INDIA

CENTRUM

May 06, 2008

FY08 Result Update/Con Call

Prime Focus

Buy

Marginally below expectations but future intact

CMP Rs 651*

Key Data	
Bloomberg Code	PRIF IN
Reuters Code	PRFO.BO
Current Shares O/S (mn)	13.0
Diluted Shares O/S(mn)	14.3
Mkt Cap (Rs bn/USD mn)	8.3/204.4
52 Wk H / L (Rs)	1549/542
Daily Vol. (3M NSE Avg.)	16,416
Face Value (Rs)	10
1 USD = Rs 40.7	

*Source: Bloomberg ; * As on May 5, 2008*

Price Performance (%)

	1M	6M	1Yr
Prime Focus	(3.4)	(40.2)	13.0
NIFTY	11.7	(10.3)	26.1

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Result Highlights

Prime Focus annual results were in line with our expectations except for the exceptional loss of Rs49.3 mn in VTR (UK subsidiary). The sales grew by 16% yoy to Rs2.3bn as against our expectation of Rs2.4bn. The operating profit margin was 31% during the year as against 29% in FY07. The adjusted net profit increased by 53.6% to Rs328bn (after adjusting for extra ordinary expenses of Rs49mn incurred during the Q4FY08). During Q4FY08, the sales grew by 3% to Rs 571 mn compared to last quarter as some of the movies were not booked during the quarter. EBITDA margin increased to 34.6% due to lower cost registered in VTR.

Result Analysis

The sales grew by 55.6% yoy to Rs858mn for the standalone business and VTR witnessed a tad growth to Rs1.4bn during FY08. While the EBITDA margin expanded by 155bps yoy to 30.5% on a consolidated basis, the standalone business witnessed a contraction in EBITDA margin by 441bps to 55.7% in FY08 mainly due to increase in salary costs and rent expenses. The company reported extraordinary item of Rs49.3 mn in the VTR on account of legal charges as a one time loss. The company has an outstanding derivative contract of Rs43.9mn.

Outlook & Valuations

Due to nature of the business, the company is likely to witness quarterly fluctuations in the sales due to shift in the projects to subsequent quarters. The company will be consolidating its sales for the two acquisition made during FY07 i.e. Frantic Films and Post Logics which would boost sales going forward. Considering the competition, growth outlook for domestic business and margin for US subsidiaries, we have reduced our sales estimates by 7.0% and 7.2% for FY09E and FY10E respectively and net profits by 27.6% and 25.3% for respective years. We believe that the company would focus on driving sales going forward. Due to change in estimates, we revise our target price from Rs1,289 to Rs856, implying a P/E of 16.5x FY10E earnings. We retain our Buy rating on the stock.

Table 1: Q4FY08 Results Consolidated

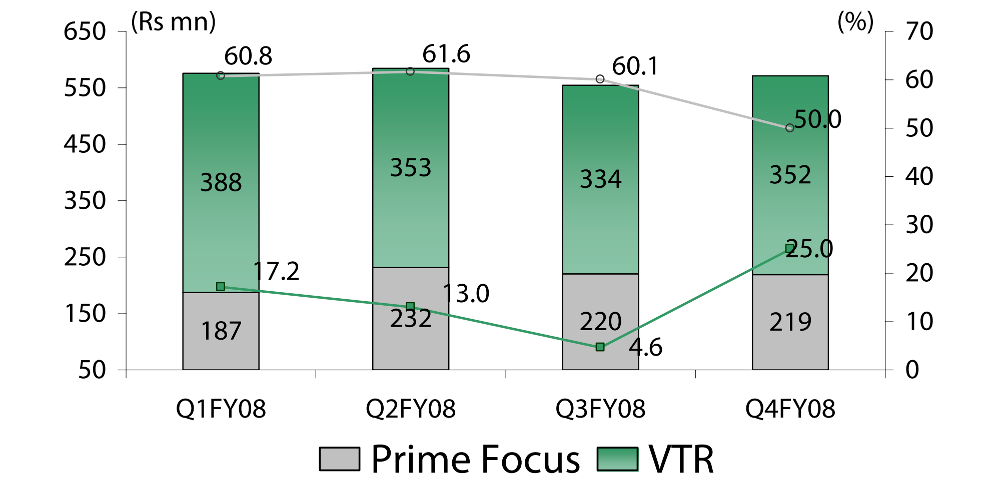
Y/E March	Q4FY07	Q3FY08	Q4FY08	QoQ (%)	YoY (%)	FY07	FY08	YoY (%)
Net sales		**555**	**571**	***3.0***		**1,955**	**2,274**	***16.3***
Operating expenditure		407	374			1,390	1581	
% of sales		*73.3*	*65.4*			*71.1*	*69.5*	
Operating profit		**148**	**198**	***33.6***		**566**	**693**	***22.5***
OPM (%)		***26.7***	***34.6***	***791 bp***		***28.9***	***30.5***	***155 bp***
Depreciation and amortisation		51	66			232	228	
Interest		26	31			63	90	
EBT		72	100	*39.6*		270	375	*39.0*
Other income		27	4			81	64	
PBT		**98**	**104**	***5.7***		**351**	**439**	***24.9***
Exceptional item (as reported)		18	49			34	49	
Provision for tax		21	15			92	83	
-effective tax rate		*18.0*	*10.0*			*23.7*	*17.0*	
PAT (reported)		59	39	*(33.7)*		225	306	*36.0*
Exceptional item (post tax)		15	44			26	41	
Less: Minority Interest						11	18	
PAT after minority interest (adjusted)		**74**	**84**	***13.0***		**214**	**328**	***53.6***
NPM (%)		***13.4***	***14.7***	***129 bp***		***10.9***	***14.4***	***350 bp***

Source: Company, Centrum Research

Improved operating performance of VTR in Q4FY08

VTR registered an improvement in sales and operating margin during Q4FY08. The sales grew 5.4% to Rs352mn. EBITDA margin stood at 25% for VTR, highest in any of the quarters. On the other hand, Prime Focus (on a standalone basis) registered flat sales during the quarter with decrease in EBITDA margin to 50% mainly due to hike in salary and higher rent payment. During the quarter, the some of the major movies for which the company booked sales include Jodha Akbar and Race. The head count of the company stands at ~800 people. Going forward, with the growth in sales, the company expects to maintain the margins in 60% range backed by growth in sales. Movies such as Love Story 2050, Krazy 4 and Tashan are expected to be booked in Q1FY09E.

Chart 1: VTR bettered the performance in Q4FY08 at operating levels



Source: Company

Conference Call Highlights

We conducted the conference call on behalf of Prime Focus for FY08 results. The key takeaways are as follows

- Domestic business is expected to grow a 30-35% rate driven by both movies and advertisements businesses.
- Some of the movies in pipeline include Tashan, Krazy 4, Bhootnath, Meerabai Not Out, Milenge Milenge, De Taali, among others.
- Equipment rental business was behind schedule during FY08 and was operational for four months. This segment is expected to add Rs140-150mn to the topline in FY09E as it would be its first full year operations.
- US acquisitions would be consolidated from Q1FY09E. The sales are expected to remain at ~US$26nm levels in the first year and subsequently witness 10% growth.
- VTR (UK subsidiary) sales were lower than the expectation mainly on account of slowdown in the economy.
- Royal Palm second phase (seating capacity of 600 employees) is expected to get operational by August-September 2008 which will be mainly used for high end visual effects work.
- On the operating margin front, the company expects the operating margin to remain in the range of 55-60% in case of domestic business mainly due to increase in salary expenses with the addition in employees for the royal palm division and general hike in salary across the company. In case of US subsidiaries, the operating margins is expected in the range of 15-20% for FY09E.

- The company would be incurring routine capex of Rs300mn for FY09E as most of the expansion is completed.

Outlook & valuation

We are revising our earning estimates considering the competitive environment in domestic market and operating profit outlook for US subsidiaries.

Table 2: Revision in estimates

		FY09E			FY10E		
		Revised	Previous	(%)	Revised	Previous	(%)
Sales	Rs mn	3,700	3,980	(7.0)	4,135	4,458	(7.2)
EBITDA	Rs mn	1,139	1,446	(21.2)	1,400	1,781	(21.4)
- Margin	*(%)*	*30.8*	*36.3*		*33.9*	*40.0*	
Net profit (adj)	Rs mn	557	769	(27.6)	744	996	(25.3)
EPS (diluted)	Rs	38.9	53.7	(27.5)	52.0	69.6	(25.3)

Source: Company, Centrum Research

The stock is trading at 28.4x its FY08 earnings after adjusting for extraordinary items. Our interaction with the management does not indicate any concerns over the sales growth. The nature of the business indicates quarterly aberrations in earnings with shift in booking of projects. In the light of strong demand environment and presence of company in key post production markets, we expect the company to post better performance going forward. Apart from growth in the existing business, the sales and earnings are expected to grow from the consolidation of Frantic Films and Post Logics from FY09E onwards. However, considering competition in the domestic market and operating margin outlook for US subsidiaries acquired from 20% earlier to 15% in FY09E, we have reduced our estimates of sales and net profits. Based on the revised estimated of EPS for FY09E and FY10E, we are revising our target price from Rs1,289 to Rs856, implying an upside of 32%. We retain our Buy rating on the stock.

Table 3: Summary Financials

Y/E March (Rs mn)	FY06*	FY07	FY08	FY09E	FY10E
Net Sales	399	1,955	2,274	3,700	4,135
-growth (%)	*27.5*	*N.M.*	*16.3*	*62.7*	*11.8*
EBITDA	243	566	693	1,139	1,400
EBITDA Margin (%)	*60.9*	*28.9*	*30.5*	*30.8*	*33.9*
Adjusted Profit after Minority Interest	140	214	327	557	744
-growth (%)	*70.3*	*N.M.*	*53.0*	*70.3*	*33.5*
NPM (%)	*35.2*	*10.9*	*14.4*	*15.1*	*18.0*
EPS	13.6	14.9	22.9	38.9	52.0
P/E (x)	*49.6*	*45.1*	*29.5*	*17.3*	*13.0*
EV/EBITDA (x)	28.4	15.7	15.9	9.0	7.0

Source: Company, Centrum Research

Key to Centrum Investment rankings:

Buy : Expected to outperform Nifty by >15%, **Accumulate :** Expected to outperform Nifty by +5 to15%, **Hold :** Expected to outperform Nifty by -5% to + 5% , **Reduce :** Expected to underperform Nifty by 5 to 15%, **Sell :** Expected to underperform Nifty by >15%

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