

## Company Flash

11 September 2008 | 9 pages

# Zee Entertainment (ZEE.BO)

## Buy: GEC Fragmentation in Play

- Market fragmentation in play; market expands** — The launch of new general entertainment channels (GECs) has expanded the overall space by c20% YTD; however it has also led to increased fragmentation in the category. Zee has done better than peers in protecting market share.
- Colors off to a flying start** — Viacom 18's new channel, Colors, has emerged as a strong No. 3 GEC in less than two months with its soap/reality/game shows doing well in prime time. More important, the success is driven lately by a soap (higher loyalty base) "Balika Vadhu" (3/top 10 slots for Week 36 2008).
- Incumbents lose share; Zee does reasonably well** — As expected, incumbents lost market share, although we admit, new players (read Colors) have taken more share than we anticipated. Zee has done better than peers with its share coming down by ~2.5% compared to ~6% for Star (over week 29-36). In terms of number of programs in Top 50, Zee TV has 17 in week 36 (compared with 18 in week 29, before launch of Colors) while StarPlus now has 23 (31 earlier).
- Other new channels tapered off; sustainability the key** — Viewership ratings of 9x and NDTV Imagine, launched some months ago, have not picked up. New entrants have made aggressive investments and viewership needs to pick up to sustain in the long run. For Colors, ratings sustainability remains the key.
- Our assumptions on ZEEL reasonable** — We have factored ad growth slowing to 22% for rest of FY09E (compared to 37% in Q1). ZEEL would be one of the biggest beneficiaries from pay revenue growth story – DTH rollout continues to progress very well across the country. Moreover, our estimates have an upside risk, as management plans to restrict the losses in Zee Next.

### Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2007A	2,375	5.48	6.5	40.9	3.7	10.0	0.7
2008A	3,858	8.90	62.4	25.2	3.4	14.1	0.9
2009E	4,049	9.34	4.9	24.0	3.1	13.4	0.9
2010E	5,480	12.64	35.3	17.7	2.7	16.2	1.1
2011E	6,902	15.92	25.9	14.1	2.3	17.8	1.1

Source: Powered by dataCentral

See Appendix A-1 for Analyst Certification and important disclosures.

<b>Buy/Medium Risk</b>	<b>1M</b>
Price (11 Sep 08)	Rs223.85
Target price	Rs240.00
Expected share price return	7.2%
Expected dividend yield	0.9%
<b>Expected total return</b>	<b>8.1%</b>
Market Cap	Rs97,152M
	US\$2,156M

### Price Performance (RIC: ZEE.BO, BB: Z IN)



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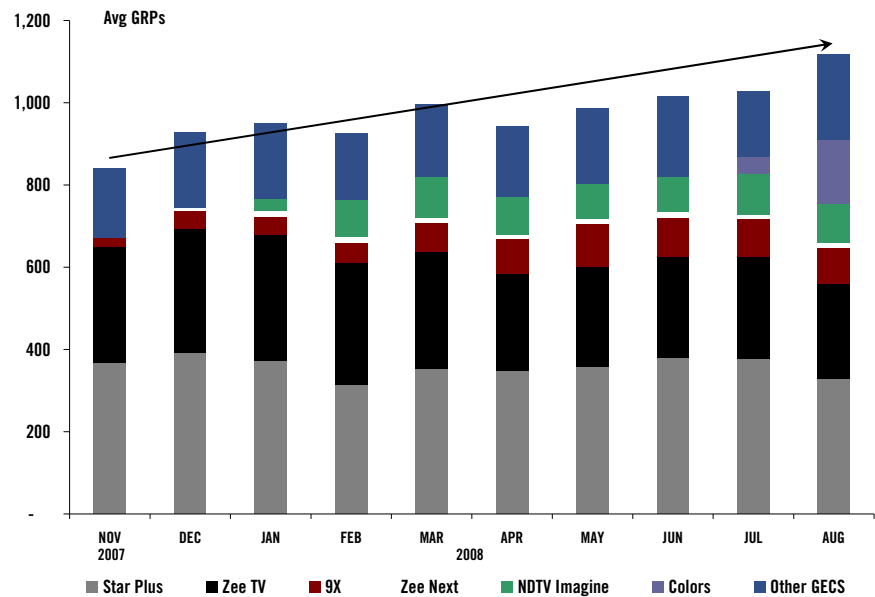
Fiscal year end 31-Mar	2007	2008	2009E	2010E	2011E
<b>Valuation Ratios</b>					
P/E adjusted (x)	40.9	25.2	24.0	17.7	14.1
EV/EBITDA adjusted (x)	30.6	18.0	15.4	12.0	9.3
P/BV (x)	3.7	3.4	3.1	2.7	2.3
Dividend yield (%)	0.7	0.9	0.9	1.1	1.1
<b>Per Share Data (Rs)</b>					
EPS adjusted	5.48	8.90	9.34	12.64	15.92
EPS reported	5.48	8.84	9.34	12.64	15.92
BVPS	60.38	65.99	72.98	82.69	95.68
DPS	1.50	2.00	2.00	2.50	2.50
<b>Profit &amp; Loss (RsM)</b>					
Net sales	15,159	18,354	22,449	26,723	31,308
Operating expenses	-12,139	-13,163	-16,421	-19,125	-21,627
<b>EBIT</b>	<b>3,019</b>	<b>5,191</b>	<b>6,028</b>	<b>7,598</b>	<b>9,681</b>
Net interest expense	-334	-516	-842	-350	-350
Non-operating/exceptionals	747	1,138	1,000	1,000	1,000
<b>Pre-tax profit</b>	<b>3,432</b>	<b>5,813</b>	<b>6,186</b>	<b>8,248</b>	<b>10,331</b>
Tax	-999	-1,627	-1,846	-2,477	-3,138
Extraord./Min.Int./Pref.div.	-58	-354	-291	-291	-291
<b>Reported net income</b>	<b>2,375</b>	<b>3,833</b>	<b>4,049</b>	<b>5,480</b>	<b>6,902</b>
Adjusted earnings	2,375	3,858	4,049	5,480	6,902
Adjusted EBITDA	3,204	5,423	6,271	7,892	10,025
<b>Growth Rates (%)</b>					
Sales	-8.4	21.1	22.3	19.0	17.2
EBIT adjusted	29.3	71.9	16.1	26.0	27.4
EBITDA adjusted	18.9	69.3	15.6	25.9	27.0
EPS adjusted	6.5	62.4	4.9	35.3	25.9
<b>Cash Flow (RsM)</b>					
<b>Operating cash flow</b>	<b>-108</b>	<b>2,674</b>	<b>5,338</b>	<b>3,631</b>	<b>4,977</b>
Depreciation/amortization	185	232	243	294	344
Net working capital	-2,798	-1,551	755	-2,434	-2,560
<b>Investing cash flow</b>	<b>-1,250</b>	<b>-1,132</b>	<b>-1,906</b>	<b>-841</b>	<b>-946</b>
Capital expenditure	-2,078	-997	-1,906	-841	-946
Acquisitions/disposals	0	0	0	0	0
<b>Financing cash flow</b>	<b>1,146</b>	<b>-792</b>	<b>-1,673</b>	<b>-1,562</b>	<b>-1,562</b>
Borrowings	-1,676	640	-366	0	0
Dividends paid	-763	-1,018	-1,017	-1,271	-1,271
<b>Change in cash</b>	<b>-212</b>	<b>750</b>	<b>1,759</b>	<b>1,228</b>	<b>2,469</b>
<b>Balance Sheet (RsM)</b>					
<b>Total assets</b>	<b>35,332</b>	<b>39,872</b>	<b>43,669</b>	<b>49,289</b>	<b>56,433</b>
Cash & cash equivalent	1,196	1,946	3,705	4,933	7,403
Accounts receivable	5,331	5,907	6,765	8,054	9,435
Net fixed assets	14,841	15,605	17,268	17,815	18,417
<b>Total liabilities</b>	<b>8,332</b>	<b>10,144</b>	<b>10,908</b>	<b>12,319</b>	<b>13,832</b>
Accounts payable	0	0	0	0	0
Total Debt	3,226	3,866	3,500	3,500	3,500
<b>Shareholders' funds</b>	<b>27,000</b>	<b>29,728</b>	<b>32,761</b>	<b>36,970</b>	<b>42,601</b>
<b>Profitability/Solvency Ratios (%)</b>					
EBITDA margin adjusted	21.1	29.5	27.9	29.5	32.0
ROE adjusted	10.0	14.1	13.4	16.2	17.8
ROIC adjusted	8.2	12.7	14.1	16.2	18.9
Net debt to equity	7.5	6.5	-0.6	-3.9	-9.2
Total debt to capital	10.7	11.5	9.7	8.6	7.6

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The entire GEC space has gone up ~20% YTD, indicating that the GEC market has expanded with the launch of new channels

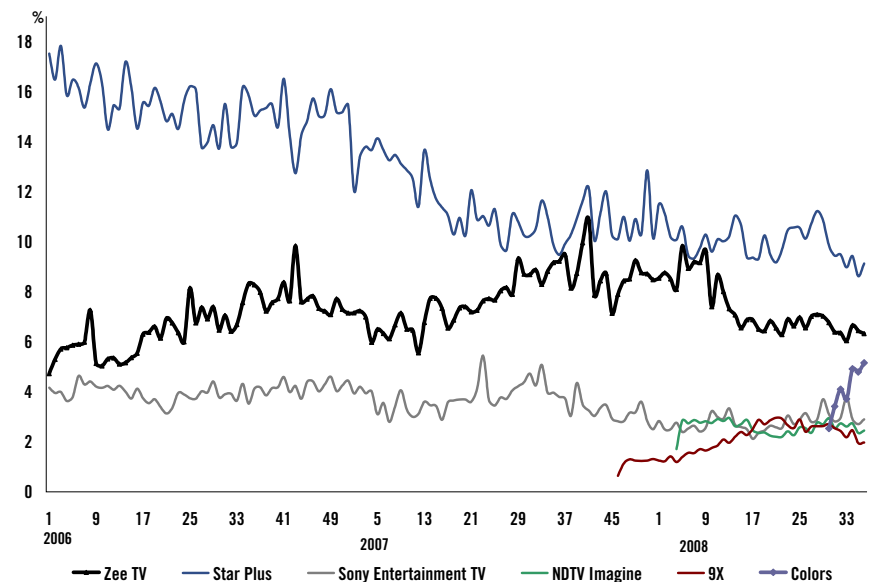
Figure 1. Increase in GEC genre size with the entry of new competition



Source: TAM Media, HSM, General Entertainment Channels, CS4+, All days, All 24 hours

Colors has been the star performer with ~5% market share (overall) in the first 7 weeks of launch. Within the incumbents, Zee has done much better – Star Plus has witnessed ~1.7% fall in market share compared to ~0.7% for Zee TV

Figure 2. Overall Channel Shares (%)



Source: TAM Media, All Channels, HSM, CS4+, All days, All 24 hours

In the latest week, Zee TV has 17 programs in Top 50 (compared to 18 in week 29, before launch of Colors), while number of programs of leader Star Plus are 23 (down from 31).

Colors has had a good beginning and currently has 8 names in Top 50.

New channels have invested huge amounts for one-off event-based shows (like reality, movie related), which might find viewership difficult to sustain. Also, new players have paid large sums as carriage fees.

Viewership needs to pick up for new channels to sustain over a longer term.

Figure 3. Top 50 Programs in General Entertainment Category

Rank	Channel	Day	Name of Programme	TVR
1	Star Plus	Thu	BIDAYI	5.54
2	Star Plus	Tue	BIDAYI	5.35
3	Star Plus	Wed	BIDAYI	5.19
4	Star Plus	Mon	BIDAYI	4.96
5	Colors	Thu	BALIKA VADHU	4.22
6	Star Plus	Tue	KIS DESH MEIN HAI MERA DIL	3.96
7	Colors	Fri	BALIKA VADHU	3.87
8	Colors	Tue	BALIKA VADHU	3.73
9	Star Plus	Thu	KYUNKI SAAS BHI KABHI BA	3.7
10	Zee TV	Thu	MAAYKA	3.66
11	Star Plus	Tue	KASTURI	3.65
12	Colors	Wed	BALIKA VADHU	3.65
13	Star Plus	Mon	KIS DESH MEIN HAI MERA DIL	3.52
14	Star Plus	Mon	KYUNKI SAAS BHI KABHI BA	3.42
15	Zee TV	Mon	BANOO MAIN TERI DULHAAN	3.4
16	Zee TV	Thu	BANOO MAIN TERI DULHAAN	3.39
17	Star Plus	Tue	KYUNKI SAAS BHI KABHI BA	3.38
18	Zee TV	Mon	MAAYKA	3.37
19	Zee TV	Fri	MAAYKA	3.37
20	Zee TV	Tue	BANOO MAIN TERI DULHAAN	3.33
21	Star Plus	Wed	KIS DESH MEIN HAI MERA DIL	3.31
22	Star Plus	Thu	KAHAANI GHAR GHAR KI	3.3
23	Zee TV	Tue	MAAYKA	3.28
24	Zee TV	Wed	MAAYKA	3.28
25	Star Plus	Tue	RAJA KI AAYEGI BAARAT	3.28
26	Star Plus	Thu	KASTURI	3.26
27	Star Plus	Thu	KIS DESH MEIN HAI MERA DIL	3.21
28	Star Plus	Wed	KASTURI	3.19
29	Zee TV	Wed	BANOO MAIN TERI DULHAAN	3.18
30	Star Plus	Mon	KASTURI	3.18
31	Zee TV	Tue	KASAMH SE	3.15
32	Zee TV	Mon	KASAMH SE	3.04
33	Colors	Fri	JAI SHRI KRISHNA	3.04
34	Zee TV	Fri	BANOO MAIN TERI DULHAAN	3.02
35	Zee TV	Mon	BETIYANN GHAR KI LAKSHMI	3.01
36	Zee TV	Wed	SAATH PHERE	2.96
37	Colors	Mon	BALIKA VADHU	2.94
38 #	Colors	Thu	JAI SHRI KRISHNA	2.92
39	Star Plus	Mon	KAHAANI GHAR GHAR KI	2.91
40 *	Sony Entertainment	Sat	10 KA DUM	2.91
41	Star Plus	Wed	RAJA KI AAYEGI BAARAT	2.86
42	Star Plus	Wed	KYUNKI SAAS BHI KABHI BA	2.85
43	Star Plus	Thu	RAJA KI AAYEGI BAARAT	2.85
44	Star Plus	Tue	KAHAANI GHAR GHAR KI	2.83
45	Star Plus	Sat	BAA BAHOO AUR BABY	2.81
46 #	Colors	Wed	JAI SHRI KRISHNA	2.81
47	Zee TV	Mon	SAATH PHERE	2.78
48	Zee TV	Thu	SAATH PHERE	2.78
49	Zee TV	Thu	BETIYANN GHAR KI LAKSHMI	2.77
50 #	Star Plus	Sun	SAIBABA	2.73

Source: TAM Media, HSM, General Entertainment Channels, CS4+, All days, All 24 hours, Week 36 for 2008

\* represents Reality Game Show, # represents mythological programmes

# Zee Entertainment

## Company description

Zee Entertainment (Zee) is India's largest vertically integrated media and entertainment company. It has an integrated range of businesses, encompassing the content-to-consumer value chain of media and entertainment business. The company owns a bouquet of channels across various genres including general entertainment, cinema, music, news and sports. Zee has aggressive plans in the motion picture business through its subsidiary, Zee Studio (ZES), which works under two banners- Zee Motion Pictures and Zee Limelight.

## Investment strategy

We rate ZEEL Buy/Medium Risk, believing it is the best play in the Indian broadcasting sector due largely to its significant exposure to the fast growing pay-revenue market in India. Also, the divestment of Zee Next would result in improving cash flows and EPS upside of ~15-16% in FY09E-10E. Despite new GECs, Zee holds its own with its share in the top 50 programs at a decent ~20 (compared to ~25 at the peak). We expect an ad revenue CAGR of ~20% and pay revenue CAGR of ~17% over FY08-10E. EPS growth will be ~19% over the same period (~28% assuming Zee Next divestment), on our estimates.

## Valuation

Our target price for ZEEL is Rs240 based on 22x average FY09-10E EPS (lowered from 27x to take into account a more uncertain macro environment). We have valued ZEEL based on its historical trading band. Since the improvement in its viewership (Jun-06), ZEEL has traded in a range of 19x-40x, with an average of 29x. Our target multiple of 22x is at ~25% discount to the average, factoring in the fragmentation in the Indian TV broadcasting industry and slower ad-revenue growth.

## Risks

We rate Zee Medium Risk based on our quantitative risk-rating system that tracks 260-day historical share price volatility. The following risks could impede the stock from reaching our target price: (1) Zee's improved TV ratings have resulted in a sharp revival in ad revenues, with Zee hiking rates over the last few years. Loss of market share to competition would result in lower ad revenue growth. (2) Delays in CAS rollouts could result in a slower-than-expected ramp-up in pay revenues. While recent press reports suggest roll-out of CAS in 55 cities, we remain cautious as CAS implementation has witnessed significant delays in the past. Set-top-box supply could also hold back ramp-up of CAS. (3) Competitive intensity could result in higher costs (in the form of new channels or higher costs in existing channels) and take a toll on Zee's margins.

## Appendix A-1

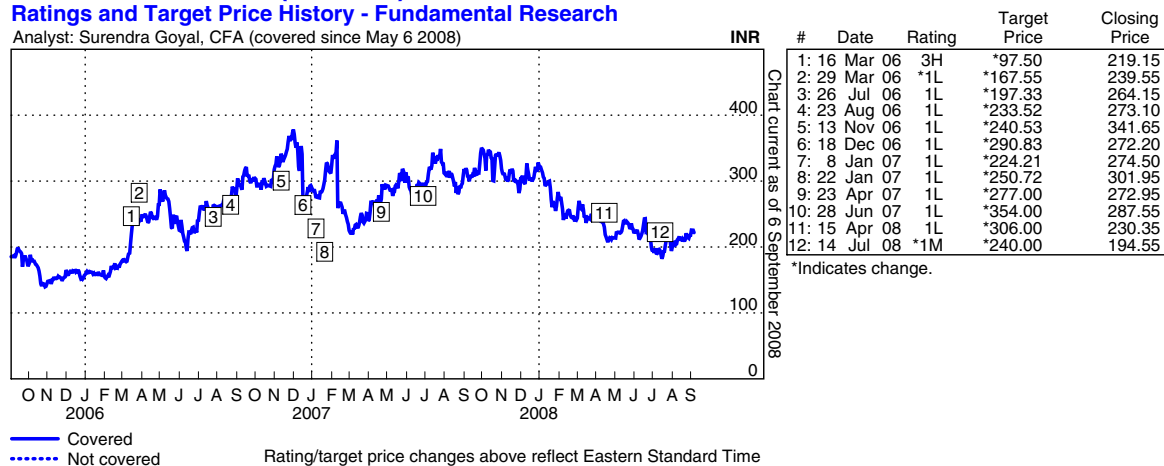
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Analyst: Surendra Goyal, CFA (covered since May 6 2008)



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