EDISON

Technicolor

Q1 results

Addressing the headwinds

Media

Technicolor's Q1 results reflect limited COVID-19 impact, which will show more markedly in Q2. Q1 disruption to Connected Home's Chinese supply chain is now broadly resolved, while lower activity in Production Services' Film and Episodic visual special effects (VFX) had been flagged previously. Connected Home is seeing good US broadband demand, while Production Services is being hit by the industry's cessation of live action filming. The group is on track to achieve run-rate cost savings of €100m by end FY20 and has identified a further €75m over the earlier €150m target for the next three years. Management anticipates reinstating guidance prior to the planned €300m equity fund raise and our estimates remain under review.

Year end	Revenue (€m)	EBITA (€m)	PBT* (€m)	EPS* (c)	DPS (c)	P/E (x)
12/17	4,253	151	47	(4.3)	0.0	N/A
12/18	3,988	98	7	(3.2)	0.0	N/A
12/19	3,800	42	(97)	(6.5)	0.0	N/A

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Mixed Q1 performance by segment

Group Q120 revenues were down 14.1% to €739m (constant currency), with adjusted EBITDA 17.3% lower at €27m. Reduced rendering costs led to a smaller adjusted EBITA loss, management's preferred earnings measure. The three business segments all had lower revenues, with divergent earnings performance. Reduced activity levels at Production Services Film and Episodic VFX reflected delays in green-lighting projects by a major client while it dealt with internal issues, resulting in a higher adjusted EBITA loss of €15m (H119: €4m loss). DVD Services' performance was in line with previous trends, while Connected Home had a good North American result, where broadband demand was robust and revenues rose 11%. Other markets were weaker, notably video in Europe/Asia and Latin America, where conditions were volatile. Management estimates exceptional costs related to COVID-19 of €2m in Q120, from under-utilisation within Production Services.

Grounds laid for rights issue

Management reported net debt at end March of €1.6bn (vs €1.2bn at FY19). The group's H1 typically sees a cash outflow, with cash generation in H2. Preparations for the intended €300m rights issue are in place, with the reverse 27:1 share split now effective. Precise timing is subject to appropriate market conditions. A successful capital raise will trigger an 18-month extension on both the existing RCF (which tapers from €250m through CY20 to €202.5m from December 2021) and the $125m facility from Wells Fargo. The rights issue as envisaged should reinforce the balance sheet and allow for investment to be made to drive improving profitability.

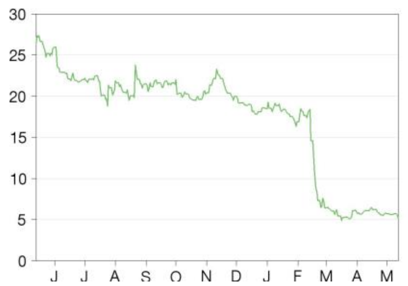
Valuation: Reflecting stock and market uncertainty

Technicolor's share price has fallen by c 70% year-to-date and at the current price, the group is trading at a historical EV/sales multiple of 0.4x, with the value of the equity dwarfed by the scale of the net debt. At current levels, the proposed refinancing would result in significant dilution.

13 May 2020

Price	**€5.08**
Market cap	**€78m**
	$1.08/€
Net debt (€bn) at 31 March 2020	1.6
Shares in issue	15.45m
Free float	100%
Code	TCH
Primary exchange	Euronext
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(16.0)	(72.0)	(81.2)
Rel (local)	(15.7)	(62.0)	(77.6)
52-week high/low		€28.08	€4.86

Business description

Technicolor is a worldwide technology leader operating in the media and entertainment industry. Its activities fall in three business segments, Production Services, DVD Services and Connected Home.

Next events

H1 results	July 2020

Analyst

Fiona Orford-Williams +44 (0)20 3077 5739

media@edisongroup.com

Edison profile page

Technicolour is a research client of Edison Investment Research Limited

Q1 renders no surprises

The group's summary results for Q120 are shown below and are broadly as we anticipated, although we do not publish quarter or half-year forecasts. Changes at constant currency, as shown in the table below, are more pronounced than expressed at current rate. While the group operates in a large number of currencies, the most important rate is that of US$:€. In Q119, this averaged at 0.88. For Q120, the equivalent rate was 0.91, a 3% difference. Management reports that the effect of COVID-19 only really affected the figures from March onwards. These numbers also do not yet reflect the benefit from the cost savings, outlined in our earlier notes (April update, February flash), although 70% of the planned headcount reduction had been achieved by the end of the quarter.

Exhibit 1: Summary Q120 results

€m	Production Services	Change y-o-y	DVD Services	Change y-o-y	Connected Home	Change y-o-y	Corporate & Other	Change y-o-y	Group	Change y-o-y
Revenue	176	-14.8%	160	-16.5%	393	-13.9%	9	+125%	739	-14.1%
Adjusted EBITDA	11	-64.1%	1	-89.8%	16	+433%	(1)	+89.0%	27	-17.3%
Margin	6.2%		0.6%		4.1%		(11.0%)		3.6%	
Adjusted EBITA	(15)	N/A	(16)	N/A	(1)	N/A	(2)	N/A	(34)	+19.3%
Margin	(8.4%)		(10.0%)		(0.2%)		(22.8%)		(4.6%)	

Source: Company accounts. Note: Changes at constant currency.

At the time of the Capital Markets Day in February, €150m of targeted savings across the group were identified with a run-rate of €100m by the end of FY20. A further €75m is now targeted over a three-year horizon, which is likely to be mostly through lease and property savings. There is a freeze on non-critical spending and the chair and CEO have both taken a 25% reduction on their fixed compensation.

Connected Home: Trading and outlook

Although Connected Home revenues were down 14%, this represented a mix by geography and by product. North American Broadband revenues were up by 16%, with good demand from major customers such as Charter, Cox, Rogers and Shaw. Comcast demand was more even between Broadband and Video. Overall North American revenues (of which a significant majority represents the Broadband offering) were up 10.6%, constrained by a deterioration in the US$:€ exchange rate. In territories where lockdown conditions have been more rigorous, management indicated that access had been more difficult, partly explaining the divergence of performance between North America and other territories. In Europe, the Middle East and Africa, where Video constitutes a larger part of the mix, revenues were down by 43%. Video revenues were down by 16.5%, but there are opportunities to enhance the quality of earnings here. After a long burn, Android TV (which may be rebranded as Google TV) is gaining traction in the market and Technicolor has been developing product that incorporates targeted adtech into the set-top box, opening up new potential revenue streams for network service providers. In Latin America, particularly in Brazil, currency devaluation and the deterioration in macro-economic conditions have made for a more difficult trading environment.

COVID-19 has highlighted the importance of reliable broadband connections and high-quality wi-fi in the home as domestic premises increasingly act as devolved workplaces, as well as needing to meet the requirements of greater content consumption. This is unlikely to change as the global economy reopens.

The strategy of focusing on fewer (large) customers with more platform-based product looks sensible, given the thin margins available.

DVD Services: Trading and outlook

DVD combined replicated volumes were down 22% on Q119, translating to a 16.5% fall in reported revenues at constant currency, representing a fall of €28m. However, the financial metrics of the business are already starting to improve after the cost savings already implemented and with the first benefits from renegotiated studio contracts. The reduction in adjusted EBITDA was €7m, with lower depreciation and amortisation making the reduction at adjusted EBITA level €3m. There was no new news on further contract renegotiations or extensions with the major studios at this juncture.

Many major new releases from the studios have been pushed back to H220, or even FY21, with a minority being released directly through to video on demand. Technicolor has been experiencing strong demand for back catalogue sales, with the retailers bolstering sales efforts. The group has also been using underused warehousing and logistical capacity to assist with distributing supplies to address the COVID-19 pandemic. Management has highlighted that, with major production facilities in Memphis and in Guadalajara in Mexico, it is possible that plants could be forced to close temporarily.

Production Services: Trading and outlook

Again, the situation is not uniform across the segment. As discussed above, the Film & Episodic business is largely at the mercy of the studios production and release schedules. A major studio client had a hiatus post corporate and internal changes in FY19 – part of the reason for increasing the emphasis on VFX for episodic productions outlined back in February. With COVID-19 having effectively halted all live action filming, the pipeline for this business and for Post Production has mostly evaporated. The group has reacted by initiating staffing reductions and staff furloughs (where schemes are available) among the creative teams, but aware of the need to retain access to the talent that it will need when production eventually restarts. The studios are obviously anxious to resume as soon as possible, but there will inevitably be a considerable time lag between the lights going back on film stages and TV studios and work coming through to Technicolor.

Other areas of the business segment are also mixed. Advertising had been performing well with a benign economy and ever-increasing creativity. With the onset and spread of the pandemic, campaigns have been pulled, delayed or pared back. The outlook depends on a recovery in economic conditions and consumer confidence. Animation and Games, on the other hand, had ‘strong double-digit’ growth in Q119. These areas are benefiting from the thirst for new content and the fact that production can be done from home provided the relevant individuals have the appropriate equipment.

Exhibit 2: Financial summary

€'m	2017	2018	2019
Year end 31 December	IFRS	IFRS	IFRS
INCOME STATEMENT			
Revenue	4,253	3,988	3,800
Cost of Sales	(3,651)	(3,521)	(3,375)
Gross Profit	602	467	425
EBITDA	345	266	301
Operating Profit (before amort. and except.)	142	58	(12)
Amortisation of acquired intangibles	(9)	(81)	(54)
Exceptionals	(54)	(127)	(55)
Reported operating profit	40	(119)	(121)
Net Interest	(96)	(51)	(84)
Joint ventures & associates (post tax)	1	0	(1)
Exceptionals	0	0	0
Profit Before Tax (norm)	47	7	(97)
Profit Before Tax (reported)	(55)	(170)	(206)
Reported tax	(112)	(54)	(3)
Profit After Tax (norm)	(65)	(47)	(99)
Profit After Tax (reported)	(167)	(224)	(208)
Minority interests	0	(1)	0
Discontinued operations	(5)	157	(22)
Net income (normalised)	(65)	(48)	(99)
Net income (reported)	(172)	(68)	(230)
Average Number of Shares Outstanding (m)	15.3	15.3	15.4
EPS - normalised (c)	(4.3)	(3.2)	(6.5)
EPS - normalised fully diluted (c)	(4.3)	(3.2)	(6.5)
Dividend per share (c)	1.6	0.00	0.00
Revenue growth (%)		(6)	(5)
Gross Margin (%)	14.2	11.7	11.2
EBITDA Margin (%)	8.1	6.7	7.9
Normalised Operating Margin (%)	3.3	1.5	(.3)
BALANCE SHEET			
Fixed Assets	2,161	2,101	2,082
Intangible Assets	1,567	1,591	1,483
Tangible Assets	243	233	476
Investments & other	38	26	40
Deferred tax and other	313	251	84
Current Assets	1,551	1,659	1,126
Stocks	238	268	243
Debtors	684	677	507
Cash & cash equivalents	319	291	64
Other	310	423	312
Current Liabilities	(1,669)	(1,909)	(1,542)
Creditors	(947)	(1,135)	(825)
Tax and social security	(33)	(34)	(41)
Short term borrowings	(20)	(20)	(95)
Other	(669)	(720)	(581)
Long Term Liabilities	(1,514)	(1,385)	(1,604)
Long term borrowings	(1,077)	(1,004)	(1,203)
Deferred tax	(193)	(193)	(27)
Other long term liabilities	(437)	(381)	(401)
Net Assets	529	466	62
Minority interests	3	1	0
Shareholders' equity	532	467	62
CASH FLOW			
Net profit	(167)	(224)	(208)
Depreciation and amortisation	240	234	322
Working capital	71	2	(69)
Tax and interest	(57)	(53)	(76)
Exceptional & other	168	159	101
Net operating cash flow	255	118	70
Capex	(145)	(113)	(169)
Acquisitions/disposals	(25)	1	(2)
Equity financing	1	0	1
Dividends	(25)	0	0
Other	(13)	28	3
Net Cash Flow	48	34	(97)
Opening net debt/(cash)	679	778	733
FX	(39)	1	
Discontinued	(88)	105	0
Other non-cash movements	(20)	(95)	(404)
Closing net debt/(cash)	778	733	1,234

Source: Company data, Edison Investment Research

General disclaimer and copyright

This report has been commissioned by Technicolour and prepared and issued by Edison, in consideration of a fee payable by Technicolour. Edison Investment Research standard fees are £49,500 pa for the production and broad dissemination of a detailed note (Outlook) following by regular (typically quarterly) update notes. Fees are paid upfront in cash without recourse. Edison may seek additional fees for the provision of roadshows and related IR services for the client but does not get remunerated for any investment banking services. We never take payment in stock, options or warrants for any of our services.

Accuracy of content: All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable, however we do not guarantee the accuracy or completeness of this report and have not sought for this information to be independently verified. Opinions contained in this report represent those of the research department of Edison at the time of publication. Forward-looking information or statements in this report contain information that is based on assumptions, forecasts of future results, estimates of amounts not yet determinable, and therefore involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of their subject matter to be materially different from current expectations.

Exclusion of Liability: To the fullest extent allowed by law, Edison shall not be liable for any direct, indirect or consequential losses, loss of profits, damages, costs or expenses incurred or suffered by you arising out or in connection with the access to, use of or reliance on any information contained on this note.

No personalised advice: The information that we provide should not be construed in any manner whatsoever as, personalised advice. Also, the information provided by us should not be construed by any subscriber or prospective subscriber as Edison's solicitation to effect, or attempt to effect, any transaction in a security. The securities described in the report may not be eligible for sale in all jurisdictions or to certain categories of investors.

Investment in securities mentioned: Edison has a restrictive policy relating to personal dealing and conflicts of interest. Edison Group does not conduct any investment business and, accordingly, does not itself hold any positions in the securities mentioned in this report. However, the respective directors, officers, employees and contractors of Edison may have a position in any or related securities mentioned in this report, subject to Edison's policies on personal dealing and conflicts of interest.

Australia

Edison Investment Research Pty Ltd (Edison AU) is the Australian subsidiary of Edison. Edison AU is a Corporate Authorised Representative (1252501) of Crown Wealth Group Pty Ltd who holds an Australian Financial Services Licence (Number: 494274). This research is issued in Australia by Edison AU and any access to it, is intended only for "wholesale clients" within the meaning of the Corporations Act 2001 of Australia. Any advice given by Edison AU is general advice only and does not take into account your personal circumstances, needs or objectives. You should, before acting on this advice, consider the appropriateness of the advice, having regard to your objectives, financial situation and needs. If our advice relates to the acquisition, or possible acquisition, of a particular financial product you should read any relevant Product Disclosure Statement or like instrument.

New Zealand

The research in this document is intended for New Zealand resident professional financial advisers or brokers (for use in their roles as financial advisers or brokers) and habitual investors who are "wholesale clients" for the purpose of the Financial Advisers Act 2008 (FAA) (as described in sections 5(c) (1)(a), (b) and (c) of the FAA). This is not a solicitation or inducement to buy, sell, subscribe, or underwrite any securities mentioned or in the topic of this document. For the purpose of the FAA, the content of this report is of a general nature, is intended as a source of general information only and is not intended to constitute a recommendation or opinion in relation to acquiring or disposing (including refraining from acquiring or disposing) of securities. The distribution of this document is not a "personalised service" and, to the extent that it contains any financial advice, is intended only as a "class service" provided by Edison within the meaning of the FAA (i.e. without taking into account the particular financial situation or goals of any person). As such, it should not be relied upon in making an investment decision.

United Kingdom

This document is prepared and provided by Edison for information purposes only and should not be construed as an offer or solicitation for investment in any securities mentioned or in the topic of this document. A marketing communication under FCA Rules, this document has not been prepared in accordance with the legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research.

This Communication is being distributed in the United Kingdom and is directed only at (i) persons having professional experience in matters relating to investments, i.e. investment professionals within the meaning of Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, as amended (the "FPO") (ii) high net-worth companies, unincorporated associations or other bodies within the meaning of Article 49 of the FPO and (iii) persons to whom it is otherwise lawful to distribute it. The investment or investment activity to which this document relates is available only to such persons. It is not intended that this document be distributed or passed on, directly or indirectly, to any other class of persons and in any event and under no circumstances should persons of any other description rely on or act upon the contents of this document.

This Communication is being supplied to you solely for your information and may not be reproduced by, further distributed to or published in whole or in part by, any other person.

United States

Edison relies upon the "publishers' exclusion" from the definition of investment adviser under Section 202(a)(11) of the Investment Advisers Act of 1940 and corresponding state securities laws. This report is a bona fide publication of general and regular circulation offering impersonal investment-related advice, not tailored to a specific investment portfolio or the needs of current and/or prospective subscribers. As such, Edison does not offer or provide personal advice and the research provided is for informational purposes only. No mention of a particular security in this report constitutes a recommendation to buy, sell or hold that or any security, or that any particular security, portfolio of securities, transaction or investment strategy is suitable for any specific person.

Frankfurt +49 (0)69 78 8076 960
Schumannstrasse 34b
60325 Frankfurt
Germany

London +44 (0)20 3077 5700
280 High Holborn
London, WC1V 7EE
United Kingdom

New York +1 646 653 7026
1,185 Avenue of the Americas
3rd Floor, New York, NY 10036
United States of America

Sydney +61 (0)2 8249 8342
Level 4, Office 1205
95 Pitt Street, Sydney
NSW 2000, Australia