

July 22, 2008

Rating	Not Rated
Price	Rs193
Target Price	NA
Implied Upside	NA
Sensex	13,850

(Prices as on July 22, 2008)

Trading Data

Market Cap. (Rs bn)	83.8
Shares o/s (m)	433.6
Free Float	58.5%
3M Avg. Daily Vol ('000)	265.1
3M Avg. Daily Value (Rs m)	58.0

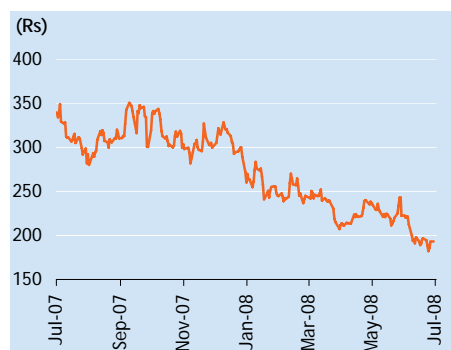
Major Shareholders

Promoters	41.5%
Foreign	26.0%
Domestic Inst.	21.1%
Public & Others	11.4%

Stock Performance

(%)	1M	6M	12M
Absolute	(10.4)	(23.5)	(39.8)
Relative	(6.3)	(7.1)	(29.6)

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



Source: Bloomberg

■ **Down, not out:** Zee TV continues to remain a strong #2, despite GRPs which is at their 52-week lows. With the recent launch of *SaReGaMaPa*'s new season, we expect its ratings to improve going forward and peak during Q4FY09E. This could positively impact ad. revenue going forward.

■ **Increasingly competitive landscape:** FY08 witnessed the launch of two new Hindi GECs (*9X* & *NDTV Imagine*), as also will FY09E with Viacom 18's *Colors* and Turner Miditech's venture. The management does not discount the new entrants' capabilities, however, we maintain that they are still single programme wonders and they have to prove their mettle with a consistent content line-up.

■ **Possibility of slowdown in ad. spend:** The management does not rule out the possibility of ad. budget cuts by clients, in view of the prevailing economic scenario; however, it believes that TV as a medium still guarantees greater reach and viewership, and hence will continue to grow from the losses of other mediums.

■ **Our take:** We continue to remain positive on the prospects of the broadcasting sector from a long-term (18-24 months) perspective, and believe the incumbents will stand to benefit from recent development such as increasing digitisation and competition. However, FY09E would see pressure on ad. spend, given the current economic scenario, hence growth would largely be driven by subscription revenue. We have built in 14% CAGR FY08-10E in revenue, margins are expected to expand by 160bps over FY08-10E, and as a result earnings are expected to grow at 14% CAGR FY08-10E. Though our numbers don't reflect our optimism, we expect the company's performance in H2FY09E to positively surprise us with improvement in ratings of Zee TV (which accounts for 50% of ad. revenue).

Key financials (Y/e March)	FY08	FY09E	FY10E	FY11E
Revenue (Rs m)	18,354	21,317	23,927	26,638
Growth (%)	21.1	16.1	12.2	11.3
EBITDA (Rs m)	5,423	6,154	7,448	8,468
PAT (Rs m)	3,833	4,412	4,951	5,516
EPS (Rs)	8.8	10.1	11.4	12.7
Growth (%)	61.4	15.1	12.2	11.4
Net DPS (Rs)	2.0	2.3	2.5	2.5

Source: Company Data; PL Research

Profitability & valuation	FY08	FY09E	FY10E	FY11E
EBITDA margin (%)	29.5	28.9	31.1	31.8
RoE (%)	14.0	14.6	14.7	14.6
RoCE (%)	13.6	15.0	13.8	13.7
EV / sales (x)	4.7	3.9	3.4	2.9
EV / EBITDA (x)	15.9	13.7	10.9	9.1
PE (x)	21.9	19.1	17.0	15.3
P / BV (x)	2.9	2.6	2.4	2.1
Net dividend yield (%)	1.0	1.2	1.3	1.3

Source: Company Data; PL Research

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Below are the key takeaways from our meeting with the management:

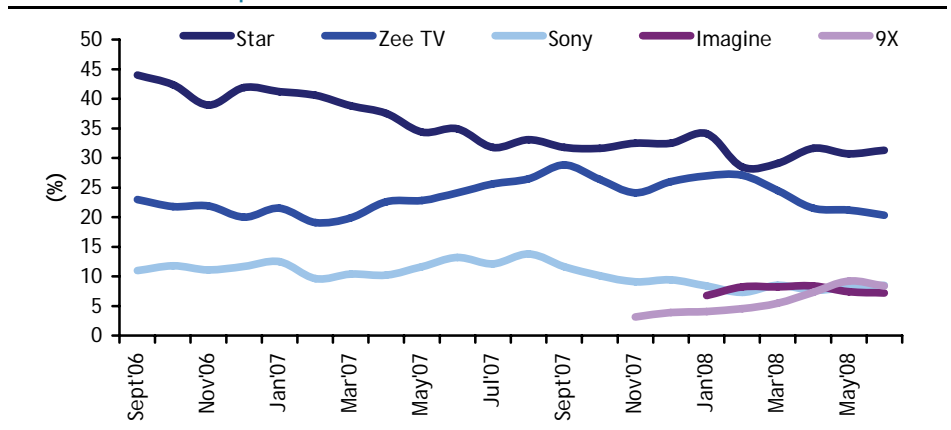
Industry

- The advertisement industry is expected to grow at 15-18%; whereas subscription revenue for the industry is likely to grow by 10-15% YoY.
- The management sees no immediate impact of the economic slowdown; the last time around (2001-02) TV as a medium saw an increase in ad. spend as against other mediums of advertising. However, in our view H2FY09E would be the true barometer of the same; we do not rule out a cut in ad. budgets.
- IPL did impact viewership; however, it will have marginal impact on ad. revenues of the genre. GRPs for the genre remains constant at 1050-1100 for the last six months.

Company

- *Zee TV* has maintained #2 position in the Hindi GEC space, whereas *Zee Cinema* continues to maintain its pole position in the movie channel genre. (*Sony Max* was #1 during IPL, however, on normalised basis *Zee Cinema* still is #1).

Hindi GEC viewership share



Source: Telepedia, C&S4+ HSM All Day

- *Zee Next*, the company's flanking channel to *Zee TV* will undergo a vertical split effective July 2008; this will improve operating metrics of the company for the remainder of FY09E. In Q1FY09 the company will book a loss of Rs500m on account of *Zee Next*.



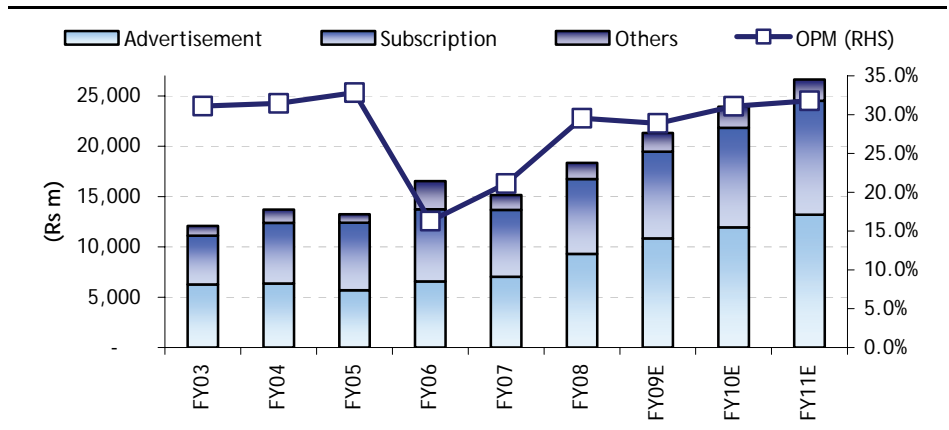
- Zee Entertainment Studios, the company's newly formed subsidiary, plans to produce/co-produce 33 films in FY09E. Twenty films are already on the floor. It plans to invest about Rs80-100m on Hindi movies and about Rs15-20m on regional films.
- Ad. revenue to grow on account of both realisations growth and volume expansion (expansion of prime time slots, weekends and afternoon slots). The management has guided for 25% YoY growth in ad. revenue.
- Subscription revenue has been guided to grow at 15-20% on the back of increasing DTH revenue and international pay revenue.
- The management has guided for 37% YoY growth in operating profit for FY09E.
- The company will incur a forex loss of about Rs450m during FY09E; however, this loss will be more than set-off by an amount (Rs570m) the company claims to have won in litigation.

Financials

We expect Zee Entertainment Enterprises' (ZEEL) total revenue to grow at 14% CAGR FY08-10E, while building in a slight slowdown in FY09E, with ad. revenue likely to grow at 13% CAGR from Rs9.31bn to Rs11.94bn. However, subscription revenue is expected to grow faster at 16% CAGR on the back of increasing DTH and international revenue from Rs7.44bn to Rs10bn.

Revenue mix				(Rs m)	
Y/e March	FY07	FY08	FY09E	FY10E	FY11E
Advertisement	7,035	9,307	10,843	11,939	13,201
<i>% of revenues</i>	<i>46.4</i>	<i>50.7</i>	<i>50.9</i>	<i>50.1</i>	<i>49.6</i>
<i>YoY gr. (%)</i>	<i>-</i>	<i>32.3</i>	<i>16.5</i>	<i>10.1</i>	<i>10.6</i>
Subscription	6,648	7,436	8,622	9,897	11,311
<i>% of revenues</i>	<i>43.9</i>	<i>40.5</i>	<i>40.4</i>	<i>41.5</i>	<i>42.5</i>
<i>YoY gr. (%)</i>	<i>-</i>	<i>11.9</i>	<i>16.0</i>	<i>14.8</i>	<i>14.3</i>
Others	1,476	1,611	1,852	2,003	2,126
<i>% of revenues</i>	<i>9.7</i>	<i>8.8</i>	<i>8.7</i>	<i>8.4</i>	<i>8.0</i>
<i>YoY gr. (%)</i>	<i>-</i>	<i>9.1</i>	<i>15.0</i>	<i>8.1</i>	<i>6.1</i>
Total Revenues	15,159	18,354	21,317	23,839	26,638
<i>YoY gr. (%)</i>	<i>-</i>	<i>21.1</i>	<i>16.1</i>	<i>11.8</i>	<i>11.7</i>

Revenue & OPM trends



Source: Company Data, PL Research

Margins over FY08-10E are expected to expand by 160bps, however, in FY09E we expect them to decline by 60bps to 28.9% on account of losses booked on *Zee Next* (Rs500m), and we believe that stagnant/declining GRPs during H1CY08 will also limit the company's leverage on ad. revenue.

Earnings are expected to grow at 14% CAGR FY08-10E from Rs3.8bn to Rs4.95bn. During FY09E the company will account for a forex loss and an amount of litigation win.

Outlook & valuation

We continue to remain positive on the prospects of the broadcasting sector from a long term (18-24 months) perspective, and believe the incumbents will stand to benefit from recent developments such as increasing digitisation and competition. However, FY09E would witness pressure on ad. spends given the current economic scenario, hence growth would be largely driven by subscription revenue.

Specific to ZEEL, we believe that its ratings (GRPs for *Zee TV*) have not done much during H1CY08, however, H2CY08 could positively surprise given the company launched its new season of *SaReGaMaPa*, which happened to be one of its key programmes last year. We believe that the stock price currently builds in for the lower ratings, hence any improvement in ratings on account of *SaReGaMaPa* or newer content lined up, will positively impact ZEEL. Also increasing DTH backed subscription revenue will continue with newer service providers (Reliance communication, Bharti and Videocon) expected to launch their respective services during FY09E. Margins, despite a decline in FY09E, are expected to prop-up in FY10E to 31%, an expansion of 160bps over FY08. As a result we expect the company to post 14% CAGR FY08-10E in earnings.

Income Statement (Rs m)

Y/e March	FY07	FY08	FY09E	FY10E	FY11E
Revenue	15,159	18,354	21,317	23,927	26,638
<i>YoY growth (%)</i>	<i>(8.4)</i>	<i>21.1</i>	<i>16.1</i>	<i>12.2</i>	<i>11.3</i>
Operating exp.	11,955	12,931	15,163	16,479	18,170
Operating profit	3,204	5,423	6,154	7,448	8,468
<i>Margin (%)</i>	<i>21.1</i>	<i>29.5</i>	<i>28.9</i>	<i>31.1</i>	<i>31.8</i>
Other income	747	1,138	960	978	1,063
EBITDA	3,951	6,561	7,115	8,426	9,530
Depreciation	185	232	254	281	304
Interest	334	516	835	276	225
Profit before tax	3,432	5,813	6,025	7,869	9,002
Tax	999	1,627	1,808	2,518	3,061
Exceptional / MI	58	354	(194)	400	425
Profit after tax	2,375	3,833	4,412	4,951	5,516
<i>Margin (%)</i>	<i>15.7</i>	<i>20.9</i>	<i>20.7</i>	<i>20.7</i>	<i>20.7</i>

Balance Sheet (Rs m)

Y/e March	FY07	FY08	FY09E	FY10E	FY11E
Source of funds					
Equity share capital	434	434	434	434	434
Reserves	25,747	28,177	31,448	35,130	39,379
Shareholders funds	26,181	28,611	31,881	35,564	39,812
Total debt	3,226	3,866	2,866	2,153	2,131
Minority interest	819	1,117	1,497	1,897	2,322
Total	30,225	33,594	36,244	39,615	44,265
Application of funds					
Gross block	15,702	16,225	17,644	18,594	19,344
Depreciation	1,081	1,239	1,493	1,774	2,077
Net fixed assets	14,622	14,986	16,151	16,820	17,267
Capital WIP	219	619	-	-	-
Deferred tax assets	75	243	243	243	243
Investments	2,326	2,515	3,515	3,515	3,515
Program & film rights	2,016	2,442	2,579	2,720	3,168
Inventories	24	32	85	46	100
Sundry debtors	5,331	5,907	6,716	7,211	7,663
Cash	955	1,652	2,616	4,938	8,529
Loans & advances	9,762	11,475	11,475	11,475	11,475
Current assets	18,088	21,508	23,471	26,391	30,935
Current liabilities	5,106	6,279	7,137	7,355	7,696
Net current assets	12,981	15,230	16,334	19,036	23,240
Misc. exp	2	-	-	-	-
Total	30,225	33,594	36,244	39,615	44,265



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PL's Recommendation Nomenclature

BUY	: > 15% Outperformance to BSE Sensex	Outperformer (OP)	: 5 to 15% Outperformance to Sensex
Market Performer (MP)	: -5 to 5% of Sensex Movement	Underperformer (UP)	: -5 to -15% of Underperformance to Sensex
Sell	: <-15% Relative to Sensex		
Not Rated (NR)	: No specific call on the stock	Under Review (UR)	: Rating likely to change shortly

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