

## The delta effect – part 2

1<sup>st</sup> August 2007

### BUY

Price	Target
<b>Rs236</b>	<b>Rs330</b>

Sensex - 15,551

### Price Performance

(%)	1M	3M	6M	12M
Absolute	0	16	35	205
Rel. to Sensex	-5	3	24	111

Source: Bloomberg

### Stock Details

Sector	Media
Reuters	DCHL.BO
Bloomberg	DECH@IN
Equity Capital (Rs mn)	492
Face Value (Rs )	2
52 Week H/L (Rs )	248/73
Market Cap (Rs bn)	57.6
Daily Avg Vol (No of shares)	430,998
Daily Avg Turnover (US\$ mn)	2.3

### Shareholding Pattern (%)

(30th Jun.'07)

Promoters	61.1
FII/NRI	18.7
Institutions	16.8
Private Corp.	1.8
Public	1.6

Source: Capitaline

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Deccan Chronicle reported robust results for Q1FY08. The net sales for the quarter increased by 58% yoy to Rs1,734mn. The EBIDTA increased by 173% yoy to Rs1,037mn. EBIDTA margins increased by a whopping 2520bps to 59.8% as compared to 34.6% during the same quarter last year. The net profit for the quarter increased by 260% yoy to Rs837mn. While the advertisement rate hike effective from May 2007 was the major contributor to the profitability, there was also a 20% growth in the advertisement volume and a decrease in the raw material cost, which also contributed towards margin expansion. As always the company has provided for lower taxes during the first quarter (11%), which boosted the net profit growth. Following the robust results in a relatively weaker first quarter, we have revised our estimates and price target. We have revised our earnings by 11% for FY08E and FY09E. We maintain a BUY recommendation on the stock with a revised price target of Rs330.

### Robust Q1 results, seasonal effect moving away

Deccan Chronicle reported Q1FY08 results with 58% growth in the net sales to Rs1734mn. The robust growth in the revenues is driven by the advertisement rate hike taken during the last quarter coupled with a 20% increase in the volumes (advertisement space). The history suggests that the first quarter for the company has always been weaker due to higher sales in the 2<sup>nd</sup> and 3<sup>rd</sup> quarters on account of festival season. The robust results for the quarter reinstate the management stance that the seasonality in the business is reducing and would eventually move away.

### Margin expansion - the delta effect

While the sales for the quarter increased by 58% the EBIDTA for the quarter increased by 173% yoy. The EBIDTA margins for the quarter stood at a mind boggling 59.8%. The increase in the EBIDTA margins reflects the delta effect; where in the incremental revenue of the company, which is largely driven by advertisement income, directly flows through the bottom line. More over, the appreciating rupee, has led to a lower cost of production as majority of the newsprint consumed by the company is imported. The newsprint cost has reduced by ~20% over the last few quarters to Rs27,000 per ton.

### Valuations

Following the robust Q1 results, we have revised our estimates for sales by 3.3% and 7.4% and PAT by 11.1% and 11.4% for FY08 and FY09 respectively. We believe that the growth momentum in revenue and profitability would accelerate further in the following quarters especially on account of the festival season and the complete effect of ad rate hike. We expect an EPS of Rs12.3 and Rs16.5 for FY08E and FY09E respectively.

While other print media stocks with lower margins, profitability and returns are trading at a higher valuation than Deccan Chronicle, we believe that Deccan Chronicle in turn should command a premium valuation. At CMP of Rs236, the stock trades at 19x and 14x EPS for FY08E and FY09E respectively. We maintain a BUY recommendation on the stock with a price target of Rs330 based on 20x EPS of Rs16.5 for FY09E.

### Key financials (Rs mn)

	Net Sales	EBITDA (Core)	EBITDA (%)	AEPS APAT	EV/ EBITDA (Rs)	P/BV	Div Yld (%)	ROCE (%)	P/E	
YE-Mar										
FY06	3309	1017	30.7	680	3.0	55.4	15.3	0.1	12.5	79.4
FY07	5528	2583	46.7	1616	6.6	21.8	6.4	0.4	22.5	35.9
FY08E	8123	4591	56.5	3036	12.3	11.9	5.2	1.7	33.6	19.1
FY09E	10353	6149	59.4	4057	16.5	8.5	4.1	1.7	37.4	14.3

### Estimates revised

Following the robust Q1 results in a relatively weaker quarter, we have revised our estimates upwards for FY08 and FY09. Based on our revised estimates, we expect the net sale to increase by CAGR 37%, EBIDTA to increase by CAGR 54% and PAT to increase by 59% CAGR over FY07-09E. We expect the company to report EPS of Rs12.3 and Rs16.5 for FY08E and FY09E respectively.

	Old estimates		New estimates		Change	
	FY08E	FY09E	FY08E	FY09E	FY08E	FY09E
Net sales	7,866.1	9,638.0	8,123.1	10,352.6	3.3	7.4
EBIDTA	4,129.0	5,387.8	4,590.6	6,148.7	11.2	4.1
EBIDTA %	52.5	55.9	56.5	59.4	402bps	349bps
PAT	2,736.4	3,645.0	3,036.1	4,057.0	11.0	1.3
EPS	11.1	14.8	12.3	16.5	11.1	1.4

### Print media – valuation matrix

	Deccan Chronicle		HT Media		Jagran Prakashan	
	FY08	FY09	FY08	FY09	FY08	FY09
Net sales	7,624.7	9,890.6	13,006.9	15,668.5	7,497.9	9,194.4
EBIDTA	4,031.1	5,160.6	2,964.8	4,002.3	1,834.2	2,406.3
EBIDTA %	53%	52%	23%	26%	24%	26%
PAT	2,401.6	3,151.1	1,560.6	2,104.8	1,072.6	1,418.4
EPS	9.9	12.8	6.7	9.0	17.8	23.5
EV/EBIDTA	14.9	11.7	18.3	13.5	16.9	12.9
P/E	23.3	18.1	34.2	25.4	29.5	22.3
ROE	23.8	24.7	18.3	20.6	20.4	21.8

Source: Bloomberg consensus, Emkay research

Based on the Bloomberg consensus estimates, Deccan Chronicle is trading at a 20-25% discount on P/E multiple, as compared to the competitors HT Media and Jagran Prakashan. We believe that Deccan Chronicle with stronger growth, higher margins and superior shareholder returns should trade at a premium to the competition.

### Huge growth potential still exists

While Deccan Chronicle has presence in Andhra Pradesh and Chennai markets, the company plans to launch the Bangalore edition by the end of FY08. The company is also considering expanding to tier 2 cities within the state of Tamilnadu and Andhra, which would increase its geographical presence and hence the circulation. Post Bangalore launch, the company also plans to add Mangalore, Mysore, and Dharwad editions to increase the presence within the state. The company also has over Rs4bn cash on books, which it intends to utilize for inorganic growth. All these indicate a potential for the growth over the next few years.

### Odyssey – on a rapid expansion

Odyssey, the 100% subsidiary of Deccan Chronicle, has increased its presence to 27 stores. The company has set a target of 50 stores by FY08 end. The management has indicated that post March 2007, once the business achieves a scale, they would list the company separately and unlock shareholder value. However, the IPO is not likely to occur in FY08. The management has maintained the guidance for Odyssey with net sales of Rs2500mn and a PBT of Rs320mn for FY08. In our estimates, we have not factored the benefits arriving from Odyssey, however the IPO of the same would act as a trigger for the stock.

## Q1FY08 result overview

Particulars	Q107	Q108	% yoy	Q407	% qoq
Net sales	1,096.3	1,733.5	58.1	1,475.5	17.5
Employee Cost	48.3	61.6	27.5	54.7	12.6
Production Cost	600.1	569.2	-5.1	601.1	-5.3
Admin and Other Costs	68.4	65.8	-3.8	88.9	-26.0
<b>Total optng exp</b>	<b>716.8</b>	<b>696.6</b>	<b>-2.8</b>	<b>744.7</b>	<b>-6.5</b>
<b>EBIDTA</b>	<b>379.5</b>	<b>1,036.9</b>	<b>173.2</b>	<b>730.8</b>	<b>41.9</b>
Other Income	28.8	102.6	256.3	205.3	-50.0
Depreciation	39.7	71.2	79.3	47.2	50.8
<b>EBIT</b>	<b>368.6</b>	<b>1,068.3</b>	<b>189.8</b>	<b>888.9</b>	<b>20.2</b>
Interest	64.3	129.8	101.9	113.3	14.6
<b>PBT</b>	<b>304.3</b>	<b>938.5</b>	<b>208.4</b>	<b>775.6</b>	<b>21.0</b>
Tax	71.8	101.0	40.7	519.7	-80.6
<b>Net Profit</b>	<b>232.5</b>	<b>837.5</b>	<b>260.2</b>	<b>255.9</b>	<b>227.3</b>

% of sales	Q107	Q108	chg bps	Q407	chg bps
Employee Cost	4.4	3.6	(85)	3.7	(15)
Production Cost	54.7	32.8	(2,190)	40.7	(790)
Admin and Other Costs	6.2	3.8	(244)	6.0	(223)
EBIDTA	34.6	59.8	2,520	49.5	1,029
Net Profit	21.2	48.3	2,710	17.3	3,097

**Income statement**

Y/E, Mar (Rs. mn)	FY06	FY07	FY08E	FY09E
Net Sales	3,309	5,528	8,123	10,353
Growth (%)	99.7	67.1	47.0	27.4
Staff Cost	197	215	284	355
% of Sales	6.0	3.9	3.5	3.4
Production Cost	1,843	2,406	2,883	3,305
% of Sales	55.7	43.5	35.5	31.9
Admin & Other Costs	251	324	366	544
% of Sales	7.6	5.9	4.5	5.3
EBITDA	1,017	2,583	4,591	6,149
Growth (%)	73.2	153.9	77.7	33.9
EBIDTA %	30.7	46.7	56.5	59.4
<i>Other Income</i>	246	323	376	268
Interest	197	332	259	168
Depreciation	103	171	308	369
PBT	964	2,403	4,400	5,880
Tax	284	788	1,364	1,823
ETR	29.5	32.8	31.0	31.0
PAT	680	1,616	3,036	4,057
Growth (%)	112.1	137.7	87.9	33.6
<i>Net Margin (%)</i>	20.5	29.2	37.4	39.2

**Cash Flow**

Y/E, Mar (Rs. mn)	FY06	FY07	FY08E	FY09E
Profit Before Tax	964	2,403	4,400	5,880
Depreciation	103	171	308	369
Interest Expenses	47	332	259	168
(Inc)/Dec in Inventory	(206)	(206)	(284)	(386)
(Inc)/Dec in Debtors	(913)	(459)	(853)	(733)
(Inc)/Dec in loans & Adv	(42)	82	(200)	100
Inc(Dec) in Cur Liab	51	439	308	312
Less: Direct Taxes	200	529	1,100	1,646
CFO	(288)	2,233	2,837	4,063
(Pur)/Sale of Fixed Asset	(1,439)	(544)	(100)	(50)
(Pur)/Sale of Investment	(833)	0	0	0
CFI	(2,972)	(544)	(100)	(50)
Incr/(Dec) in Borrowings	3,541	(3,388)	(500)	(800)
Increase in Capital	0	4,628	0	0
Dividend Paid	(47)	(277)	(1,107)	(1,107)
Interest Paid	(47)	(332)	(259)	(168)
CFF	3,104	632	(1,866)	(2,075)
Net Inc/(Dec) in Cash	(156)	2,321	871	1,938
Opening Balance	2,213	2,056	4,377	5,248
Closing Balance	2,056	4,377	5,248	7,186

**Balance Sheet**

Y/E, Mar (Rs. mn)	FY06	FY07	FY08E	FY09E
Equity Capital	412	492	492	492
Reserves	2,766	8,653	10,581	13,531
Networth	3,178	9,145	11,074	14,023
Total Debt	5,888	2,500	2,000	1,200
Deferred Tax Liabilities	243	502	766	942
Deferred expenses	10	10	10	10
<b>Capital Employed</b>	<b>9,318</b>	<b>12,157</b>	<b>13,849</b>	<b>16,175</b>
Gross Block	3,741	4,091	4,491	4,591
Less Depreciation	239	410	718	1,087
Net Fixed Assets	3,502	3,681	3,773	3,504
CWIP	406	600	300	250
Investments	893	893	893	893
Goodwill	173	173	173	173
Inventory	400	606	890	1,276
Debtors	1,358	1,817	2,671	3,404
Cash and Bank	2,056	4,377	5,248	7,186
Loans & Advances	882	800	1,000	900
Cur Liab & Provisions	521	959	1,267	1,580
Net Current Assets	4,176	6,641	8,541	11,186
Miscellaneous exp	169	169	169	169
<b>Total Assets</b>	<b>9,318</b>	<b>12,157</b>	<b>13,849</b>	<b>16,175</b>

**Ratios**

Y/E, Mar (Rs. mn)	FY06	FY07	FY08E	FY09E
EBITDA %	30.7	46.7	56.5	59.4
EBIT%	35.1	49.5	57.4	58.4
NPM %	20.5	29.2	37.4	39.2
ROCE (%)	12.5	22.5	33.6	37.4
Adj. ROE (%)	21.4	17.7	27.4	28.9
Adj. EPS	3.0	6.6	12.3	16.5
Cash EPS	3.4	7.3	13.6	18.0
Book Value	15.4	37.2	45.0	57.0
DPS	0.2	1.0	4.0	4.0
Payout %	6.9	17.1	36.5	27.3
Debtors days	150	120	120	120
Asset Turnover	0.4	0.5	0.6	0.6
PE (x)	79.4	35.9	19.1	14.3
Cash PE	69.0	32.5	17.4	13.1
P/BV	15	6	5	4
EV/Sales	4.1	10.2	6.8	5.0
EV/EBITDA	13.3	21.8	11.9	8.5
Dividend Yield %	0.1	0.4	1.7	1.7

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