Valerian and the City of a Thousand Planets" and "R.A.I.D." Special Unit were the most viewed local films.

The box office in Germany returned to growth in 2017, but the rise was largely driven by an increase in the average ticket price, as cinema admissions dropped to a historical low of 118.1M.

The cinema market in Central and Eastern Europe continues to grow with most of the territories enjoying a good year in 2017. Russia continues to grow with cinema attendance increasing by 11.3%, and box office rising by 13.7% in local currency. Exchange rate is still an issue in the market which leads to a lower value in US dollars. Poland (7.5% in admissions and 12.3% in box office), Slovakia (17.5% in admissions and 18.3% in box office), Romania (11.3% in

admissions and 14.1% in box office) and Estonia (6.7% in admissions and 9.5% in box office) all posted a significant growth in 2017.

TV Production

The Italian television market is characterised by a strong concentration of revenues by the top 3 operators (Mediaset, Sky and RAI) which account for 90% of the total. As for Free TV, RAI is the largest player with an almost 50% market share, followed by Mediaset with 33%. This segment is estimated to reach about 25M Italian families, while 9M families subscribed to Pay TV. As for the latter, SKY dominates the segment with a 77% market share, followed by Mediaset with 20%.

In recent years, the appeal of the Italian TV series has increased, thanks to the success of high-budget productions, and to the new business approach adopted by Sky, Netflix and other digital providers. The first two are investing heavily in production and in the distribution of local series with targets that are no longer just local but also international. The recent big success of the Spanish series "La casa de papel", or the Italian "Gomorra", prove the success of this distribution approach.

Thanks also to the aforementioned Law n.220, there are significant financial and tax savings benefits for producers of Italian movies and series. We highlight in particular the legal obligation by broadcasters to invest part of revenues, ranging from 10 to 20%, in local productions.

Multiplex market

The Italian cinema market now essentially comprises multiplexes. In 2017 the revenue breakdown was:

- 130 multiplexes with more than 7 screens collected EUR 329.1M. The 1,354 screens in Italy generated about EUR 243k each;
- The smallest multiplexes, from 5 to 7 screens, had revenues of EUR 113.7M, with a yield for the 667 screens of approximately EUR 170k;
- The 313 cinemas from 2 to 4 rooms made EUR 92.2M (840 screens, average income EUR 109k);
- The 649 single-screen cinemas earned EUR 49.7M, i.e. around EUR 76k per screen.

In this context, the group (through the subsidiary Stella Film) ranks among the major players in the Italian market, preceded only by UCI and The Space. However, it should be noted that Stella is ranked as the first independent Italian player in the market.

The new legislative framework

With the enforcement of the new cinema and audio-visual law in January 2017 ("Legge Cinema n° 220/2016"), companies in the cinematographic sector can benefit from numerous incentives and aids for the production and distribution of film content.

First, the **"Fund for the development of investments in cinema and audio-visual"** was created, to support film and audio-visual interventions through tax incentives and automatic contributions that unify the current resources from Fus Cinema and tax credit. Thanks to the fund, the resources should increase by 60% (quantified at EUR 150M). The fund is fuelled directly by revenue already coming from the activities of programming and television transmission, film distribution, cinematographic projection, and the provision of Internet access services by telephone and telecommunications companies. Thus, as from 2017, a fixed percentage (11%) of the IRES and VAT proceeds from these activities will constitute the basis for the calculation of the state resources allocated to the financing of the Cinema and the audio-visual sector. There are no new taxes, but an innovative and virtuous mechanism of "self-financing" of the production chain, that is incentivised to invest and innovate and removes the current uncertainty as to the funds to be allocated to the cinematographic sector: the new fund will never fall below EUR 400M annually.

Up to 18% of the fund is also dedicated each year to support:

- Films by first-and second-time directors;
- Young authors;
- Start-ups;
- Small cinema rooms;
- Contributions to festivals and quality reviews;
- Contributions for the activities of the Venice Biennale, Istituto Luce Cinecittà and the Experimental Cinematography Centre.

3% of the fund is then reserved for actions to strengthen students' cinematographic and audio-visual skills, on the basis of intervention lines agreed by the Ministry of Cultural Heritage Activities and Tourism with the Ministry of Education and Scientific Research.

The new Cinema Law also abolishes the ministerial commissions for the allocation of funding based on the so-called 'cultural interest' and introduces a system of automatic incentives for Italian works. Along with tax concessions, automatic contributions arise whose quantification takes place according to objective parameters that takes into account economic and artistic results: from the awards received to the success in the hall. Film and audio-visual producers and distributors will receive contributions to make new productions.

Furthermore, the existing **6 Tax Credits** have been strengthened to encourage film and audio-visual production and distribution and to encourage foreign investments in the sector. The entities which can benefit from the 6 Tax Credits are:

- Production, distribution, and post-production companies;
- Distributors who plan Italian cinema, encouraging competition and increasing market share;
- Italian companies that work for foreign productions;
- Companies outside the sector that invest in Italian cinema;
- Companies who manage the cinema rooms.

In order to help audio-visual market players overcome the difficulties to access credit, a special section of the Guarantee Fund for small and medium-sized enterprises was set up by a decree by Mise and Mibact, to guarantee financing operations for audio-visual products. This unit has an initial endowment of EUR 5M.

The strengthening of the support to cinema and audio-visual production is accompanied by an incentive intervention for those who restructure and invest in new cinemas. On the multiplex side, in fact, the number of screens and the quality of the rooms will increase, involving a much wider number of spectators, in favour of Italian films. For this reason, an **extraordinary plan** for up to EUR 120M in five years, has been drawn up, in order to re-open the closed rooms and open new ones.

Moreover, the recognition of the status of "cultural interest" for cinemas will be easier to obtain. Thanks to this intervention it will be possible to favour the conservation and valorisation of the historical rooms through the constraint of intended use.

At the government level, as a substitute for the Cinema Section of the Consulta dello Spettacolo, the **Superior Council for Cinema and Audio-visual** has been established, which carries out sector policy-making activities, regarding the definition of guidelines and general investment criteria in support of cinematographic and audio-visual activities. The Board comprises 11 members of high competence and experience in the sector and representatives of the main associations.

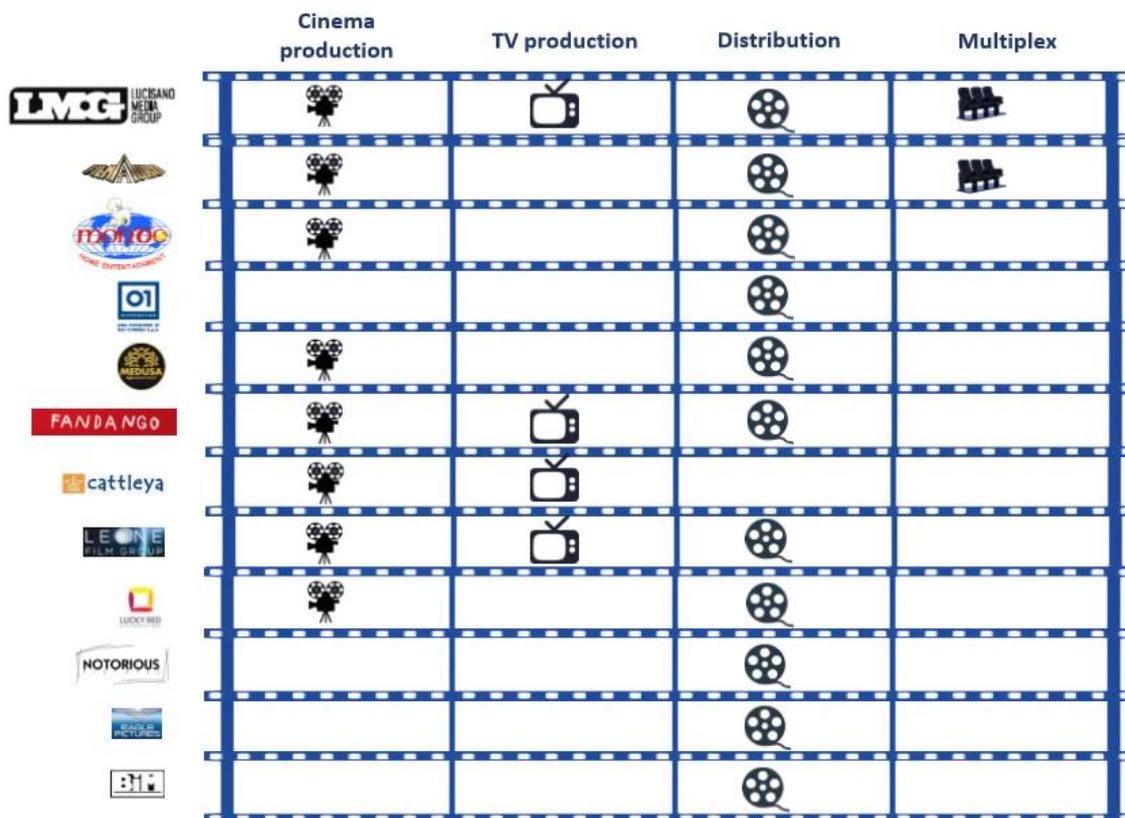
Regarding the television market, the law provides stricter procedures for the programming of films on TV and for television investments. The Government has been delegated to adopt one or more legislative decrees to introduce more transparent and effective procedures concerning the investment and planning obligations of European and local audio-visual works by the suppliers of audio-visual media services.

Lastly, another important measure was taken on state censorship. In fact, there will **no longer be ministerial commissions to evaluate the films**, with the law that provides a proxy to the government to define a new classification system that makes film producers and distributors more responsible. As already happens in other sectors, the same operators will define and classify their films; the State intervenes and sanctions only in cases of abuse.

Competitive Positioning

In the chart below, we show the competitive positioning of Lucisano vs. its main Italian competitors, where it emerges as the only fully integrated player.

Competitive Landscape



Source: Company data

Historical Financials

FY17A results

In FY17A, revenues increased by 0.7% to EUR 38.4M, with revenues from services down by 4.6% to EUR 28.1M and other revenues up by 19% to EUR 10.2M.

Lucisano Media Group - Key economic data (FY17)			
EUR M	FY16A	FY17A	yoy %
Revenues from services	29.5	28.1	-4.6
Other revenues	8.6	10.2	19.0
Revenues	38.1	38.4	0.7
EBITDA	15.0	14.2	-5.4
EBITDA margin (%)	39.3	36.9	
EBIT	6.1	5.8	-5.8
Net income	3.9	3.8	-3.4
Net debt	23.2	30.9	33.0

A: actual; Source: Company data

The main drivers of revenues from services were:

- Revenues from box office at multiplexes decreased by 5.8% to EUR 9.3M, due to lower admissions;
- Revenues from TV rights were broadly stable at EUR 5.9M;
- The "Sale of film property shares" revenues increased by 13.8% to EUR 5.1M;
- Other revenues from multiplexes were broadly stable at EUR 2.4M;
- The contribution from third parties was EUR 2.3M, and was mainly attributable to the contract stipulated with RAI for the sale of the work "Prima che la notte";
- Revenues from film distribution increased by 11.3% to EUR 1.4M, due to the good results of works released in theatres;
- Revenues from HV - Est - Vod - Svod³ services rose significantly to EUR 1.3M. This result follows a change in consumer preferences towards new technologies and ways of viewing films and television series, and is starting to represent an important revenues item for the group.

Lucisano Media Group - Revenues from service break-down (FY17A)			
EUR M	FY16A	FY17A	yoy %
Theatrical distribution	1.2	1.4	11.3
TV rights	5.9	5.9	-0.9
Hv - Est - Vod - Svod Rights	0.2	1.3	610.4
Third-party contributions	4.0	2.3	-42.9
Sale of film property shares	4.5	5.1	13.8
Other revenues from film works	1.2	0.5	-63.5
Multiplexes – box office collections	9.9	9.3	-5.8
Multiplexes - others	2.4	2.4	-2.3
Others	0.1	0.1	-17.9

A: actual; Source: Company data

Other revenues were broken down as follows:

- A 61.9% increase in revenues from contributions to EUR 1.7M, represented by government grants on the proceeds accrued for films produced and distributed;

³ **Est** = electronic-sell-through (the model whereby a consumer purchases or perpetually licences a digital reproduction); **Vod** = Video-on-demand (content not owned or perpetually licensed by the consumer that is either streamed or downloaded to an internet-connected device for viewing by the end-user at the end-user's discretion on an on-demand basis); **Svod** = subscription video-on-demand (for a fixed, recurring fee, subscribers may have unlimited streaming to a licensed catalogue of content for the duration of their active subscription term); Source: DIGITAL EMA

- Income from tax credits doubled to EUR 4M, mostly reported in relation to the cost of films made during the year for which specific requests were presented to the MIBAC as required by law 244/2007;
- Revenues from associated partnership contracts decreased from EUR 1.5M in 2016 to EUR 1M in 2017. These revenues represent the share of external investors' contributions that will not have to be repaid based on contractual agreements and are related to the performances of the respective films;
- Thanks to the regional contributions for the films produced in 2016-17, there was also a substantial increase in grants for current expenses, which increased by 305.6%.

Lucisano Media Group - Other revenues breakdown (FY17A)			
EUR M	FY16A	FY17A	yoy %
Grants – in aid	1.1	1.7	61.9
Tax credit	2.0	4.0	102.3
External tax credit	1.5	1.0	-34.9
Other grants	0.4	1.5	305.6
Other	3.7	2.1	-44.9

A: actual; Source: Company data

Looking at costs, we highlight that:

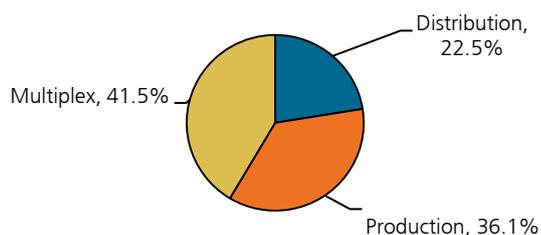
- Raw materials costs rose by 15.5% to EUR 0.6M (weighting in revenues at 1.6% vs. 1.4% in FY16A). These costs are related both to the purchase of products destined for resale in the multiplex bars and to the purchase of maintenance and consumable materials for digital projectors in cinemas;
- Increase of 20.6% in costs for services to EUR 29.9M, which have the highest weighting in the general distribution of costs (weighting in revenues at 77.9% vs. 65% in FY16A). Within this category, the items that contributed most to this increase were film production costs (+41.4% to EUR 14.7M), costs for film projects (+47% to EUR 1.3M), and other costs (+25.3% to EUR 2.5M, which include costs for the participation in industry festivals and other operating costs). On the other hand, there was a decrease in costs related to the management of multiplexes, following the abovementioned decrease in revenues: the cost for renting movies decreased by 4.8% to EUR 4.3M, rent of theatres declined by 3.7% to EUR 1.6M;
- Labour costs rose by 13.9% to EUR 3.3M (weighting in revenues at 8.5% vs. 7.5% in FY16A);
- Capitalised costs grew by 69.1% to reach EUR 10.1M. These costs refer to the costs incurred to produce film works that were suspended and capitalised with respect to the intangible asset item costs of film production in progress.

Lucisano Media Group - Costs breakdown (FY17A)			
EUR M	FY16A	FY17A	yoy %
Raw materials (net)	0.5	0.6	15.5
Cost for services	24.8	29.9	20.6
Cost of labour	2.9	3.3	13.9
Other costs	0.9	0.5	-41.7
Capitalised costs	-6.0	-10.1	69.1
Weighting in revenue (%)	FY16A	FY17A	
Raw materials (net)	1.4	1.6	
Cost for services	65.0	77.9	
Cost of labour	7.5	8.5	
Other costs	2.4	1.4	
Capitalised costs	-15.7	-26.3	

A: actual; Source: Company data

The expenses which have historically impacted revenues the most are service costs, which absorb around 60/70% of revenues, with a substantial increase in 2017, due to the postponement of the releases of several films produced and distributed. The production of films and television series generates and capitalises the greatest amount of costs, and the management of multiplexes is the business unit whose costs have a greater impact on EBITDA, due to the costs to rent cinemas and films.

Lucisano Media Group - Costs by business unit (FY17A)



Source: Company data

Reflecting the abovementioned trends in revenues and costs, FY17A EBITDA was EUR 14.2M (-5.4% yoy), with a margin contraction of 240bps to 36.9%. D&A decreased by 5.2% to EUR 8.4M, including EUR 6.2M of depreciation of immaterial assets (investments in movie production and acquisition of distribution rights), and EUR 1.9M in depreciation of material assets (buildings and machineries in theatres). Therefore, EBIT was EUR 5.8M, -5.8% yoy. Financial charges were broadly stable at EUR 1M, leading to a EUR 3.8M net income (-3.4% yoy).

Business unit analysis

Lucisano's operations can be divided into three business units, the Production BU, the Distribution BU, and the Multiplex BU:

- **Production:** revenues increased by 0.2% to EUR 21.3M, and EBITDA grew by 6.4% to EUR 13.2M, thanks to the reduction in production costs and the increase in revenues coming from government contributions and tax credit. Net income was EUR 11.7M, +9.2% yoy;
- **Distribution:** revenue rose by 52.1% to EUR 4.3M, also thanks to the Hv-Est-Vod-Svod platforms, which still represent a marginal contribution to total revenue, but shows a change in consumer preferences towards new ways of watching media content. EBITDA declined to EUR -0.5M from EUR 0.1M in 2016, due to higher distribution costs. The unit reported a net loss of EUR 7.3M, -11.1% yoy;
- **Multiplex** was affected by lower admissions (1.88M vs. 2.02M in FY16A), therefore revenues declined by 8.7% to EUR 12.9M. Revenue contraction also affected EBITDA, which declined by 39.2% to EUR 1.5M. Net loss was EUR 0.5M.

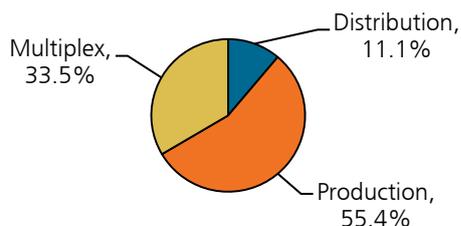
Lucisano Media Group - Business units breakdown (FY17 vs. FY16)

EUR M	Production			Distribution			Multiplex		
	FY16A	FY17A	yoy %	FY16A	FY17A	yoy %	FY16A	FY17A	yoy %
Revenue	21.2	21.3	0.2	2.8	4.3	52.1	14.1	12.9	-8.7
EBITDA	12.4	13.2	6.4	0.1	-0.5	NM	2.5	1.5	-39.2
EBITDA margin (%)	58.3	61.9		4.0	-12.1		17.7	11.8	
EBIT	12.4	13.2	6.4	-6.3	-7.0	-11.2	0.04	-0.4	NM
Net income	10.7	11.7	9.2	-6.6	-7.3	-11.1	-0.09	-0.5	NM

NM: not meaningful; A: actual; Source: Company data

In the chart below, we show the weighting in total revenues of the three business units.

Lucisano Media Group - Revenues by business unit (FY17A)



Source: Company data

Finally, we highlight that the production BU revenues benefit from the tax credit, as of the new Italian regulatory framework, and from public contributions.

Alongside supporting production revenues, the tax credit and grants flow directly to the production BU EBITDA, which reports a margin of around 60%, broadly stable over the recent years.

Net debt and net working capital

As for the group's existing loans, in 2016, a EUR 40M financing was renewed with a pool of banks including Unicredit S.p.A and Mediocredito Italiano S.p.A. This loan was undertaken to finance the acquisition and production of new films, as well as to have a credit discounting in relation to the production and distribution of films. This loan must be repaid by February 2024, ideally through the proceeds from films. In recent years, the group has also committed to reducing the debt, which has led to a gradual decrease in financial expenses, which in 2017 amounted to EUR 0.971M.

In FY17, the net financial position, amounting to EUR 30.9M, increased by approximately EUR 8.2M vs. EUR 23.2M as of 31 December 2016, mainly due to the significant investments by the subsidiary Italian International Film S.r.l. in the production and purchase of film works and the launch of the expansion works of the Benevento multiplex. These investments only partially realised their revenues and the consequent cash flows. Four 2017 productions, in fact, are going to be released in 2018. Similarly, acquisitions of films on international markets have found their place in new agreements signed at the end of 2017 with M2 Pictures and Vision Distribution, and will be released between 2018 and 2019.

Shareholders' equity increased from EUR 28.7M to EUR 31.7M due to the positive result of the year.

Net working capital increased by approximately EUR 6.2M due to the combined effect of the increase in receivables related to public contributions (state and regional) and the decrease in payables linked to the contributions from external investors.

We highlight that the net debt/EBITDA ratio increased from 1.5x in FY16A to 2.2x in FY17A, a level we regard as sustainable.

Lucisano Media Group - Key balance sheet items FY17A)		
EUR M	FY16A	FY17A
Equity	28.9	31.9
Net working capital	14.6	20.8
Net working capital to revenue (%)	38.3	54.3
Net debt	23.2	30.9
Net debt/EBITDA (x)	1.5	2.2

A: actual; Source: Company data

Earnings Outlook

From revenues to EBITDA...

We expect revenues to slightly increase in FY18E vs. FY17A, to then grow by 20.5% in FY19E and by 8.7% in FY20E.

Lucisano Media Group - Revenues breakdown (FY17A-20E)				
EUR M	FY17A	FY18E	FY19E	FY20E
Production	21.3	22.7	28.4	31.3
Distribution	4.3	4.6	6.0	6.7
Multiplex	12.9	11.5	12.5	13.0
Total revenues	38.4	38.9	46.8	50.9

A: actual; E: estimates; Source: Company data and Intesa Sanpaolo Research

The key drivers of our revenue assumptions are:

Our revenue assumptions

- **Production:** in FY18E, 3 movies have already been released and a further 2 are already programmed for release at the end of September and in mid-October, as shown in the table below. We project an increase of around 7% vs. FY17A, when 4 movies were released. For FY19E and FY20E, we expect a significant growth (+25% and +10% yoy, respectively), driven by 4-5 movies release (see the table below) and by the release of one important TV series each year (worth between EUR 5M and EUR 9M). We did not include in our FY18-20E estimates any contribution from the international TV series "Les Italiens", given the uncertainty about the start of the production, but it may represent a positive surprise on top of our projections.

Lucisano Media Group - Production releases	
Film	
Nessuno come Noi	Oct-18
Io c'è	released
Prima che la Notte	released
Ricchi di Fantasia	Sep-18
Una vita spericolata	released
Non ci resta che il crimine	2019
Aspromonte	
Gli uomini d'oro	
Sienna	
Mollami!	

Source: Company data

- **Distribution:** for FY18-20E, we expect a yoy growth broadly in line with the production trend;

Lucisano Media Group - Distribution releases	
Film	
Georgetown	18/19
Departures	18/19
Escape Plan 2	released
Megan Leavey	18/19
The Foreigner	18/19
Gringo	18/19
Hurricane Heist	released
Terminal	18/19

Source: Company data

- **Multiplex:** regarding multiplex revenues, we assumed that the number of visitors decreases in FY18E given the distribution releases so far this year and in line with the Italian market trend (no "blockbuster" in the year), to then recover in FY19E and slightly increase in FY20E. We assume a stable average ticket price, while we slightly increased the average revenue for miscellaneous revenues (beverage, snacks, etc.).

Lucisano Media Group - Multiplex assumptions (FY17A-20E)				
	FY17A	FY18E	FY19E	FY20E
Visitors (M)	1.88	1.69	1.83	1.89
Occupancy rate (%)	53.9	48.5	52.5	54.1
Average ticket (EUR)	4.9	4.9	4.9	5.0
Average miscellaneous (EUR)	1.3	1.3	1.3	1.4

A: actual; E: estimates; Source: Company data and Intesa Sanpaolo Research

At the EBITDA line, we assumed a margin of around 60% for the production BU (58.3% in FY16A and 61.9% in FY17A), and of 2% for the distribution BU, which we calculated at breakeven for both FY16A and FY17A. For the multiplex BU, we assume an around 7% margin in FY18E, slightly increasing to 9% in FY20E (17.7% in FY16A and 11.8% in FY17A). The EBITDA margin in FY18-20E should range between 38% and 39% (it was around 40% in the average FY13A-17A).

Lucisano Media Group - EBITDA breakdown (FY17A-20E)				
EUR M	FY17A	FY18E	FY19E	FY20E
Production	13.2	13.9	17.2	18.5
Distribution	-0.5	0.1	0.1	0.1
Multiplex	1.5	0.8	1.0	1.2
Total EBITDA	14.2	14.8	18.3	19.8
Total EBITDA margin (%)	36.9	38.0	39.1	38.8

A: actual; E: estimates; Source: Company data and Intesa Sanpaolo Research

... and from EBITDA to net income

For D&A, we assume a depreciation of material assets (mainly the multiplexes) broadly stable at EUR 2M, while for the depreciation of immaterial assets (EUR 6.2M in FY17A, related to the capitalisation of production costs and/or to licence rights), we assumed an increase up to EUR 11M in FY20E, in line with the capex trend. Due to the abovementioned dynamics, we expect an EBIT decline in FY18E (EUR 4.6M vs. EUR 5.8M in FY17A), then an increase to EUR 6.8M in FY19E and EUR 6.8M in FY20E.

Lucisano Media Group - Earnings (FY17A-20E)				
EUR M	FY17A	FY18E	FY19E	FY20E
EBITDA	14.2	14.8	18.3	19.8
EBITDA margin %	36.9	38.0	39.1	38.8
D&A	-8.4	-10.2	-11.5	-13.0
EBIT	5.8	4.6	6.8	6.8
EBIT margin %	15.0	11.9	14.6	13.3
Pre-tax profit	4.8	3.8	6.0	6.0
Tax	-1.0	-0.8	-1.3	-1.3
Net income	3.8	3.0	4.8	4.7

A: actual; E: estimates; Source: Company data and Intesa Sanpaolo Research

Net income should follow a trend similar to EBIT, with a contraction in FY18E (EUR 3.0M vs. EUR 3.8M in FY17A), followed by an increase to EUR 4.8M in FY19E and EUR 4.7M in FY20E, with a 2017A-20E EPS CAGR of around 8%.

Cash flow

We projected a working capital ratio and a capex/revenue ratio broadly in line with FY17A. Net debt should reduce from EUR 30.9M in FY17A to EUR 24M in FY20E, also including a EUR 5cent dividend per year (a 2.7% yield).

We calculate that the net debt/EBITDA ratio, thanks to the cash generation and the increase in EBITDA, should decrease from 2.2x in FY17A to 1.2x in FY20E.

Lucisano Media Group - Cash flow (FY17A-20E)				
EUR M	FY17A	FY18E	FY19E	FY20E
Net fin debt beg of year	23.2	30.9	27.1	26.6
Net income	3.8	3.0	4.8	4.7
Depreciation	8.4	10.2	11.5	13.0
Change in working capital	-7.4	1.1	-3.2	-1.7
Operating cash flow	4.8	14.2	13.0	16.0
Capex	-11.7	-9.7	-11.7	-12.7
Investments	0.0	0.0	0.0	0.0
Disposals	0.0	0.0	0.0	0.0
Free cash flow	-6.9	4.5	1.3	3.3
Dividends	-0.7	-0.7	-0.7	-0.7
Other movements	-0.1	0.0	0.0	0.0
Cash flow	-7.7	3.8	0.6	2.5
Net fin debt end of year	30.9	27.1	26.6	24.0
Net debt/EBITDA (x)	2.2	1.8	1.5	1.2

A: actual; E: estimates; Source: Company data and Intesa Sanpaolo Research

Lucisano Media Group - Key data							
Rating	Target price (EUR/sh)	Mkt price (EUR/sh)	Sector	Free float (%)		Reuters Code	
BUY	Ord 3.3	Ord 1.81	Media	11.9		LMG.MI	
Values per share (EUR)			2016A	2017A	2018E	2019E	2020E
No. ordinary shares (M)			14.88	14.88	14.88	14.88	14.88
No. NC saving/preferred shares (M)			0.00	0.00	0.00	0.00	0.00
Total no. of shares (M)			14.88	14.88	14.88	14.88	14.88
Market cap (EUR M)			21.88	34.79	27.00	27.00	27.00
Adj. EPS			0.20	0.26	0.20	0.32	0.32
CFPS			0.86	0.82	0.88	1.1	1.2
BVPS			1.9	2.1	2.3	2.6	2.8
Dividend ord			0.05	0.05	0.05	0.05	0.05
Income statement (EUR M)			2016A	2017A	2018E	2019E	2020E
Revenues			38.11	38.39	38.87	46.85	50.92
EBITDA			14.98	14.17	14.78	18.32	19.75
EBIT			6.12	5.77	4.63	6.82	6.75
Pre-tax income			5.15	4.80	3.75	6.01	6.00
Net income			3.94	3.80	2.97	4.75	4.74
Adj. net income			2.99	3.80	2.97	4.75	4.74
Cash flow (EUR M)			2016A	2017A	2018E	2019E	2020E
Net income before minorities			4.0	3.8	3.0	4.8	4.7
Depreciation and provisions			8.9	8.4	10.2	11.5	13.0
Others/Uses of funds			0	0	0	0	0
Change in working capital			1.1	-7.4	1.1	-3.2	-1.7
Operating cash flow			13.9	4.8	14.2	13.0	16.0
Capital expenditure			-8.6	-11.7	-9.7	-11.7	-12.7
Financial investments			0	0	0	0	0
Acquisitions and disposals			0	0	0	0	0
Free cash flow			5.4	-6.9	4.5	1.3	3.3
Dividends			-0.7	-0.7	-0.7	-0.7	-0.7
Equity changes & Other non-operating items			-0.4	-0.1	0	0	0
Net cash flow			4.3	-7.7	3.8	0.6	2.5
Balance sheet (EUR M)			2016A	2017A	2018E	2019E	2020E
Net capital employed			52.1	62.8	61.2	64.7	66.1
of which associates			0	0	0	0	0
Net debt/-cash			23.2	30.9	27.1	26.6	24.1
Minorities			0.2	0.2	0.2	0.2	0.2
Net equity			28.7	31.7	33.9	37.9	41.9
Minorities value			0	0	0	0	0
Enterprise value			45.2	65.9	54.3	53.7	51.2
Stock market ratios (x)			2016A	2017A	2018E	2019E	2020E
Adj. P/E			7.3	9.2	9.1	5.7	5.7
P/CFPS			1.7	2.9	2.1	1.7	1.5
P/BVPS			0.76	1.1	0.79	0.71	0.64
Payout (%)			25	20	25	16	16
Dividend yield (% ord)			3.4	2.1	2.8	2.8	2.8
FCF yield (%)			24.6	-19.7	16.7	4.8	12.1
EV/sales			1.2	1.7	1.4	1.1	1.0
EV/EBITDA			3.0	4.7	3.7	2.9	2.6
EV/EBIT			7.4	11.4	11.7	7.9	7.6
EV/CE			0.87	1.0	0.89	0.83	0.77
D/EBITDA			1.5	2.2	1.8	1.5	1.2
D/EBIT			3.8	5.4	5.9	3.9	3.6
Profitability & financial ratios (%)			2016A	2017A	2018E	2019E	2020E
EBITDA margin			39.3	36.9	38.0	39.1	38.8
EBIT margin			16.1	15.0	11.9	14.6	13.3
Tax rate			22.0	20.5	21.0	21.0	21.0
Net income margin			10.3	9.9	7.6	10.1	9.3
ROCE			11.8	9.2	7.6	10.5	10.2
ROE			14.4	12.6	9.0	13.2	11.9
Interest cover			6.3	5.9	5.3	8.5	8.9
Debt/equity ratio			80.4	96.9	79.6	69.8	57.2
Growth (%)				2017A	2018E	2019E	2020E
Sales				0.7	1.2	20.5	8.7
EBITDA				-5.4	4.3	24.0	7.8
EBIT				-5.8	-19.9	47.4	-0.9
Pre-tax income				-6.8	-21.8	60.1	-0.3
Net income				-3.4	-22.0	60.1	-0.3
Adj. net income				27.2	-22.0	60.1	-0.3

NM: not meaningful; NA: not available; A: actual; E: estimates; Source: Company data and Intesa Sanpaolo Research

Appendix 1: Brief Description of LMG Peers

Notorious engages in the acquisition of rights of cinematographic works and its distribution and marketing through all available channels. Its activities for the acquired films include the editing for the Italian market, printing and advertising, theatrical release, home video distribution, sale of television rights, and sale of new media rights.

Notorious: founded by Guglielmo Marchetti on 4 July 2012, headquartered in Rome, Italy

Leone Film engages in the production, co-production, and distribution of audiovisual products. It operates through the following business units: Film Production, Distribution. The Film Production unit engages in filmmaking produced independently by the company or with the participation of third parties for the Italian market; as well as co-producing of films made for the international market. The Distribution unit exploits film rights that belong to the company's library through cinema, home entertainment, free television, pay television, video on demand, subscription video on demand, and new media marketing channels.

Leone Film: founded by Sergio Leone in 1989, headquartered in Rome, Italy

Lions Gate Entertainment engages in motion picture production and distribution, television programming and syndication, home entertainment, family entertainment, digital distribution, new channel platforms and international distribution and sales. It operates through the following segments: Motion Pictures, Media Networks and Television Production segments. The Motion Pictures segment consists in the development and production of feature films, acquisition of North American and worldwide distribution rights, North American theatrical, home entertainment and television distribution of feature films produced and acquired, and worldwide licensing of distribution rights to feature films produced and acquired. The Television Production segment is involved in the development, production and worldwide distribution of television productions, including television series, television movies and mini-series and non-fiction programming. The Media Networks segment consists of starz networks, which includes the licensing of premium subscription video programming to US multichannel video programming distributors; streaming services, which represent the Lionsgate legacy start-up direct to consumer streaming services on its subscription video-on-demand; and content & other, which includes the licensing of the Media Networks' original series programming to digital media platforms, international television networks, home entertainment and other ancillary markets.

Lions Gate Entertainment: founded by Frank Guistra on 28 April 1997, headquartered in Santa Monica, CA (US)

Mondo TV engages in the production and distribution of animated cartoon series and full-length feature films for television and cinema. It distributes its own productions and Japanese cartoon series in Italy as well as in some Spanish-speaking territories. Its ancillary activities include the sale and rental of home videos, soundtracks, software, publications and merchandise based on its cartoon series and movies.

Mondo TV: founded by Orlando Corradi on 13 December 1985, headquartered in Rome, Italy

Medusa Film engages in the production and distribution of motion pictures. The company was established in 1995, and has its head office in Rome, Italy. The company is a leading operator in the film distribution sector. The company offers film producing and distributing services for Italian and international movies. The company's editorial line focuses on Italian productions that include various genres, including comedies, romantic movies, and action. The company is the movie production and distribution arm of former Italian Prime Minister Silvio Berlusconi's Fininvest, which is one of Italy's leading purveyors of comedy. Its product offerings include full-length films, short films, documentaries, drama, radio and television programs. The company also distributes foreign films in Italy, such as the United States movies, What Women Want and Autumn in New York.

Medusa Film: operates as a subsidiary of Mediaset SpA, which operates in the television (TV) industry in Italy and Spain

Lucky Red engages in the business of motion picture and video production in Italy. The company is primarily involved in producing motion pictures, videos, television programs, and television commercials. Some of its programs include reality TV, documentary series, game shows and movies.

Lucky Red: operates in Italy since 1987, headquarters located in Potsdam

Eagle Picture engages in motion picture and video production. The company is primarily involved in producing and distributing motion pictures, videos, television programs, or television commercials. Its business operation is principally active in Italy. The company operates as one of the subsidiaries of Prima TV Spa, which operates as a production and distribution company in theatrical and home entertainment markets.

Eagle Picture: founded in 1986, registered business office strategically in Milan, Italy

Appendix 2: LMG History at a Glance

Lucisano Media Group was founded in Rome in 1958 by Fulvio Lucisano, and since then has been characterised by an intense production activity, realising films that have become milestones at the national cinema level, particularly for Italian comedy. The group has steadily expanded its activities to become a leading independent Italian film and television producer and distributor. The main development steps up to 2017 are shown below:

Lucisano Media Group – Group history	
Year	Event
1958	Italian International Film is established in Rome by Fulvio Lucisano
1960	Beginning of the production of films and the international co-production activities
1970	Production of the “Italian comedies” and the “spaghetti western” films
1980	Exclusive contracts for the distribution of Cannon Group Inc. movies, and distribution agreement for Metro Goldwyn Mayer Inc. (MGM) films
1990	Distribution agreement for Polygram Filmed Entertainment films
1995	Establishment of IIF Homevideo and the De Laurentis-Lucisano cinema circuit
1996	Inauguration of the Modernissimo Multiplex in Naples
1998	Fulvio Lucisano is nominated chairman of ANICA, and the Andromeda Multiplex in Rome is inaugurated
2001	Beginning of the TV production and inauguration of “Big Maxicinema” Multiplex
2002	Beginning of the production of television miniseries and the inauguration of the “Happy Maxicinema” multiplex
2003	Federica Lucisano became CEO of IIF and chairwoman of the group
2006	Acquisition of Stella Film and release of the film “Notte prima degli esami”
2007	Inauguration of the “Andromeda Brindisi” multiplex; Fulvio Lucisano is appointed “Cavaliere del Lavoro” (Knight of Labor)
2008	First co-production with Walt Disney
2009	Fulvio Lucisano received the David of Donatello for his career
2009-13	Releases of many blockbuster films produced such as “Maschi contro femmine”, “Ex”, “Viva l’Italia”, “Mai stati uniti”, and “Buongiorno Papà”
2014	Listing on the AIM segment of Borsa Italiana S.p.A.
2015	Inauguration of the first Imax room in South Italy inside the Happy Maxicinema multiplex in Afragola, and release of the film “Noi e la Giulia”, which won several awards
2016	Constitution of the distribution company “Vision Distribution S.p.A”, together with Sky Italia, Cattleya, Palomar, Indiana production, and Wildside
2017	Alevi S.r.l enters the group’s shareholding structure

Source: Company data

Appendix 3: Tax Credit

The law n. 220 of 2016 introduced a Cinema and Audio-visual Fund with an endowment of EUR 400M per year for the financing of all financial instruments to support the sector, from tax incentives in the form of tax credits to automatic contributions, from the facilities for the film and audio-visual promotion to the Plan for the upgrading of the rooms.

The whole tax credit system has been revised by law, which provides for:

- A tax credit for production companies, of no less than 15% and no more than 30% of the total cost to produce cinematographic and audio-visual works;
- A tax credit for film distribution companies, of no less than 15% and no more than 30% of the total expenses incurred for the local and international distribution of cinematographic and audio-visual works;
- A tax credit for companies in the film industry, the technical and post-production industries, of no less than 20% and no more than 49% of the total expenses incurred for the restructuring and the structural and technological adaptation of cinemas and the related facilities and ancillary services, and for the construction of new rooms or the restoration of inactive rooms;
- A tax credit for the upgrading of the Italian and European film offer, commensurate with the planning of Italian and European works carried out in the respective rooms by exhibitors;
- A tax credit for the attraction in Italy of cinematographic and audio-visual investments, therefore regarding cinematographic and audio-visual works or parts realised in Italy, using Italian workers, commissioned by foreign productions, with an entity of between 20% and 30% of the production cost of the single work;
- A tax credit for companies not belonging to the cinematographic and audio-visual sector associated in participation pursuant to Article 2549 of the Italian Civil Code, applying a maximum rate of 30% of the cash contribution made by these companies to the production and distribution in Italy and abroad of cinematographic and audio-visual works.

Notes

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Target price and market price trend (-1Y)	Historical recommendations and target price trend (-1Y)				
	BUY	ADD	HOLD	REDUCE	SELL
Initiation of Coverage					
Initiation of Coverage					

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Equity rating key (short-term horizon: 3M)

Equity rating key (short-term horizon: 3M)	
Short-term rating	Definition
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In particular, the description of the measures taken to manage interest and conflicts of interest – related to Articles 5 and 6 of the Commission Delegated Regulation (EU) 2016/958 of 9 March 2016 supplementing Regulation (EU) No. 596/2014 of the European Parliament and of the Council with regard to regulatory technical standards for the technical arrangements for objective presentation of investment recommendations or other information recommending or suggesting an investment strategy and for disclosure of particular interests or indications of conflicts of interest as subsequently amended and supplemented, the FINRA Rule 2241, as well as the FCA Conduct of Business Sourcebook rules COBS 12.4 - between the Intesa Sanpaolo Banking Group and issuers of financial instruments, and their group companies, and referred to in research products produced by analysts at Intesa Sanpaolo S.p.A. is available in the "Rules for Research " and in the extract of the "Corporate model on the management of inside information and conflicts of interest" published on the website of Intesa Sanpaolo S.p.A.

At the Intesa Sanpaolo website, webpage http://www.group.intesasanpaolo.com/scriptlsir0/si09/studi/eng_archivio_conflitti_mad.jsp you can find the archive of disclosure of interests or conflicts of interest of the Intesa Sanpaolo Banking Group in compliance with the applicable laws and regulations.

Furthermore, we disclose the following information on the Intesa Sanpaolo Banking Group's conflicts of interest:

- 1 One or more of the companies of the Intesa Sanpaolo Banking Group plan to solicit investment banking business or intends to seek compensation from Lucisano Media Group in the next three months
- 2 Banca IMI acts as Specialist, Nominated Advisor relative to securities issued by Lucisano Media Group

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