

## Zee Entertainment Enterprises

Q3FY10/ Target price change

20 January 2010

## Buy

Target Price: Rs302

CMP: Rs271\*

Upside: 11%

\*as on 19 January 2010

## Cost management at its best

**Zee Entertainment Enterprises (ZEEL) posted broadly in-line results with ad revenue growth back in black and DTH subscription (subs) revenues continuing to grow at a healthy pace. International and analog sub revenues disappointed but the management once again proved its ability to manage costs and grow margins. Maintain Buy.**

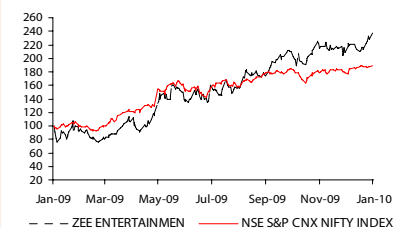
- **Ad revenue growth back in black:** Ad revenues grew 1% YoY (we estimated 2% YoY growth) to Rs2,707mn on the back of higher ad rates coupled with increased inventory utilization.
- **Analog and international subs revenue disappoints:** Analog subs revenues declined 3% YoY to Rs820mn on the back of some churn due to the DTH platform. International subs revenues too fell 12% YoY for the third consecutive quarter to Rs1,014mn.
- **Best margin in last 2 years:** ZEEL reported healthy margin of 29.6% (up 762bp YoY and 172bp QoQ) as it continues to reap the benefits of its cost-saving measures. The management has once again proved its focus on profitability and ability to manage costs.
- **Maintain Buy, target price raised:** We have raised our target price to Rs302 (previously Rs279), since we now use proforma FY11E EPS of Rs12.6 (consolidating the R-GECs). We now value the company at 24x FY11E earnings, similar to Sun TV Network.

## Key Data

Bloomberg Code	Z IN
Reuters Code	ZEE.BO
Current Shares O/S (mn)	434.0
Diluted Shares O/S(mn)	434.0
Mkt Cap (Rsbn/USDbn)	117.6/2.6
52 Wk H / L (Rs)	293/88
Daily Vol. (3M NSE Avg.)	1,212,874
Face Value (Rs)	1

1 USD = Rs45.6

## One year Indexed Stock Performance



## Price Performance (%)

	1M	6M	1Yr
Zee Ent.	7.9	46.3	125.0
NIFTY	5.8	20.6	85.3

Source: Bloomberg, Centrum Research  
\*as on 19 January 2010

Y/E Mar (Rsmn)	Q3FY10	Q3FY09	YoY (%)	Q2FY10	QoQ (%)	Q3FY10E	Variance (%)
<b>Net sales</b>	<b>5,309</b>	<b>5,456</b>	<b>(2.7)</b>	<b>5,405</b>	<b>(1.8)</b>	<b>5657</b>	<b>(6.1)</b>
Total Expenditure	3,737	4,256	(12.2)	3,897	(4.1)	4,065	(8.1)
Employee Cost	372	382	(2.8)	442	(15.9)	465	(20.1)
as % of sales	7.0	7.0		8.2		8.2	
Programming & op. cost	2,306	2,684	(14.1)	2,229	3.5	2350	(1.9)
as % of sales	43.4	49.2		41.2		41.5	
Selling & other expenses	1,059	1,190	(11.0)	1,226	(13.6)	1250	(15.3)
as % of sales	19.9	21.8		22.7		22.1	
<b>EBIDTA</b>	<b>1,573</b>	<b>1,200</b>	<b>31.0</b>	<b>1,508</b>	<b>4.3</b>	<b>1,592</b>	<b>(1.2)</b>
<b>% margin</b>	<b>29.6</b>	<b>22.00</b>	<b>762bp</b>	<b>27.90</b>	<b>172bp</b>	<b>28.14</b>	<b>190bp</b>
Other Income	323	401	(19.5)	291	11.0	270	
Depreciation	76	84	(8.9)	77	(0.8)	77	
EBIT	1,819	1,518		1,722		1,785	
Interest	65	386		84		87	
Exceptional Item	(313)	(26)		-		-	
PBT	2,067	1,158	78.5	1,638	26.2	1,698	
Tax	603	318		529		560	
% Tax	29.2	27.5		32.3		33.0	
<b>PAT before MI</b>	<b>1,464</b>	<b>840</b>	<b>74.4</b>	<b>1,109</b>	<b>32.0</b>	<b>1,138</b>	
MI and associates	(100)	15		(32)		-	
<b>PAT after MI (reported)</b>	<b>1,564</b>	<b>825</b>		<b>1,141</b>		<b>1,138</b>	
PAT after MI (adjusted)	1,251	799	56.6	1,141	9.7	1,138	10.0

Source: Company, Centrum Research

Ankit Kedia  
ankit.kedia@centrum.co.in  
+91 22 4215 9634

Y/E Dec (Rsmn)	Rev	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY %	Fully DEPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)	P/BV
FY07	15,159	(8.4)	3,204	21.1	2,375	11.9	5.5	9.3	7.1	49.3	36.5	4.5
FY08	18,354	21.1	5,423	29.5	3,858	62.4	8.9	14.6	11.1	30.3	21.5	4.1
FY09	21,773	18.6	5,480	25.2	3,673	(4.8)	8.5	11.1	9.7	31.9	21.8	3.4
FY10E	20,769	(4.6)	5,733	27.6	4,534	23.5	10.4	11.7	8.5	25.8	20.3	3.2
FY11E	23,663	13.9	6,766	28.6	5,203	14.8	12.0	12.8	9.2	22.5	16.8	2.9

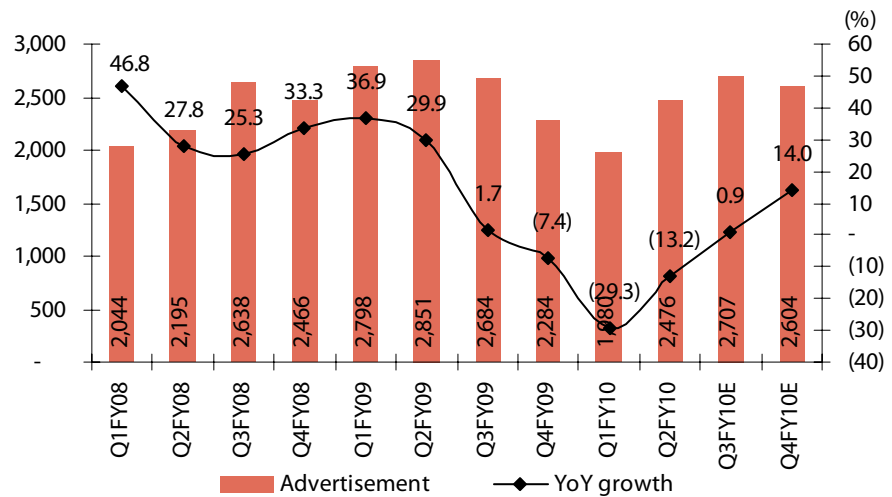
Source: Company, Centrum Research Estimates

Please refer to important disclosures/disclaimers in Appendix A

### Ad revenue growth back in black

ZEEL's advertisement revenues grew 1% YoY (we estimated 2% YoY growth) to Rs2,707mn on the back of higher ad rates coupled with increased inventory utilization, currently at 90% for the network. Ad revenues returned to black after three consecutive quarters of decline on the back of strong festival demand and up-tick in ad market. The management maintained that all new deals were happening at higher rates, which would translate into strong ad revenue growth in the coming quarters.

Exhibit 1: Ad revenue growth (YoY)

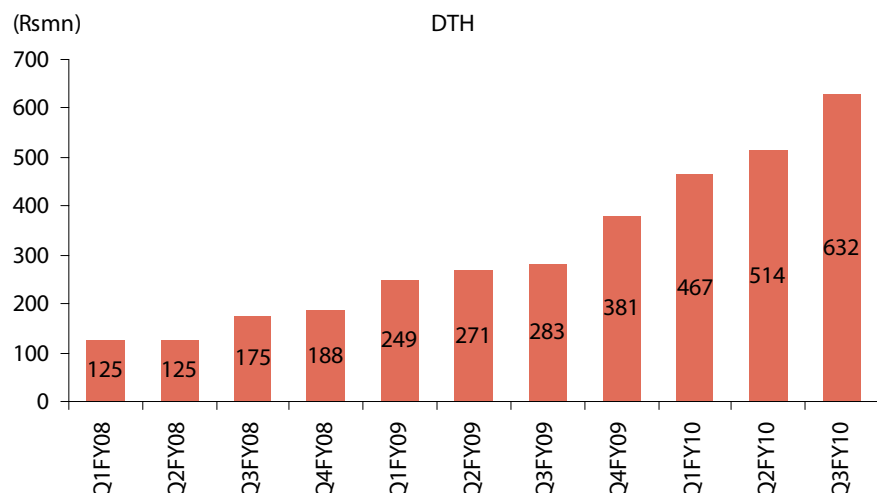


Source: Company, Centrum Research Estimates

### DTH subscription revenues continue to be strong...

DTH subscription revenues grew 123% YoY to Rs632mn (up 23% QoQ) on the back of strong subs addition. The management maintained that total DTH paying subscriber base was at about 9mn, up by about 1mn during the quarter. During the quarter the company generated non-recurring revenue of Rs49.8mn on the back of arrears, which was recovered from the DTH operators. DTH subs revenue will continue to be a key growth driver for the company, in our view with estimated revenues of Rs2,854mn for FY11.

Exhibit 2: DTH subscription revenue growth

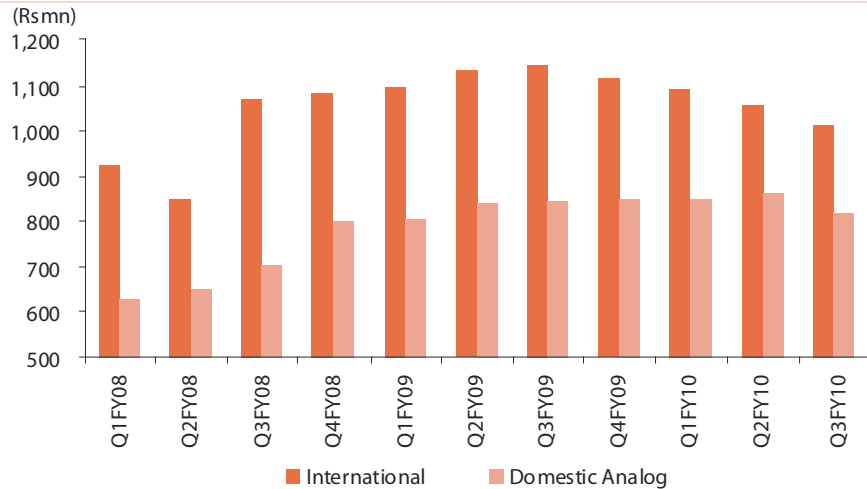


Source: Company, Centrum Research

### ...but domestic analog and international subscription disappoints

Domestic analog subs revenues fell 3% YoY (-4.8% QoQ) to Rs820mn on the back of some churn due to the DTH platform. This business has not seen much pick-up in its revenues, which has been hovering at Rs800-860mn over the last 7 quarters. International subscription revenues too declined 12%YoY for the third consecutive quarter to Rs1,014mn. We expect the decline to continue for the next few quarters due to economic slowdown, predominantly in Europe and also on the back of rupee appreciation.

**Exhibit 3: Domestic and international subs revenues under pressure**

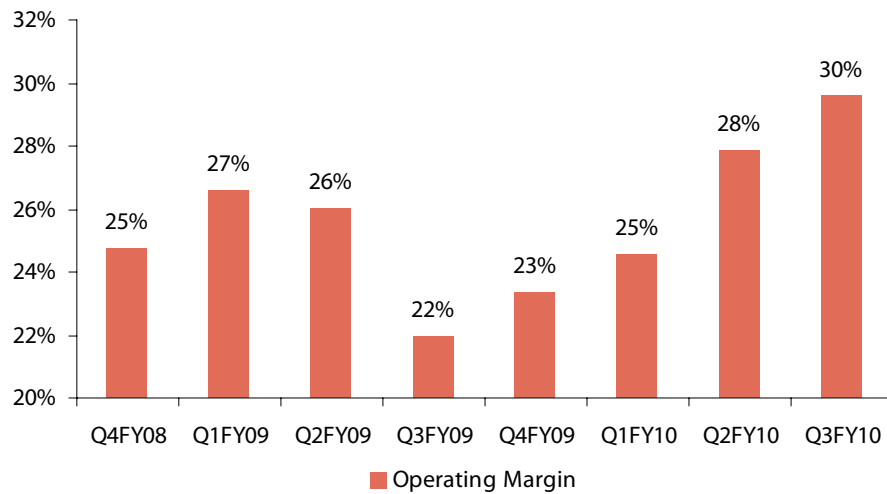


Source: Company, Centrum Research

**Best margin in last 2 years**

ZEEL reported healthy margin of 29.6% (up 762bp YoY and 172bp QoQ), the highest in the last 8 quarters, as it continues to reap the benefits of its cost-saving measures. The management has once again proved its focus on profitability and ability to manage costs. Programming & operating costs as a percentage of sales stood at 43.4% vs 49.2% in Q3FY09. Going forward, the channel might have to increase original programming hours, which would also raise its programming costs. Employee cost too declined 2.8% YoY and 16% QoQ to Rs372mn, lowest in last two years.

**Exhibit 4: Significant expansion in operating margin**



Source: Company, Centrum Research

**Other highlights**

The ZEEL board has approved the proposal to acquire additional 45% stake in its subsidiary Taj TV Mauritius and additional 50% stake in its subsidiary, Taj Television (India) from Bukhatir Group for \$44.145mn. The company acquired a 50% stake in Ten Sports in FY07 at an enterprise value of \$114mn. We believe this acquisition will have strong synergies with the current business since it will now integrate Zee Sports team with Ten Sports, which currently works independently for sales, content and distribution.

The management claimed that Rs3.85bn has been re-paid by group companies to ZEEL during January 2010 and about Rs5bn is yet to be paid by the group companies, of which a substantial amount would be paid during the current quarter.

## Estimates revised

We have slightly raised our margin estimate for the company on the back of significant cost savings during the quarter.

### Exhibit 5: Revised estimates

	FY10E			FY11E		
	Revised	Previous	%change	Revised	Previous	%change
Sales	20,769	21,791	(4.7)	23,663	25,131	(5.8)
EBIDTA	5,733	5,908	(3.0)	6,766	7,118	(4.9)
EBIDTA Margin (%)	27.6	27.1	49bp	28.6	28.3	27bp
Adj PAT after MI	4,534	4,420	2.6	5203	5239	(0.7)

Source: Company, Centrum Research Estimates

## Target price raised; maintain Buy

We have increased our target price to Rs302 (previously Rs279) since we have use proforma FY11E EPS of Rs12.6 (consolidating the R-GECs). We now value the company at 24x FY11E similar to Sun TV Network, considering that ZEEL would now have all the regional channels and command a higher multiple.

## Financials

### Exhibit 6: Income Statement

Y/E March (Rsmn)	FY07	FY08	FY09	FY10E	FY11E
Net Sales	15,159	18,354	21,773	20,769	23,663
Growth (%)	(8.4)	21.1	18.6	-4.6	13.9
Cost of Revenues	8,080	7,818	9,810	9,152	10,530
% of Sales	53.3	42.6	45.1	44.1	44.5
Employee Cost	1,017	1,438	2,031	1,627	1,871
% of Sales	6.7	7.8	9.3	7.8	7.9
Admin & other expenses	2,858	3,675	4,452	4,258	4,496
% of sales	18.9	20.0	20.4	20.5	19.0
<b>EBIDTA</b>	<b>3,204</b>	<b>5,423</b>	<b>5,480</b>	<b>5,733</b>	<b>6,766</b>
EBIDTA Margins (%)	21.1	29.5	25.2	27.6	28.6
Depreciation	185	232	310	310	350
PBIT	3,019	5,191	5,170	5,423	6,416
Interest expenses	334	516	1,339	325	300
PBT for operations	2,685	4,675	3,831	5,098	6,116
Other non operating income	747	1,138	1,572	1,450	1,650
PBT before extra-ordinary items	3,432	5,813	5,403	6,548	7,766
Extraordinary inc/(exp)	-	(26)	1,451	313	-
PBT	3,432	5,787	6,854	6,861	7,766
Provision for tax	999	1,627	1,633	2,264	2,563
Effective tax rate (%)	29.1	28.1	23.8	33.0	33.0
<b>Reported Profit before MI</b>	<b>2,433</b>	<b>4,160</b>	<b>5,221</b>	<b>4,597</b>	<b>5,203</b>
Minority interest	78	338	100	(250)	-
Reported PAT after MI	2,375	3,833	5,124	4,847	5,203
Recurring PAT	2,375	3,858	3,673	4,534	5,203

Source: Company, Centrum Research Estimates

### Exhibit 7: Balance Sheet

Y/E March (Rsmn)	FY07	FY08	FY09	FY10E	FY11E
Share Capital	434	434	434	434	434
Reserves & Surplus	25,747	28,177	33,561	36,180	40,365
Total Shareholders Funds	26,181	28,611	33,995	36,614	40,799
Minority Interest	819	1,117	948	698	698
Loan Funds	3,226	3,866	5,757	5,550	5,100
Deferred Tax Liab	-	-	-	-	-
<b>Total Capital Employed</b>	<b>30,225</b>	<b>33,594</b>	<b>40,700</b>	<b>42,862</b>	<b>46,597</b>
Gross Block	15,702	16,225	18,932	20,015	20,595
Less:- Accumulated Depreciation	1,081	1,239	1,508	1,926	2,358
Net Block	14,622	14,986	17,423	18,089	18,237
Capital WIP	219	619	669	350	350
Total assets	14,841	15,605	18,093	18,439	18,587
Differed tax asset	75	243	113	113	113
Investments	2,326	2,515	1,271	1,271	1,271
Inventory	24	32	44	50	65
Debtors	5,331	5,907	6,437	6,439	7,099
Loans & advances	9,762	11,475	14,087	13,085	13,961
Programming & film rights	2,016	2,442	4,532	4,900	5,100
Cash & bank balances	955	1,652	1,926	5,254	7,454
Total current assets	18,088	21,508	27,026	29,728	33,679
Current liabilities and provisions	5,106	6,279	5,803	6,689	7,053
Net current assets	12,981	15,230	21,223	23,039	26,626
Misc Expenditure	2	0	0	0	0
<b>Total</b>	<b>30,225</b>	<b>33,594</b>	<b>40,700</b>	<b>42,862</b>	<b>46,597</b>

Source: Company, Centrum Research Estimates

### Exhibit 8: Cash flow

Y/E March (Rsmn)	FY07	FY08	FY09	FY10E	FY11E
<b>Cash flows from operating</b>					
Profit before tax	3,432	5,813	5,403	6,548	7,766
Depreciation & amortisation	185	232	310	310	350
Others	(138)	(262)	882	(1,915)	(1,268)
<b>Operating charges bef. WC changes</b>	<b>3,479</b>	<b>5,783</b>	<b>6,596</b>	<b>4,943</b>	<b>6,848</b>
Working capital changes	(486)	(1,622)	(4,837)	1,512	(1,388)
Cash inflow from operations	2,993	4,162	1,759	6,456	5,460
Income tax paid	(1,279)	(1,151)	(757)	(2,264)	(2,563)
<b>Net cash inflow from operations</b>	<b>1,714</b>	<b>3,011</b>	<b>1,002</b>	<b>4,191</b>	<b>2,897</b>
<b>Cash flows from investing</b>					
Capex	(460)	(1,019)	(594)	(764)	(580)
Investments	(4,272)	(1,497)	(3,278)	-	-
Other Income	452	862	3,075	1,450	1,650
<b>Cash from investment</b>	<b>(4,280)</b>	<b>(1,654)</b>	<b>(798)</b>	<b>686</b>	<b>1,070</b>
<b>Cash flow from financing</b>					
Minority Interest	293	(20)	(20)	-	-
Borrowings/ repayments	2,650	680	1,958	(207)	(450)
dividend paid	(498)	(764)	(1,016)	(1,018)	(1,018)
Interest paid	(236)	(561)	(852)	(325)	(300)
<b>Cash from financing</b>	<b>2,209</b>	<b>(664)</b>	<b>71</b>	<b>(1,549)</b>	<b>(1,768)</b>
Net inc/dec. in cash & cash eq.	(357)	693	274	3,328	2,199
Cash & cash eq. beginning of the year	1,286	955	1,652	1,926	5,254
Exceptions	27	4	-	-	-
<b>Cash at the end of the year</b>	<b>955</b>	<b>1,652</b>	<b>1,926</b>	<b>5,254</b>	<b>7,454</b>

Source: Company, Centrum Research Estimates

### Exhibit 9: Key Ratios

Y/E March	FY07	FY08	FY09	FY10E	FY11E
<b>Margin ratios (%)</b>					
EBIDTA Margins	21.1	29.5	25.2	27.6	28.6
PBIT Margins	19.9	28.3	23.7	26.1	27.1
PBT Margins	22.6	31.7	24.8	31.5	32.8
PAT Margins	16.1	22.8	17.3	20.6	22.0
<b>Growth ratios (%)</b>					
Revenues	(8.4)	21.1	18.6	(4.6)	13.9
EBIDTA	18.9	69.3	1.1	4.6	18.0
Recurring Net Profit	11.9	62.4	(4.8)	23.5	14.8
<b>Return Ratios (%)</b>					
ROCE	7.1	11.1	9.7	8.5	9.2
RoIC	11.9	18.4	15.5	15.0	17.6
ROE	9.3	14.6	11.1	11.7	12.8
<b>Turnover Ratios</b>					
Average collection period(days)	128	117	108	113	110
Average payment period (days)	119	117	97	99	91
Working Capital Cycle (days)	10	2	13	17	21
<b>Per Share (Rs)</b>					
Recurring EPS	5.5	8.9	8.5	10.4	12.0
Recurring CEPS	6.0	10.2	9.4	10.6	12.8
Book Value	60.4	66.0	78.3	84.4	94.0
Dividend	1.5	2.0	2.0	2.0	2.0
<b>Valuations (x)</b>					
P/E	49.3	30.3	31.9	25.8	22.5
P/BV	4.5	4.1	3.4	3.2	2.9
EV/EBIDTA	36.5	21.5	21.8	20.3	16.8
EV/Sales	7.7	6.4	5.5	5.6	4.8
M-cap/Sales	7.7	6.4	5.4	5.6	5.0

Source: Company, Centrum Research Estimates

## Appendix A

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**Sanjeev Patni**  
**T. S. Baskaran**

**Head - Institutional Equities**  
**Joint Head – Institutional Equities**

**sanjeev.patni@centrum.co.in**  
**ts.baskaran@centrum.co.in**

**91-22-4215 9699**  
**91-22-4215 9620/87**

**Research**

Dhananjay Sinha	Economist	Economy & Strategy	dhananjay.sinha@centrum.co.in	91-22-4215 9619
Niraj Shah	Sr Analyst	Metals & Mining, Pipes	niraj.shah@centrum.co.in	91-22-4215 9685
Mahantesh Sabarad	Sr Analyst	Automobiles/Auto Ancillaries	mahantesh.sabarad@centrum.co.in	91-22-4215 9855
Madanagopal R	Sr Analyst	Infra, Power, Capital Goods	r.madanagopal@centrum.co.in	91-22-4215 9684
Abhishek Anand	Analyst	Telecom, Education, Hotels	a.anand@centrum.co.in	91-22-4215 9853
Adhidev Chattopadhyay	Analyst	Real Estate	adhidev@centrum.co.in	91-22-4215 9632
Ankit Kedia	Analyst	Media, FMCG	ankit.kedia@centrum.co.in	91-22-4215 9634
Manish Kayal	Analyst	Infrastructure	manish.kayal@centrum.co.in	91-22-4215 9313
Nitin Padmanabhan	Analyst	Technology	nitin.padmanabhan@centrum.co.in	91-22-4215 9690
Pranshu Mittal	Analyst	Food & Bev, Sugar & Retail	p.mittal@centrum.co.in	91-22-4215 9854
Rajan Kumar	Analyst	Cement	rajan.kumar@centrum.co.in	91-22-4215 9640
Rajagopal Ramanathan	Analyst	Banking & Financial Services	rajagopal.ramanathan@centrum.co.in	91-22-4215 9644
Rohit Ahuja	Analyst	Oil & Gas	rohit.ahuja@centrum.co.in	91-22-4215 9636
Saikiran Pulavarthi	Analyst	Banking & Financial Services	saikiran.pulavarthi@centrum.co.in	91-22-4215 9637
Siddhartha Khemka	Analyst	Logistics	siddhartha.khemka@centrum.co.in	91-22-4215 9857
Sriram Rathi	Analyst	Pharmaceuticals	s.rathi@centrum.co.in	91-22-4215 9643
Amit Sinha	Associate	Power, Capital Goods	amit.sinha@centrum.co.in	91-22-4215 9927
Janhavi Prabhu	Associate	Food & Bev, Sugar, Retail	janhavi.prabhu@centrum.co.in	91-22-4215 9864
Jatin Damania	Associate	Metals & Mining, Pipes	jatin.damania@centrum.co.in	91-22-4215 9647
Komal Taparia	Associate	Economy & Strategy	komal.taparia@centrum.co.in	91-22-4215 9195
Rahul Gaggar	Associate	Hotels, Healthcare	rahul.gaggar@centrum.co.in	91-22-4215 9683
Sarika Dumbre	Associate	Telecom	sarika.dumbre@centrum.co.in	91-22-4215 9194
Shweta Mane	Associate	Banking & Financial Services	shweta.mane@centrum.co.in	91-22-4215 9928
Vijay Nara	Associate	Automobiles/Auto Ancillaries	vijay.nara@centrum.co.in	91-22-4215 9641

**Sales**

V. Krishnan		+91-22-4215 9658	v.krishnan@centrum.co.in	+91 98216 23870
Ashish Tapuriah		+91-22-4215 9675	ashish.tapuriah@centrum.co.in	+91 99675 44060
Ashvin Patil		+91-22-4215 9866	ashvin.patil@centrum.co.in	+91 98338 92012
Siddharth Batra		+91-22-4215 9863	s.batra@centrum.co.in	+91 99202 63525

**Centrum Securities (Europe) Ltd., UK**

Dan Harwood	CEO	+44-7830-134859	dan.harwood@centrum.co.in
Michael Orme	Global Strategist	+44 (0) 775 145 2198	michael.orme@centrum.co.in

**Centrum Securities LLC, USA**

Melrick D'Souza	+1-646-701-4465	melrick.dsouza@centrumsecurities.com
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**PMS REGISTRATION NO.:** INP000000456  
**Website:** www.centrum.co.in  
**Investor Grievance Email ID:** investor.grievances@centrum.co.in

**REGD. OFFICE Address**

Bombay Mutual Bldg., 2nd Floor, Dr. D. N. Road, Fort, Mumbai - 400 001

**Correspondence Address**

Centrum House, 6th Floor, CST Road, Near Vidya Nagari Marg, Kalina, Santacruz (E), Mumbai 400 098.  
Tel: (022) 4215 9000