FIRST BERLIN
Equity Research

BKN INTERNATIONAL AG

GERMANY / MEDIA & ENTERTAINMENT

Primary Exchange: Frankfurt General Standard
Secondary Exchange: London
Symbol: BKQ ISIN: DE0005290704

RATING: Buy	
PRICE TARGET: €4.80	
RISK RATING: High	

REACTION TO CONVERTIBLE BOND ANNOUNCEMENT

COMPANY PROFILE

BKN and its subsidiaries are enganged in the production, distribution and marketing of children's animation television programs and the merchandising and licensing of the rights of those programs. The parent company is located in Cologne, Germany, with headquarters, BKN Media Ltd. in London.

KEY POINTS

BKN announced the placing of a €3.2m convertible bond yesterday. The bond, which was placed with a US investor group, carries a US Prime +2% coupon and will be repayable in December 2010. The bond can be converted any time at a strike price of €3.20 and will be followed by a cash bond with warrants in the beginning of 2007.

According to management, BKN will use the additional funding to finance its ‘Classic Collection’ range of DVD releases, which it says will cost around €5m to produce and distribute. BKN has not licensed these titles to its distributors, but rather will pay them distribution fees and bear the replication and marketing costs itself. In return for this outlay, BKN retains all sales rights and expects to earn a margin of approximately 40%. The first title is now *A Christmas Carol*, scheduled for release in November, which represents a two-month delay to the original launch schedule. In addition, further cash from the bond will go towards ramping up the production of major new property *Zorro-Generation Z*, with delivery expected by the end of 2007.

RECOMMENDATION

BKN will present the largest raft of products in its history at this year’s MipCom, with 1,636 minutes or 27 hours of new programming on offer. Aside from DVD distribution, the additional funding will be used to speed up production in FY07 and onwards. While we do not expect a boost to top-line before FY08, the interest expenses on the bond should reach an additional €0.35m considering the current US prime rate of 8.25%. We thus revise our expected EPS (basic) for FY07 to €0.26 from €0.28. In addition, the current placement increases diluted earnings per share by 1.0m shares to 19.14m shares reducing FY06 diluted EPS from €0.18 to €0.17 and from €0.24 to €0.21 for FY07 respectively.

Based on the strong operative fundamentals of the company we continue to believe there is excellent value in the stock at present levels. Due to a slight reduction in average multiples of comparable companies currently trading at 28.2x FY06 median expected earnings (FY07: 14.1x) and based on reduced FY07 EPS (basic), we slightly reduce our price target to €4.80. We maintain our Buy recommendation and High risk rating.

RISKS

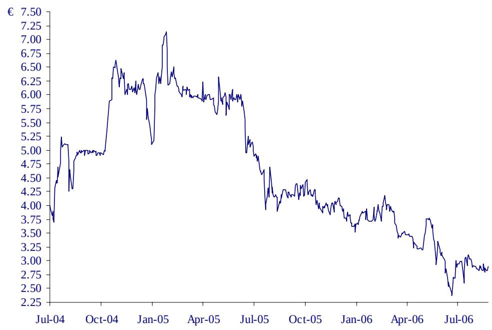
Risks to our price target include delays of animated series development, decrease in TV programming spending, delays in client acquisitions, non-renewals of existing contracts and changing consumer interests.

IMPORTANT DISCLOSURES ARE AT THE BACK OF THIS REPORT

TRADING DATA

Market Capitalisation (23.08.06)	€45.58m
Shares Outstanding	15.72m
Closing Price (23.08.06)	€2.90
52-Week Range	€2.37 / 4.47
Free Float (According to Company)	63%
Average Daily Share Volume (year)	24,466

STOCK OVERVIEW



Source: Bloomberg & First Berlin

FINANCIAL HISTORY & PROJECTIONS

	2004A	2005A	2006E	2007E
Revenue €m	8.29	11.97	15.08	18.85
Yr/Yr Growth	84.6%	44.4%	26.0%	25.0%
Operating Profit €m	1.85	3.20	4.08	5.48
Operating margin	22.3%	26.7%	27.1%	29.1%
Net income €m	1.69	2.97	3.23	4.08
EPS € (basic)	0.13	0.19	0.21	0.26

COMPANY DATA (as of 31 March 2006 unless noted)

Liquid Assets	€2.47m
Current Assets	€4.28m
Intangible Assets	€29.47m
Total Assets	€36.20m
Current Liabilities	€0.96m
Total Shareholders’ Equity	€25.52m

ANALYST INFORMATION

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FIRST BERLIN RECOMMENDATION & PRICE TARGET HISTORY

Report No.:	Date of Publication	Previous Day Closing Price	Recommen-dation	Target Price	Interim High	% Change to High
Initial Report	3 February 2006	€1.87	Strong Buy	€2.75	-	-
2...5	↓	↓	↓	↓	↓	↓
6	27 May 2005	€5.94	Buy	€6.70	€6.01	1.2%
7	21 November 2005	€4.05	Buy	U.R.	€4.18	3.2%
8	26 April 2006	€3.23	Buy	€5.50	€3.77	16.7%
9	Today	€2.90	Buy	€4.80	-	-

Source: Bloomberg & First Berlin

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First Berlin's investment rating system includes an investment recommendation and a risk rating. Our recommendations, which are a function of our expectation of total return (forecast price appreciation and dividend yield) in the year specified, are as follows:

BUY: Expected return greater than 15%
HOLD: Expected return between 0% and 15%
SELL: Expected negative return

Our risk ratings are Low, Medium, High and Speculative and are determined by ten factors: corporate governance, quality of earnings, management strength, balance sheet and financing risk, competitive position, standard of financial disclosure, regulatory and political uncertainty, company size, free float and other company specific risks. These risk factors are incorporated into our valuation models and are therefore reflected in our price targets. Our models are available upon request to First Berlin clients.

Up until 30 June 2005, First Berlin's investment rating system was five tiered and was a function of our expectation of return (forecast price appreciation and dividend yield) over the specified year. Our investment ratings were as follows: STRONG BUY: expected return greater than 20%, BUY: expected return greater than 10%, HOLD: fairly valued, REDUCE: expected return between -10% and 0%, SELL: expected return to depreciate by more than 15%. In addition, we had a SPECULATIVE BUY recommendation for stocks which we projected had the potential to give a return of 50% or more but which we also expected to be exceptionally volatile (movement up or down of 50% or more). Our risk ratings were Low, Medium, High and Speculative and were a reflection of expected price volatility, the strength of the balance sheet and the predictability of earnings.

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