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Your Personal Investment Guide

IPO Analysis

Pyramid Saimira Theatre Rs 88 - 100

13th Dec 2006

High Risk – High Returns

Subscribe

Issue Details	
Offer Price band	Rs 88-100
Face Value	Rs 10
Issue Size	Rs 84.44 crores
Type	Equity
Listing (Stock Exchange)	NSE & BSE
Offer Open Date	11th Dec06
Offer Close Date	18th Dec06

Website: www.pstl.in

Scrip Estimates (at Max. Offer Price)	
Market Cap (Rs crores)	283
P/E (x) - FY07e (fully diluted)	29
Market Cap/Sales (x) FY07e	2.7

	Pre Offer	Expected Post Offer
Promoters	27.3	19.2
Mr Nirmal Kotecha	41.9	29.4
Other Pre-Issue Investors	30.8	21.6
Shares allotted on Public issue	-	29.9
Total	100.0	100.0

Financials (Rs crores)	FY05	FY06	6M FY07
Revenues	2.9	5.0	52.5
Operating Profit	0.0	1.4	5.6
PBT	0.0	1.4	5.5
PAT	0.0	1.7	4.9
Equity	4.8	16.2	19.8
Pre-issue EPS (Rs)	0.0	1.05	4.94

Investors should read the risk factors and more detailed information in the Prospectus and the Application form before investing in the issue.

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Asset Light Business Model

The exhibition business model of Pyramid Saimira Theatre Ltd (PSTL) hinges on acquiring theatres on long-term leases, improving their infrastructure to modern standards, thereby offering high-quality viewing experience. PSTL's business model is 'Asset Light', as it does not invest in acquiring properties for exhibiting films; rather, it identifies existing properties with revenue potential across categories, i.e. standalone Theatres, Malls, Multiplexes and Cineplexes, and acquires control on long-term lease, the duration of which is around 5-15 years. Thus, the outflow for the Company is only the lease.

Riding on Technology

The Company has evolved a composite satellite-distribution mechanism to replace the existing film-based mechanism. Digital distribution increases the number of simultaneous exhibition points, which is specifically important, considering the low shelf-life of films, as a carpet release of new films is possible, especially taking into account the paucity of film prints, thus optimising the revenue potential of a film. This saves Rs 60,000-70,000 per movie per theatre, amounting to approximately Rs 20 lakhs per theatre per annum.

Huge Business Expansion Plans

PSTL commenced its exhibition business in Nov05 and, since then, has expanded at a rapid pace. It currently has 148 screens, with 90,906 seats under management, in the states of Tamil Nadu,, Andhra Pradesh and Karnataka . It plans to expand it's footprints in other regions of the country and for this, has tied up for multiplex operations in approximately102 malls in the states of Punjab, Haryana, Rajasthan and Himachal Pradesh. It has set a mega plan to increase its operations to 2,000 in more than 1,000 locations, by 2010.

High Execution Risk

PSTL plans to grow its exhibition business by more than 13x, in the next 4.5 years. This would produce significant demand on the management team and other resources, specifically considering its short experience in the business. Getting and retaining skilled employees at the managerial and operational level across different regions, on a huge scale, seems to be a risk, specially considering the fact that PSTL plans to add two screens per day, going forward; better financial strength of the competitors may lead to attrition problems for the Company.

Valuations

Although, on FY07e(H1 annualised) Post Issue EPS of Rs 3.46 and corresponding P/E multiple of 29x on the upper end of Rs 100 of the price band, the stock seems expensive, this number is misleading, considering the growth that the Company promises. Thus, the IPO qualifies as 'High Risk - High Return', considering the growth prospects and corresponding risks. We recommend investors, with a moderate to high-risk appetite and medium-term holding period, to subscribe to the issue, at the upper end of the price band of Rs 100.

Company Background

Pyramid Saimira Theatres (PSTL) was originally incorporated as 'Pyramid Films International Pvt. Ltd', for production of Tamil feature films, in 1997. The Company produced 10 films under its erstwhile brand; however, in Aug04, it strategically shifted business focus to Film Distribution and Exhibition, by discontinuing film production. PSTL now focuses on building a "Mega Digital Theatre Chain" by gaining presence in all categories of theatres, including Mall, Multiplexes, Cine-plexes and standalone Theatres. It has been acquiring theatres on long-term leases and improving their infrastructure to bring it on-par with modern standards, to offer high-quality viewing experience.

Business Model

PSTL's business consists of:
-Distribution and Exhibition of films
-Management of Malls, Multiplexes and Theatres

The Company's exhibition business model hinges on acquiring theatres on long-term leases, improving their infrastructure to modern standards, thereby offering high-quality viewing experience. PSTL's business model is 'Asset Light', as it does not invest in acquiring properties for exhibiting films; rather, it identifies existing properties with revenue potential across categories, i.e. standalone Theatres, Malls, Multiplexes and Cine-plexes, and acquires control on long-term lease, the duration of which is around 5-15 years. Thus, the outflow for the Company is only the lease rental that averages to ~Rs 75,000 per month per single-screen cinema and for multiplexes, it is approximately Rs 32 per sq ft. PSTL banks on the Digital Cinema Technology for growth. It converts films into digital formats and transmits them using satellites, to various theatres in the chain across India. This saves Rs 60,000-70,000 per movie per theatre, amounting to approximately Rs 20 lakhs per theatre per annum. The Company is the first mover in digitalisation of films for exhibition; it added the first theatre in its chain in Sep05. Currently, it has 148 screens, with 90,906 seats under management, in the states of Tamil Nadu, Andhra Pradesh and Karnataka and has a mega plan to increase it to 2,000 in more than 1,000 locations, by 2010.

Management

Mr V. Natarajan - Chairman. Age 62, has 4 decades of experience in film/ content production and is a member of various film trade bodies.
Mr P.S. Saminathan - MD. Age 39, is a CWA by qualification. Throughout his career, he has been a finance head, has experience in construction, engineering, aquacultures, and consumer durables industries and is active in the field of convergence, with experience in Cable and Television, communications and networking.
Mr N. Narayanan - Director. Age 58, is an MBA by qualification and has wide exposure in leadership and man-management.

Tie Ups

- To expand in the other regions of the country, besides its strong presence in the South, PSTL entered into an agreement with Spirit Global Constructions Pvt. Ltd in July06, whereby, Spirit would construct 60 malls with multiplexes, in the states of Punjab and Himachal Pradesh, in locations approved by PSTL. PSTL would take-over the entire mall, including the screens, retail space, food courts and entertainment areas, on a 10-year lease, renewable upto a period of 25 years. PSTL would pay a fixed lease per month and would manage the entire operations of all the 60 malls. A similar agreement is entered into with Swatantra Land and Finance Ltd (SLFL), for 22 malls in Haryana and 20 malls in Rajasthan. Thus, in all, PSTL has tied up for 102 malls in North India. However, it does not plan entry in Western India, due to high property prices, leading to high lease rentals for the Company and concentration of other big players in this region.
- PSTL has an agreement with Valuable Media Pvt. Ltd, for supply of comprehensive digital cinema equipment and solutions, on a pay-per-use basis, for 1,000 theatres.
- On the content procurement side, PSTL has tie-ups with 12 top-notch production houses in the Tamil Film community.

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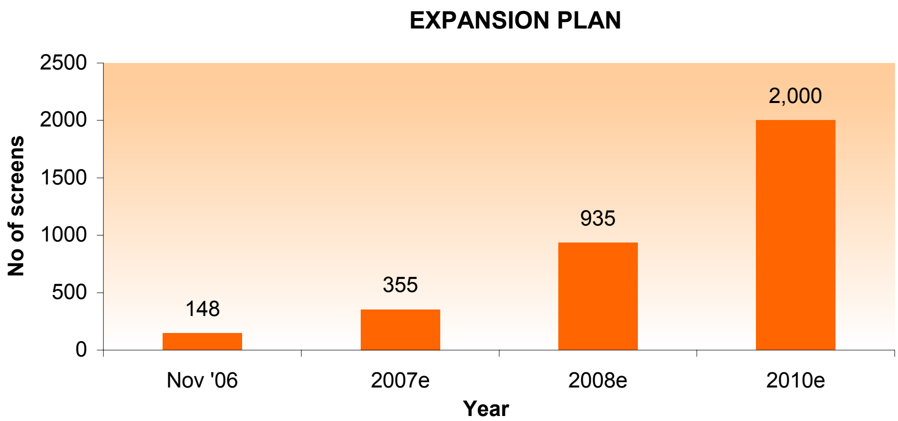
Objects of the issue

Particulars	Rs crores
Renovation & Upgradation of Theatres & Other Footfall Rights	36.8
Plant & Machinery &Installation cost for digitalisation of Theatres	24.1
Plant & Machinery and other cost for Central Network Operating Centre	3.0
Recoverable Security Deposit with Theatres & Multiplexes	20.3
Recoverable Security Deposit with Valuable Media Pvt. Ltd	7.1
Preliminary Expenses	1.5
Brand Building	4.0
Working Capital	7.8
Cost relating to Public Issue	5.0
Contingencies	1.5
Total	**111.2**

To be Financed By	
Public Issue Proceeds	84.4
Pre-issue capital and internal accruals	26.8
Total	**111.2**

Expansion Plans:



Technology

PSTL has evolved a composite satellite distribution mechanism to replace the existing film-based mechanism. Here, the production can be in the existing film-based method itself (Film negative). This negative would be converted into a digital form and the digital copy would be encrypted using the highest encryption mode available, to prevent tampering copyright violation and piracy. This encrypted file would be sent via satellite, which would be received at the theatres and stored in the respective servers at the theatres. Upon authorisation from the central control room, the server would play the movie using a Digital projector. Though live broadcast is also possible, PSTL is using the store and forward method, for content distribution. In this process, a simultaneous release of 12 new films is possible at any number of locations.

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Advantages of Digital Cinema

- Digital distribution increases the number of simultaneous exhibition points, which is specifically important, considering the low shelf-life of films, as a carpet release of new films is possible, especially taking into account paucity of film prints, thus optimising the revenue potential of a film.
- High-quality viewing experience.
- Savings of approximately Rs 60,000-Rs 70,000 per movie per theatre, which, in totality, accounts for Rs 20 lakhs per theatre per annum.
- Threat of Piracy could be reduced, as the media could be highly encrypted and supply-side problems are reduced, as requirement of film prints is cut substantially.
- The Digital system would extend the presentation capabilities, beyond just showing movies. Special showings of live events and other programmes open up many new entertainment venues for the theatre segment.
- Smaller Theatres become cost effective, due to low distribution costs.

Strengths

- First mover in digitalisation of theatres
- Highly knowledgeable management
- The only one to have displayed the successful commercial use of the digital technology in India

Risks and Concerns

Execution Risk

PSTL has been in the exhibition business for a very short period of time and is scaling up very fast, in terms of adding more theatres in its chain. Although it has been successful in tying up large number of properties in a short span, profitable business execution at these properties seems to be a risk because of the following reasons:

- The large-scale expansion planned by the Company would put significant demands on the management team and other resources.
- Getting and retaining skilled employees at the managerial and operational level, across different regions and on a huge scale, seems to be a risk, specially considering the fact that PSTL plans adding 2 screens per day, going forward. Better financial strength of competitors may lead to attrition problems for the Company.

Business Risk

- The Management seems to be dominated by one person, Mr Saminathan, as far as core business understanding and strategy is concerned. This poses a risk, as he may become irreplaceable.
- The Company aims to carve a unique integrated model, based on use of better technology. However, evolution of superior technology may prove fatal to the Company's business.
- PSTL has lease contracts for 5-15 years. With competition setting-in, further visibility of the business remains a concern.
- The company is going to invest Rs.36.8cr on 'Renovation & Up gradation of leased Theatres', however this amount will be written off over the lease period and will not create any asset for the company, the amount being substantial considering the topline this remains a concern,
- The exhibition industry strives basically on good content. The availability of good content and at affordable prices is a primary requisite for the business.

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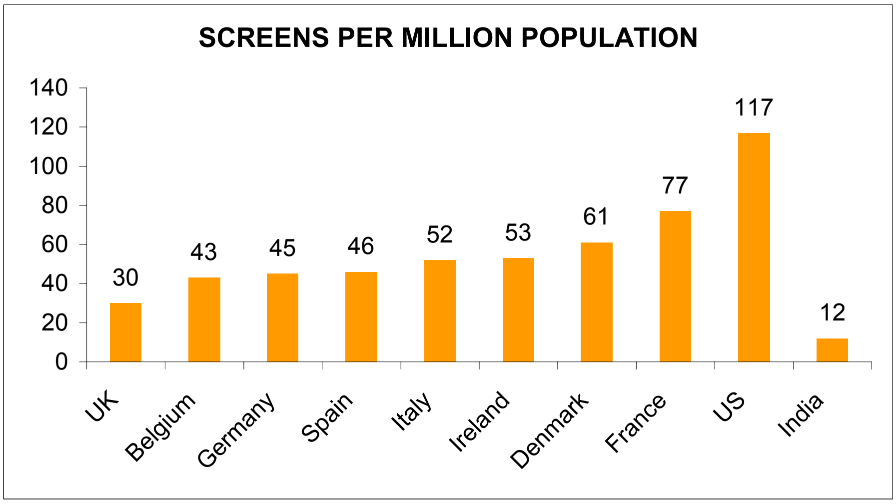
Industry Background

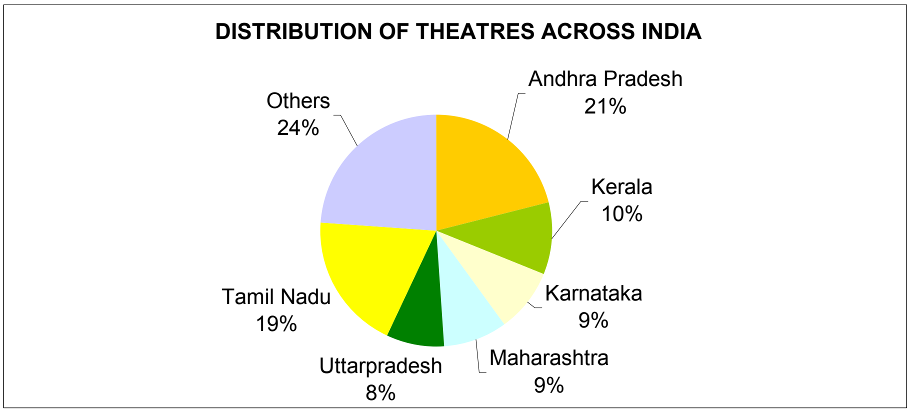
The film industry is the oldest and the most prominent and popular forms of entertainment in India and it is the largest film industry in the world, in terms of the number of films produced and admissions each year. The Indian film industry currently realises almost 70% of its total revenues from domestic and overseas box office sales. As the average Indian gets richer and his more compelling needs are met, his propensity to spend on discretionary items such as entertainment increases. Further, as his consumption of various goods and services rises, companies try to reach out to him through more marketing and advertising. Higher demand and an increased investment would result in an expansion of the entertainment industry, in the years to come. The emergence of the Indian middle-class, with greater earning power and a higher disposable income, is one of the key factors that would drive the growth of the Indian entertainment sector. Indian film industry revenues are expected to grow annually at 16% from Rs 5,900 crores, to cross the Rs 10,000 crore-mark by 2007 and reach Rs 14,300 crores in 2010. Revenue generation from releases in the domestic market is expected to grow annually at 17%, from Rs 3,400 crores in 2004 to Rs 8,600 crores in 2010.

EXHIBITION INDUSTRY

The Exhibition industry consists basically of theatres. India's screen density is very low, with around 12,900 active screens (down from 13,000 in 1990), out of which, over 95% are standalone single-screens. In contrast, China, which produces far less films than India, has 65,000 screens, while US has 36,000. There is a need for at least 20,000 screens in India, as against the current 12,900.



The Southern states of Tamil Nadu, Karnataka, Kerala and Andhra Pradesh account for 59% of the number of theatres in India, while servicing 22% of the Indian population. As a result, the rest of India is significantly under-screened, in comparison to the national average. This also reflects appetite for films in South India.



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Several positive changes have taken place in the exhibition industry over the last few years, with various state governments providing entertainment tax exemptions, for approximately 5 years, to multiplexes. The emergence of this class of exhibition properties has picked up pace in most regions of the country, making it increasingly compelling for the old single-screen theatres to improve infrastructure, to provide a competitive viewing experience at affordable prices and even so, maintain there profitability.

Financials

(YE March 31)#	FY 05	FY 06	6M FY07
Films/ Serials Produced by the company	2.9	-	-
Films/ Serial Rights distributed & Exhibited	0.0	5.0	52.5
Income from Operations	**2.9**	**5.0**	**52.5**
Cost of Pictures/ Rights - Serials & Films	2.8	1.2	28.0
Cost of Export Rights & Expenses	0.0	0.0	0.0
Expenses of Exhibition at Theatres	0.0	1.8	16.4
Selling, Dist & Administration	0.1	0.3	2.2
Deferred Revenue Expenses	0.0	0.2	0.4
Total Expenditure	**2.9**	**3.5**	**46.9**
Operating Profit	**0.0**	**1.4**	**5.6**
Other income	0.0	0.0	0.0
PBDIT	**0.0**	**1.4**	**5.6**
Interest, Depreciation & Others	0.0	0.0	0.1
PBT	**0.0**	**1.4**	**5.5**
Tax	0.0	-0.3	0.6
PAT	**0.0**	**1.7**	**4.9**
Equity	4.76	16.15	19.82
Pre Issue EPS Annualised	0.0	1.05	4.94*
PAT	**0.4%**	**34.4%**	**9.3%**
OPM	**0.8%**	**28.9%**	**10.6%**
RONW	**0.3%**	**15.6%**	**39.4%**
ROCE	**0.4%**	**12.8%**	**44.3%**

 # Numbers not comparable, as the Company's business model has changed, from production to distribution and exhibition.
***Post issue FY07e annualised EPS assuming allotment at upper band of Rs 100 is Rs 3.46**

Investment Argument

The Company is a new entrant in the exhibition business. However, it is scaling up very fast by leveraging on its first-mover advantage and sound business knowledge of running theatres on lease. While this is going to help it grow faster than its peers, it also poses risk of execution, as it would really test the Management's ability to implement its plans on such a huge scale.

Though on FY07e (H1 annualised) Post Issue EPS of Rs 3.46 and corresponding P/E multiple of 29x on the upper end of Rs 100 of the price band, the stock seems expensive. But this number is misleading, considering the growth that the Company promises. Thus, the IPO qualifies as 'High Risk - High Return' and we recommend investors with a moderate to high-risk appetite and medium-term holding period, to subscribe to the issue at the upper end of the price band of Rs 100.

WAY2WEALTH Research

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