Cinemax India

CMP: Rs 145 | **Target: Rs 189** | **BUY**

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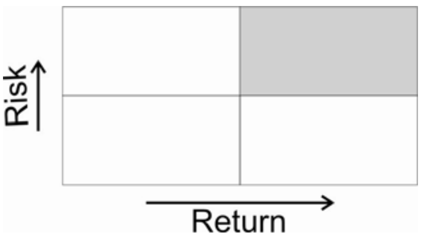
BSE Code	532807
NSE Code	CINEMAX

Risk-return profile



Company data

Particulars	
Market cap (Rs mn / US$ mn)	4,060/100.2
Outstanding equity shares (mn)	28
Free float (%)	31.9
52-week high/low (Rs)	204/101
3-month average daily volume	1,378,695

Stock performance

Returns (%)	1-mth	3-mth	6-mth
Cinemax	16.9	NA	NA
Sensex	7.9	(4.1)	(5.4)

Shareholding pattern

(%)	Mar-07
Promoters	68.1
FIIs	1.5
Banks & FIs	0.4
Public	30.0

Source: BSE

Picture perfect

Among the best plays on India's booming multiplex industry

- Leading multiplex operator with 10 theatre properties largely concentrated in cinema-hub Mumbai; owns largest number of properties vis-à-vis peers
- Multiplex segment which contributes a bulk of exhibition revenues has been growing at 80-100% YoY; we expect even stronger growth, led by rising disposable incomes, growth in organised retail and tax benefits
- Plans pan-India presence with ambitious projects in strategic locations during FY08 and FY09. Promoters' real estate development expertise and surplus real estate strengthen future growth prospects
- Revenue CAGR of 55% expected over FY07-FY09 to Rs 2.4bn with a 61% CAGR in net profits on the back of expansion, cost rationalisation and higher realisations
- We initiate coverage with Buy with a 12-month target price of Rs 189 based on DCF valuations

Financial snapshot

(Rs mn)	Sales	PAT	FDEPS (Rs)	P/E (x)	EV/EBITDA (x)	RoE (%)
FY07E	979.1	155.7	5.6	26.1	20.0	16.6
FY08E	1,505.8	252.6	9.0	16.1	12.1	14.3
FY09E	2,365.4	401.5	14.3	10.1	7.5	19.2

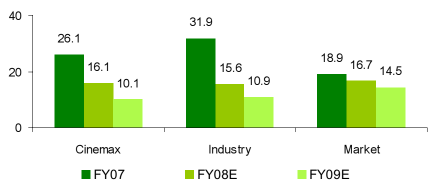
Source: Company, Religare Research

Growth profile

(%)	Sales	EBITDA	PAT	FDEPS
FY07E	35.4	51.8	102.7	(56.6)
FY08E	53.8	63.6	62.3	62.3
FY09E	57.1	60.2	59.0	59.0

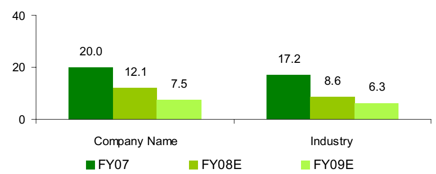
Source: Religare Research

P/E multiple (x)



Source: Religare Research

EV/EBITDA multiple (x)



Source: Religare Research

Industry outlook

Indian cinemas clocked 3.1bn footfalls in FY04 compared to 1.5bn in the US

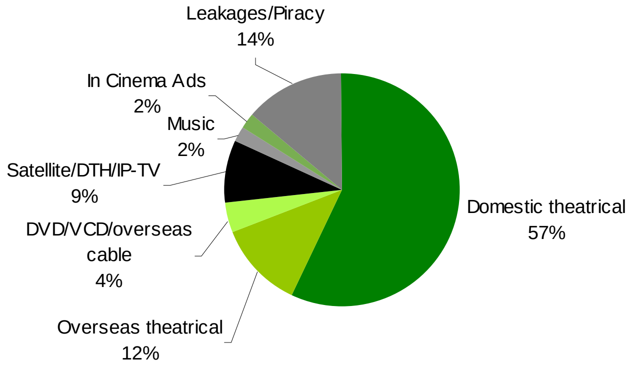
High cinema admissions point to strong growth prospects

Catching a movie in a cinema hall is one of the most popular entertainment options in India. In FY04, the total number of admissions or people visiting Indian cinemas stood at 3.1bn. The second-largest number of admissions was recorded in the US, at 1.5bn during the same period. India's high viewership levels point to the tremendous growth potential of cinemas, especially of multiplexes.

Box office sales make up a bulk of revenues

The Indian film industry currently realises almost 70% of its total revenues from domestic and overseas box office sales. In comparison, the US film industry earns only 35% of its revenue from box office sales, while the remaining 65% is derived from other sources such as sales of DVDs and VHS tapes, and the sale of cable and satellite television rights.

Distribution of film industry revenues



Source: Company RHP

Multiplexes constitute just 2% of total screens in India but garner over 30% of revenues

Multiplexes constitute a small proportion of total screens in India…

The Indian film exhibition sector can be divided into two segments – single and double screen cinemas, and multiplex cinemas. The sector earned revenues of Rs 34bn during FY04. As of March 2006, there were approximately 13,000 cinemas in India, of which 85 were multiplexes with a total of 276 screens - these constituted 2.4% of the total screens.

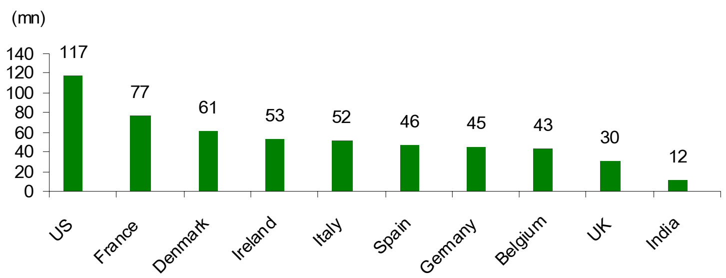
…but account for over a quarter of gross collections

Based on the gross box office collections (GBOC) available for Hindi films released in FY04, multiplexes constitute 28-34% (depending on 35-40% occupancy) of total GBOC for the top 50 Hindi films and 21- 25% of the total GBOC for all Hindi films.

Average number of screens falls far short of global average

In India, the number of screens per million population is just 12, while the average in Western countries is around 40. A Unesco study shows that India needs 20,000 screens versus about 12,000 at present to cater to the cinema viewing population.

Screens per million population



Source: Company RHP

Advantages of multiplexes

With approximately 250 seats per screen, multiplex cinemas are often characterised by good ambience and quality viewing, with high-end sound systems, comfortable seating, and popular food and beverages. Multiplexes offer significant economic advantages over similar size single-screen theatres due to the following -

Higher occupancy rates

Since multiplexes have several screens with different seating capacities, they offer flexibility as regards screening a movie based on its earning potential. This in turn results in higher occupancy rates compared to a single-screen theatre.

Greater number of shows

Flexible screening schedules result in better utilisation and higher revenues

A multiplex operator has the flexibility to decide on a screening schedule that will maximise the number of shows, thus accommodating a higher number of patrons.

Better exploitation of a movie

A movie can be released in multiple screens in the first week of its release and then gradually moved to one screen in the largest cinema, and finally to the smallest cinema within the complex. This helps to better exploit the revenue-earning potential.

Improved cost management

A multiplex cinema benefits from a set of shared facilities such as the box office, rest rooms, food and beverages facilities, and manpower, resulting in lower overheads per screen.

Growth drivers

Multiplex industry in a nascent phase

The number of multiplex screens is estimated to have risen 80-100% YoY in FY06

The multiplex segment is in a nascent stage of growth in India. More than 60 multiplexes with over 220 screens were slated to commence operations by the end of FY06, depicting a growth rate of 80-100% YoY. The tremendous growth in the multiplex segment is being driven by several factors such as a) an increase in disposable incomes, b) demographic changes in favour of cinema-going age groups, c) organised retail growth, d) entertainment tax benefits for multiplexes, and e) an increase in the number of high-grade films targeted at a particular audience segment.

Increase in disposable income

As disposable incomes rise, more is spent on discretionary items like movies and theatre

The rising earning power and growing disposable income of the Indian middle class is a key factor fuelling the growth of multiplexes. As incomes rise, a greater percentage is spent on discretionary items such as movies and theatre. From FY99 to FY03, the average Indian household increased its spending on movies and theatre from 1% of its disposal income to 4.6%

Favourable demographic shift

Urban population between the ages of 15-34 years is expected to increase from 107mn in FY01 to 138mn in FY11, a CAGR of 30%. During the same period, the urban population between 15-44 years is expected to grow from 146mn to 186mn, a 27% CAGR. As the 15-34 age group constitutes the largest movie-going demographic worldwide, growth in this segment would propel the popularity of multiplexes.

Organised retail set to grow rapidly…

The organised retail business in India is projected to grow robustly on the back of higher consumption levels, changing lifestyles, the availability of quality real estate and significant investments in malls. The organised retail segment is expected to increase its market share from 2% as of FY04 to 12-13% by FY10. Added availability of quality retail space is likely to reduce overall occupancy costs for tenants over the next three to five years, and will also facilitate their rapid expansion.

Multiplex growth closely linked to organised retail platforms like malls

…and is closely linked to growth in multiplexes

The growth in malls is not restricted to metros, but is also spreading to Tier-II towns which represent a very large base of consumers. The number of malls in India is expected to increase from approximately 50 at the end of FY04 to around 250 by the end of FY06. As per a CII-KPMG Report (2005), the presence of multiplexes in and around a mall increases footfalls by around 40-50%. Thus, the expected organised retail growth would result in a significant increase in the number of multiplex cinemas.

Entertainment tax benefits

In order to encourage investment in the film exhibition sector, many state governments have announced entertainment tax benefits to multiplex operators. This has encouraged the growth of multiplex cinemas and also led single-screen theatres to convert into multiplexes.

Entertainment tax exemption

State	Year1	Year2	Year3	Year4	Year5	Year 6&7	Min Seating	Min Screens
Maharashtra	100	100	100	75	50		1250	4
Rest of Maharashtra	100	100	100	75	50		1000	3
Punjab	100	100	100	100	100		1000	3
West Bengal	100	100	100	100			1000	3
Rajasthan	50	50	50	50	50	50	1000	NA
Uttar Pradesh	100	100	100	100	100		1000	3
Madhya Pradesh	100	100	100	75	50		1000	3
Karnataka	100	100	100	75	50		NA	NA

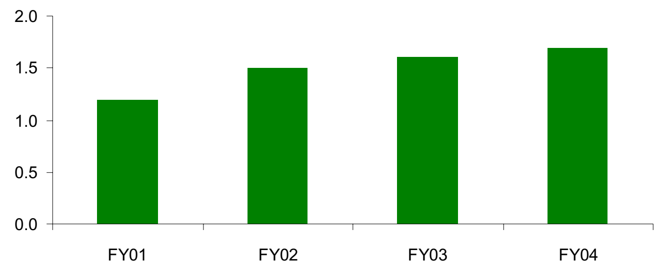
Source: Company RHP

Raising corporatisation of film production will lead to more high-grade films

Increase in number of high-grade films

The demand for a particular movie is generally driven by both its critical reviews and word-of-mouth. As shown below, from FY01 to FY04, the number of releases per week for high-grade Hindi films witnessed a CAGR of 48%. These films are in higher demand, and with the increasing corporatisation of the film production sector, we expect a larger number of high-quality films to be produced.

Average number of Hindi films released per week



Source: Company RHP

Company overview

Promoted by real estate developer – Kanakia Group

Cinemax India is a part of the Kanakia Group which has a track record of over 20 years in real estate development. The promoters entered into the film exhibition industry with the acquisition of a single-screen theatre named 'Samrat' at Goregaon, Mumbai in 1997, which was subsequently retrofitted. The promoter group initially retrofitted (remodeled) single or multiple screen theatres. With the introduction of the Multiplex Policy by the Maharashtra government, the group moved on to the development of multiplexes.

Primarily focused on film exhibition

Cinemax operates 10 properties with 33 screens and 9,220 seats

Cinemax is focused mainly on the exhibition business with limited interests in mall development and gaming. It is one of the largest exhibition theatre chains in India, and is a dominant player in Mumbai – home of the Hindi film industry. The company operates 10 properties with 33 screens and 9,220 seats, comprising a combination of high-end multiplexes and budget retrofit single screens. Cinemax plans to aggressively expand into new markets and establish a pan-India presence.

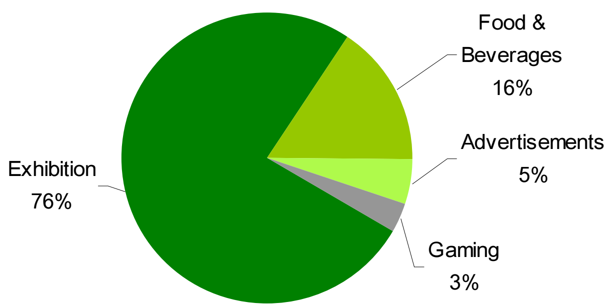
Limited interests in gaming and malls

Cinemax has developed the Eternity Mall at Thane on 200,000sq ft of carpet area. This mall houses a company multiplex as well as its gaming business which goes by the brand name *Giggles-The Gaming Zone*. This zone has been developed over 13,000sq ft and offers around 50 state-of-the-art games catering to all age groups. The company is also constructing a 100,000sq ft mall at Nagpur, which includes an approximate area of 30,000sq ft for a 3-screen multiplex.

Two multiplexes run by subsidiaries

Cinemax currently has three wholly owned subsidiaries, Vista Entertainment (VEPL), Growel Entertainment (GEPL) and Nikmo Finance (NEPL), a wholly owned subsidiary of GEPL. VEPL and NEPL operate two multiplexes in Mumbai (at Versova and Kandivali East respectively), pursuant to business conducting agreements.

Existing revenue model



Source: Company, Religare Research

Investment rationale

Realty background helps in cost control and time management

Derives significant benefits from promoters' realty expertise

The Kanakia Group has been associated with real estate development for more than two decades, and has developed over 5mn sq ft of residential and commercial space. Cinemax has been able to harness this extensive experience in real estate development to control cost and time overruns without compromising on quality and ambience. Moreover, the realty expertise has also helped it to identify strategic locations and acquire properties at competitive prices. This is because the group has established good relationships with various suppliers which enable it to get preferred services and negotiate for competitive commercial terms.

Largest chain of owned theatre properties

Cinemax is the largest owner of theatre properties in India. It has 8 fully owned properties comprising 21 screens spread over approximately 146,200sq ft. This saves on lease rent which is a key element of cost in the case of a leased business model. An ownership model also provides the flexibility of remodeling screen formats with newer technology, concepts or technology formats.

Major presence in Mumbai, the largest territory for film exhibition revenue

Major presence in Mumbai – the hub of Indian cinema

Cinemax owns 8 properties covering 120,000sq ft in Mumbai and Thane alone. Mumbai is the largest film exhibition territory in India, accounting for 15% of the all-India box office collections. Cinemax has a strong presence in Mumbai and Thane with 9 theatres (owned plus leased), 30 screens and a seating capacity of 8,218. The theatres are strategically located in high catchment areas in and around Mumbai such as Sion, Andheri, Versova, Goregaon, Kandivali, Mira Road and Thane.

Professional team ensures best location selection

The company has an experienced team of professionals to assess the potential of a location after evaluating its demographic trends in terms of catchment areas, purchasing power and competing alternatives. This helps Cinemax to zero in on relatively untapped locations and gain the first-mover advantage. The proximity of the company's multiplexes in a particular location also allows flexibility in rotating prints between the theatres, thereby maximising returns.

Existing multiplexes

Multiplex	Screens	Seats	Start Date
Andheri	1	362	Aug 1998
Eternity Mall, Thane	4	1,056	May 2006
Goregaon	2	698	Dec 1997
Kandivali (W)	1	287	Feb 1998
Mira Road	3	1,018	May 2004
Nashik	3	1,002	May 2004
Sion	5	827	Oct 2000
Wonder Mall, Thane	4	1,136	Dec 2003
Versova	6	1,575	Sep 2005
Kandivali (E)	4	1,259	Jan 2006
Total	**33**	**9,220**	

Source: Company

Innovative concepts to differentiate the theatre experience

Cinemax focuses on constant innovation in its services and facilities which ensures customer satisfaction and helps it stay ahead of the competition. For instance, it has introduced novel luxury recliner-style seating in a Mumbai multiplex entitled *The Red Lounge,* which is available at premium ticket rates. This initiative has been a success with high-income viewers.

Aggressive growth plans to establish pan-India presence

Plans to triple capacity by FY08

As part of its strategy to grow its film exhibition business on a national scale, Cinemax proposes to expand either through lease tie-ups or through acquisition of exhibition theatres. From its current presence primarily in Mumbai and Thane, the company has plans to spread across India with 21 properties, 97 screens and a seating capacity of 24,713 by FY08, i.e., to nearly triple its current capacity. It further plans to be present in 42 locations in 11 states by FY09. The company has already invested Rs 86mn from internal accruals together with its IPO proceeds to finance its expansion plans.

Surplus real estate available to fund future capex

The 200,000sq ft Eternity Mall houses the company's exhibition and gaming businesses, with the balance space (around 30,000 sq ft) being leased out to companies like Globus, Proline and Planet M. Around 65,000sq ft of the Nagpur property is also free to be leased out to different brands for their retail outlets. The sale of such leased properties could rake in an amount of Rs 650mn-750mn, and offer a financing option for the company's expansion that does not involve debt.

Financial outlook

Expect 55% revenue CAGR over FY07-FY09

We believe that the existing multiplexes as well as forthcoming properties would add significant value to Cinemax's financials. We expect the company to clock a consolidated revenue CAGR of 55% over FY07-FY09 to Rs 2.4bn.

Strong operating performance

Added revenues as well higher ticket prices, coupled with a larger base would help the company spread its overheads, thus expanding operating profit and margins going forward. We forecast a 62% CAGR in operating profit over FY07-FY09.

Net profit to grow at 61% CAGR

An increase in the number of multiplexes generating higher operating profit would drive earnings growth. We expect net profit to expand at a 61% CAGR over FY07-FY09 to Rs 401.5mn.

Valuation

Valuations are attractive

Available at attractive valuations vis-à-vis peers

At the current market price of Rs 145, the stock is quoting at 26.1x and 16.1x on FY07 and FY08 expected earnings of Rs 5.6 and Rs 9 respectively. On an EV/EBIDTA basis, the stock is quoting at 20x and 12.1x for the two years respectively. Despite being the largest owner of theatre properties in India, with a strong presence in Mumbai and the requisite expertise in multiplex set-ups, the stock is available at an attractive valuation compared to its peers.

Comparative valuation

Company	CMP (Rs)	EPS (Rs)		P/E (x)		EV/EBIDTA (x)		ROCE(%)		RONW(%)		Price/BV	
		FY07E	FY08E	FY07E	FY08E	FY07E	FY08E	FY07E	FY08E	FY07E	FY08E	FY07E	FY08E
Cinemax	145	5.6	9.0	26.1	16.1	20.0	12.1	17.9	18.1	16.6	14.3	2.5	2.2
PVR	202	4.6	12.7	44.0	15.9	19.8	8.0	7.9	17.6	5.9	14.7	2.5	2.2
Inox	126	4.0	7.4	31.8	17.1	19.9	11.6	12.0	18.0	9.3	14.0	2.6	2.2
Shringar	52	2.6	3.8	19.9	13.6	11.8	6.2	10.7	12.9	17.4	21.5	2.5	2.1

Source: Religare Research

DCF valuation yields fair value of Rs 189

We prefer using a discounted cash flow (DCF) model for valuing Cinemax as the method fairly reflects the growth momentum of the company. Our DCF model estimates a fair value of Rs 189 per share for Cinemax, based on a terminal growth of 4% and a weighted average cost of capital (WACC) of 15.4%. We have considered an industry average beta of 1.1 for the company, which is higher than that of PVR and Inox. The sensitivity of our target price to various terminal growth rates and beta are presented below.

Sensitivity analysis

Terminal growth (%)	Beta				
	0.9	1.0	1.1	1.2	1.3
3.0	207	191	176	164	152
3.5	215	198	183	169	157
4.0	224	206	189	175	162
4.5	234	214	197	181	168
5.0	246	224	205	188	174

Source: Religare Research

Buy with target of Rs 189

DCF price target of Rs 189, an upside of 33%; Buy

We believe that Cinemax's aggressive move to add properties is in line with the opportunities in the multiplex segment, especially considering the expected growth in organised retail. We expect the company to be a prominent player in the segment and believe that it holds significant growth potential. Our target of Rs 189 represents a 33% appreciation to the current price; we initiate coverage with a Buy.

Financials (Consolidated)

Profit and Loss statement

(Rs mn)	FY06	FY07E	FY08E	FY09E
Revenues	723.3	979.1	1505.8	2365.4
Growth (%)	114.7	35.4	53.8	57.1
EBITDA	151.6	230.1	376.5	603.2
Growth (%)	47.1	51.8	63.6	60.2
Depreciation	29.3	30.8	50.1	60.1
EBIT	122.3	199.3	326.4	543.1
Growth (%)	50.6	63.0	63.8	66.4
Interest	40.6	38.9	37.1	35.3
Other income	22.4	73.0	89.4	94.2
EBT	104.1	233.4	378.7	602.0
Growth (%)	30.4	124.1	62.3	59.0
Tax	27.8	77.7	126.1	200.5
Effective tax rate	26.7	33.3	33.3	33.3
Adj net income	76.8	155.7	252.6	401.5
Growth (%)	23.5	102.7	62.3	59.0
Shares outstanding (mn)	6.0	28.0	28.0	28.0
FDEPS (Rs)	12.8	5.6	9.0	14.3
DPS (Rs)	0.0	1.0	2.0	3.0
CEPS (Rs)	17.7	6.7	10.8	16.5

Source: Company, Religare Research

Balance sheet

(Rs mn)	FY06	FY07E	FY08E	FY09E
Cash and cash eq	27.9	660.2	318.1	177.2
Accounts receivable	37.9	53.7	86.6	142.6
Inventories	169.7	222.7	330.0	505.5
Others current assets	336.4	345.0	360.0	365.0
Current assets	571.9	1281.5	1094.8	1190.3
LT investments	8.5	800.0	800.0	1000.0
Net fixed assets	516.3	548.8	1332.2	1872.1
CWIP	125.5	96.2	0.0	0.0
Total assets	1222.2	2726.5	3227.0	4062.4
Payables	331.5	450.7	697.2	1101.7
Others	39.0	77.7	126.1	200.5
Current liabilities	370.5	528.4	823.3	1302.2
LT debt	601.1	551.1	501.1	451.1
Other liabilities	6.5	12.1	15.1	20.1
Equity capital	60.0	280.0	280.0	280.0
Reserves	184.2	1354.9	1607.5	2009.0
Net Worth	244.2	1634.9	1887.5	2289.0
Total liabilities	1222.2	2726.5	3227.0	4062.4
BVPS (Rs)	40.7	58.4	67.4	81.8

Source: Company, Religare Research

Cashflow statement

(Rs mn)	FY06	FY07E	FY08E	FY09E
Net income	76.8	155.7	252.6	401.5
Depreciation	29.3	30.8	50.1	60.1
Other adjustments	0.0	0.0	0.0	0.0
Changes in WC	(174.1)	80.6	139.6	242.5
Operating cash flow	(68.0)	267.1	442.2	704.1
Capital expenditure	(177.3)	(34.0)	(737.2)	(600.0)
Investments	3.4	(791.5)	0.0	(200.0)
Other investing inc/(exp)	0.0	0.0	0.0	0.0
Investing cash flow	(173.9)	(825.5)	(737.2)	(800.0)
Free cash flow	(241.9)	(558.4)	(295.0)	(95.9)
Issue of equity	(42.7)	1235.0	0.0	0.0
Issue/repay debt	158.6	(50.0)	(50.0)	(50.0)
Dividends paid	0.0	0.0	0.0	0.0
Others	(1.1)	5.7	3.0	5.0
Financing cash flow	114.9	1190.7	(47.0)	(45.0)
Beg. cash & cash eq	154.9	27.9	660.2	318.1
Chg in cash & cash eq	(127.1)	632.3	(342.0)	(140.9)
Closing cash & cash eq	27.9	660.2	318.1	177.2

Source: Company, Religare Research

Financial ratios

(Rs mn)	FY06	FY07E	FY08E	FY09E
EBITDA margin (%)	21.0	23.5	25.0	25.5
EBIT margin (%)	16.9	20.4	21.7	23.0
Net profit margin (%)	10.6	15.9	16.8	17.0
EPS growth (%)	23.5	(56.6)	62.3	59.0
Receivables (days)	19.1	20.0	21.0	22.0
Inventory (days)	85.7	83.0	80.0	78.0
Payables (days)	167.3	168.0	169.0	170.0
Current ratio (x)	1.5	2.4	1.3	0.9
Interest coverage (x)	3.0	5.1	8.8	15.4
Debt/equity ratio (x)	2.5	0.3	0.3	0.2
ROE (%)	33.8	16.6	14.3	19.2
ROCE (%)	19.1	17.9	18.1	24.7
ROAE (%)	16.2	13.1	14.2	21.0
EV/Sales (x)	2.0	4.7	3.0	1.9
EV/EBITDA (x)	9.7	20.0	12.1	7.5
P/E (x)	11.3	26.1	16.1	10.1
P/BV (x)	3.6	2.5	2.2	1.8
P/CEPS (x)	8.2	21.8	13.4	8.8

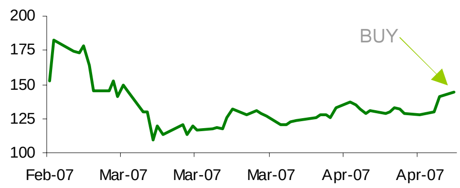
Source: Company, Religare Research

Recommendation history

Date	Event	Target (Rs)	Reco
9-May-07	Initiating Coverage	189	Buy

Source: Religare Research

Stock performance



Source: Bloomberg

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