Indian Cable & Satellite Space

Encrypting Value

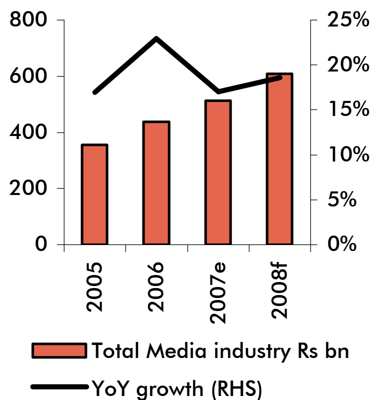
Indian C&S space to unlock tremendous value through digitization & consolidation: The Indian cable & satellite (C&S) space is valued at Rs167bn, growing at a brisk pace of ~22% p.a. Despite being the largest segment in the Indian Media & Entertainment industry, almost all players within the space have been suffering losses due to lack of addressability in the analogue transmission mode and high level of fragmentation as a result of low entry barriers. However, the space is all set for a phase of sustained digitization and consolidation led by consumer demand for quality and technology making it affordable. We believe that half of India's C&S homes will be converted to digital by 2015, creating one of the world's largest digital subscriber base.

Balance of power shifting towards MSOs and DTH players: As the distribution space goes digital, power will shift from the local cable operators, who have enjoyed a virtual monopoly until now, to DTH players and Multi System Operators (MSOs) who have the ability to invest in digital infrastructure. We believe that of the overall subscription revenues generated in the TV distribution space, 65% will be in digital mode, creating tremendous value for players in the space.

Digital penetration to be driven by subsidies: We believe that due to lack of any differentiation among offerings of various players coupled with consumer preference towards low priced offerings at present, subscriber acquisition will be increasingly driven by price based competition. This will create a high entry barrier within the space in the form of high funding requirements. However, we believe that as players become more invested in the space and attain critical size of ~5-6mn subscribers, value added services would improve the chances for higher ARPUs.

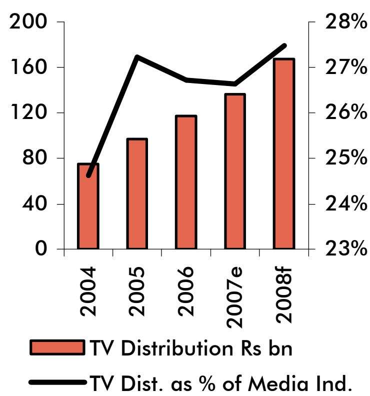
Initiating coverage on WWIL and Dish TV: We believe that the long term fundamentals of the space are sound and will provide value creating opportunities for players with the capacity to fund expansion and the ability to manage large B2C networks. We intiate coverage on Dish TV and WWIL, both leaders in their respective space, with a '**BUY**' recommendation and target price of Rs20.3 and Rs15.3 respectively.

M&E Industry growth in double digit



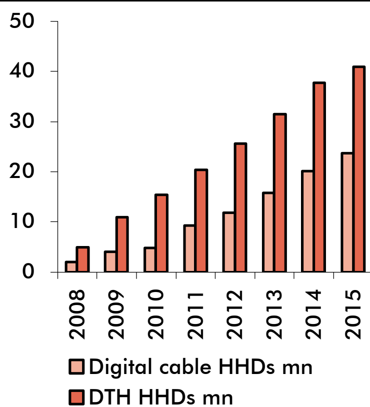
Source: PWC

TV Dist. - largest chunk in M&E ind.



Source: PWC

Digital HHDs to reach 65mn by 2015



Source: Ambit Capital Research

Valuation summary

	Dish TV	WWIL
CMP (Rs)	15.0	9.3
Target Price (Rs)	20.3	15.3
Recommendation	BUY	BUY
Upside (%)	36	64
MCap/Sales - FY09E (x)	2.0	0.6
MCap/Sales - FY10E (x)	1.3	0.4
EV/Sales - FY09E (x)	3.1	3.7
EV/Sales - FY10E (x)	2.0	2.3

Source: Ambit Capital Research

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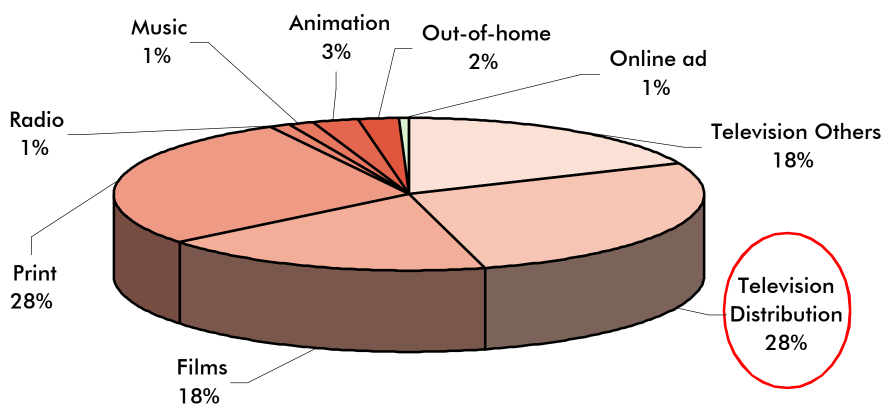
Indian C&S Space - the largest & growing

The Indian cable and satellite space (C&S space) comprises of delivery of TV signals to consumers through cable, satellite or broadband. The industry is a decade and a half old, third largest in the world in terms of cable network reach, and highly fragmented and unorganized because of low entry barriers in the analogue mode. The C&S distribution segment is the last leg in the television industry's value chain which comprises of content producers, broadcasters, Multi System Operators (MSOs), Local Cable Operators (LCOs) and satellite players. Even though the sector comprises 28% of the total entertainment and media industry and is growing at 22% per annum, most of the value creation is being cornered by the LCOs due to lack of addressability in the value chain. However, we believe that the sector is all set to witness disruptive change brought through technology, which will shift the balance of power towards MSOs and DTH players, unlocking huge value for operators in this space.

The Indian C&S space contributes 28% of the total Media and Entertainment industry, growing at 22% p.a.

Media and Entertainment Industry - Segment-wise break-up 2008



Source: PWC

Increasing C&S penetration driving growth

	FY02	FY03	FY05	FY06
C&S HHDs (mn)	38	40	60	68
C&S Growth (%)	30	7	36	13
ARPU (Rs./sub/month)	102	120	150	150
Consumer Spend (Rs bn)	3,866	4,848	9,000	10,200
Broadcaster earning (Rs bn)	557	873	1,296	1,417

Source: NRS

Indian C&S - Present Scenario

Fragmented value chain

The Indian C&S space is highly fragmented, leaving little value for individual operators

Since cable networks have grown in a largely unregulated environment, this has translated into a highly fragmented value chain comprising of around 7,000 Multi System operators (MSOs) who receive TV signals from broadcasters, and an estimated 60,000 LCOs, who in turn receive these signals from MSOs and distribute to the consumer through their cable network. The revenue flow is in reverse, the LCO collects cable charges from the customers, pays the MSO his negotiated share, and MSO in turn shares the proceeds with the broadcaster.

As compared to the US, where top 5 MSOs control 80% of the total video subscribers, in India, the top 5 operators control only ~20% of the market. We believe that here in lies a huge opportunity for consolidation in this industry, which has already begun in parts.

80% of US cable space controlled by 5 MSOs

MSO	Basic Video	Subscribers	Rank
Comcast Cable Communications	24,553,000	38%	1
Time Warner Cable	13,297,000	20%	2
Cox Communications(e)	5,403,740	8%	3
Charter Communications	5,162,000	8%	4
Cablevision Systems	3,132,000	5%	5
Total	51,547,740	80%	

Source: NCTA

LCOs hold the last mile - tremendous bargaining power

Many MSOs - one LCO

Given the high bargaining power of the local cable operator in the analog distribution mode, LCOs have been cornering the lion's share of subscription revenues

Throughout the 90s, cable TV growth has been tremendous, and the sole fuel power behind this has been the entrepreneurship of the local cable operator. LCO owns the last mile network and has access to the customer homes. Since cable is a natural monopoly, usually there exists only one LCO per area. As the MSO has to send his signals through the LCO network, he has to deal with the LCO in each locality in which he wants to be present. This results in many MSOs vying for the same LCO network in order to reach the consumer, which gives the LCO tremendous bargaining power in deciding his share out of the cable subscription revenues.

Low switching costs in the analogue mode

In the analogue mode, it is very easy for an LCO to switch from one MSO to another simply by changing cable feed that he receives from the MSO. Since all MSOs provide almost the same content and there is no change at the customer's end, the MSOs' competitive positioning is weakened to a large extent while entering in to negotiations with LCOs to decide subscription revenue sharing agreements.

Underpayment based on negotiated subscriber base

This gives rise to underpayment by LCO which gets translated into lower subscription revenues for the MSO and in turn for the broadcaster. It is important to note that there exist significant economies of scale for the MSO; the larger the subscriber base, the greater is carriage fee charged from the broadcaster. Hence, multiple MSOs try and woo the same cable operator through undercutting each other by agreeing to charge for fewer households than the LCO actually services. This is the sole reason for the dismal performance of all players in the value chain, despite being present in the largest segment of the Indian media industry (television is 46% of the total industry, and growing at 21% per annum on average).

TV distribution; the largest and growing at a brisk pace

	2004	2005	2006	2007	2008
Total Media industry (Rs bn)	305	356	438	513	608
YoY growth (%)		17	23	17	19
Total Television industry (Rs bn)	129	159	191	226	278
YoY growth (%)		23	21	18	23
Television Distribution (Rs bn)	75	97	117	137	167
TV Distribution as % of M&E Ind.	25	27	27	27	27

Source: PWC

Unprofessional LCO - dissatisfied customers

High fragmentation at the multi-system operators' end coupled with high bargaining power of LCOs is leaving very little on the table for MSOs

Since LCO enjoys local monopoly, most of the time he takes customers for granted. The condition of cable networks is not very good in most areas because of low investments in the upgradation giving rise to very poor signal reception and frequent blackouts at the consumer's end. On the other hand, cable bill has been rising year on year, leaving the consumer very dissatisfied. This dissatisfaction can be easily gauged by the huge consumer acceptance of an alternative distribution channel, DTH.

MSOs left with nothing - surviving on carriage fee

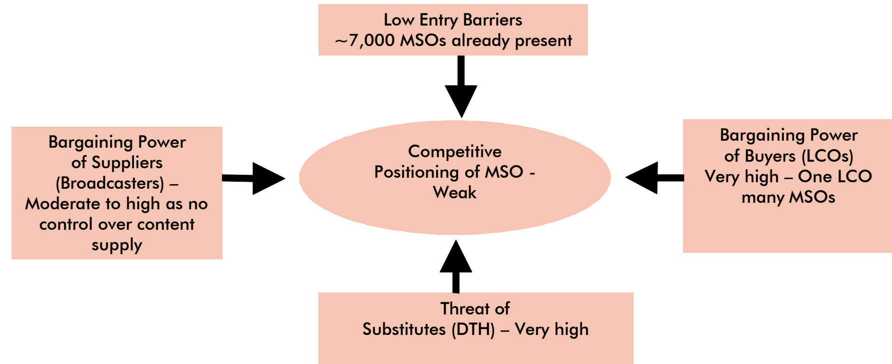
By investing in the head ends, MSO acts as a content aggregator from different broadcasters and content distributor to multiple LCOs. For this, he collects cable charges from different LCOs and pays to the broadcasters after retaining 5%-10%. Other revenue streams are carriage fee and advertising revenues from the local cable channels.

Due to lack of clarity about the exact number of viewers of a particular channel, MSOs pay the broadcasters on the basis of negotiated subscriber base and not on the per subscriber basis. Since the bargaining power of broadcaster has increased because of their bouquet offering e.g. One alliance, Zee-turner etc., the MSO ends up paying almost all of the subscription revenues that he receives from the LCOs or faces channel blackout from the broadcasters.

The only significant revenue stream for MSOs is carriage fee, which is a type of right of usage fee paid by the broadcasters to have their channels placed in the MSO network. Since the network capacity in the analogue mode is limited while the number of channels are increasing, carriage fee has emerged as a significant source of revenue for the MSO.

Understanding industry dynamics through Porter's Model (from MSO's perspective)

Our analysis of the MSO space on the Porter framework suggests that the space is highly competitive



Bargain power of suppliers (broadcasters) - moderate to high; though provider of content, has to depend on the cable networks to distribute it since there is no other meaningful alternative as of now.

Bargaining power of LCO (switching costs for LCOs) - High, since there is zero switching cost for an LCO from one MSO to another.

Threat of entry barriers (number of MSOs) - High, 7,000 MSOs vying for the same LCO

Threat of substitutes (DTH) - High; DTH penetration has risen tremendously in past two years.

Overall opinion - moderate to high competition

Source: Ambit Capital Research

We believe that the cable industry is a very good example of a sector which holds great overall revenue potential, but none of the incumbents is able to benefit from it because of low entry barriers and high bargaining power of the customer (LCO). This analysis explains the poor performance of all other players in the value chain except for the LCO.

C&S Space - On the verge of revolution

We believe that TV distribution will witness a fundamental shift in its operating model in the next few years, because of the reasons given below. The space is all set to become organized unlocking huge value for broadcasters, MSOs and DTH players.

Change no 1 - World going digital

Higher addressibility and better quality are increasingly driving digitization in the C&S universe globally

Analogue cable networks are giving way to the digital mode the world over due to better technology. Digital TV distribution mode is able to carry far more channels due to advanced compression technology than the analogue mode. As the number of channels keep on increasing, this becomes more and more relevant for the consumer. Moreover, there is a huge scope for delivering value added services like HD channels, VoIP, video on demand, broadband and pay per view through digital mode, attracting investments in the sector. Various countries have fixed target dates for converting their TV transmission to digital, showing favorable regulatory regime due to increased addressability.

Because of the inherent addressability in the digital mode of TV signal distribution, it attracts organized funding despite being highly capex intensive, as the investment viability can be easily gauged. Moreover, it also creates high switching costs for the local cable operator and the consumer because of the presence of advanced decrypting equipments needed for receiving digital signals.

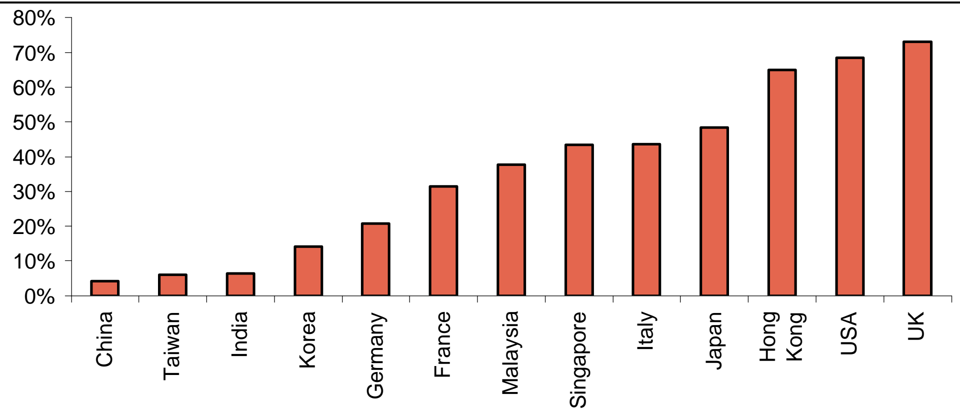
We believe that both the push and the pull towards digital transmission will be key drivers of consolidation within India's huge unorganized cable market. As the industry moves towards digitization, the revenue share will shift more and more from the local cable operators towards the multi system operators and broadcasters.

Analog switch off deadlines

2009 - USA,
2011 - Japan,
2012 - Hong Kong, UK
2015 - Malaysia, Singapore,China

Source: CASBAA

Digital Cable Penetration - Country-wise



Source: CASBAA

Change no 2 - India all set to become a DTH market

DTH penetration is on an aggressive rise throughout the country mainly because of 5 very strong players in this space who have deep pockets and nationwide sales network. These 5 players are spending close to Rs6bn on advertisement alone creating awareness about the product and expanding the market in the process. Coupled with this is the general dissatisfaction of the consumers with analogue cable, which is behind such an encouraging response to a totally new technology in the country.

We believe that the DTH subscriber base will reach 41mn by 2015 at the very least because of two main reasons;

The first round of digitization race will go to the DTH platform because of the presence of 5 very strong players as compared to none in the digital cable space.

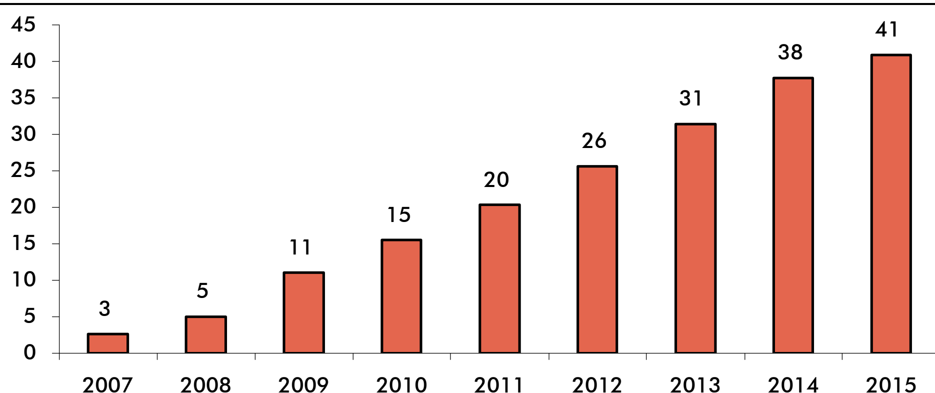
1. Each player in the DTH space is capable of competing on all four parameters of effective DTH service viz. Brand, Distribution Reach, Service, and most importantly Price. As every one is on par, it also means that there exists no competitive advantage for any player to compete on. Combine this with the fact that the consumer has shown huge response to the low priced schemes (The Rs999 Sun package and Free STB scheme launched by Dish TV in October), and it is clear that customer acquisition will be driven by subsidies only.

   In the absence of any significant differentiation apart from pricing, we believe that ARPUs will remain depressed till each player gains significant size (5-6mn), as players try to compete on price. Since each player wants to get there faster than others, this will lead to highly subsidized offerings for the consumer leading to aggressive market expansion.

DTH market is expected to be 41mn subscribers strong by 2015.

2. There is simply no one on the cable side to counter the DTH threat posed by the likes of Bharti and Big TV at present. Contrary to the DTH players, the cable space, being highly unorganized, lacks access to capital markets. As cable is not recognized as an industry, organized funding from banks is also very difficult. Hence, apart from the 4 leading MSOs, there exists very little competition from the cable side giving DTH players a free run.

India to have 41mn DTH Subscribers by 2015



Source: Industry, Ambit Capital Research

Changing rules of the game - LCO network rendered irrelevant

Aggressive DTH expansion is leading to serious erosion of LCO subscriber base; as more consumers opt for digital mode, his analogue network is becoming redundant resulting in weak bargaining power.

This has worried LCOs a lot as they have been losing their quality customer base at a very fast pace. Since DTH is a direct substitute to the cable networks, rising acceptance of DTH platform has rendered the cable distribution system useless along with its owners, the LCOs. As LCOs are mostly dependent on the cable networks for their existence, we are likely to see the LCO's hold on the last mile loosening in the near future.

We believe that the current developments in the space will have great implications for all the players in the value chain. We expect the space to become more organized and consolidated in the years to come, benefiting the broadcasters and large MSOs.

How the Value will be Encrypted

Given the current macro changes happening in the space, we have tried to understand their implications on the MSOs. We believe that the current digitization wave will present a Rs29bn opportunity for the bigger MSOs and we expect pan-India players like WWIL, InCable, DigiCable, and Hathway to benefit from it.

Market opportunity for the leading MSOs by 2012

Total C&S HHDs by 2012 (mn)	110
DTH HHDs (mn)	26
Rest (mn)	80
Digital Cable Share (%)	11
Digital Cable HHDs (mn)	12
ARPU (Rs)	250
Size of the market (Rs bn)	36.3
Share of Top 4 MSOs (%)	80
Opportunity for top 4 MSOs (Rs bn)	29

Source: Ambit Capital Research

DTH - a great 'friend' of MSOs in the short term

Interestingly, DTH has emerged as the best thing that has happened to the cable industry since its inception. The dominant power enjoyed by LCOs because of lack of any substitute had resulted in very weak competitive positioning of MSOs in the TV distribution value chain. Throughout the years, MSOs have lost money and had to depend on just the carriage fee for survival, while LCOs pocketed subscription money from as many as 85% of the subscribers in their areas.

The emergence of DTH as a strong substitute of cable networks has changed the rules of the game almost overnight, making LCO, the strongest player in the value chain, the weakest in the process. The only way to counter the DTH threat is to provide affordable digital cable, which is a highly capital intensive proposition. LCOs mostly being single proprietorship firms, lack the wherewithal to make their networks digital.

LCOs to turn to MSOs to counter the threat

MSOs with the ability and willingness to upgrade LCO networks to digital will be able to own the last mile without incurring any acquisition cost

We believe that DTH will force LCOs to collaborate with the MSOs to counter the threat. The large MSOs, who have the capacity to make the required investments in infrastructure, will be key beneficiaries of this trend as MSOs are willing to incur the STB seeding and infrastructure upgrading costs for an LCO network only if LCOs are willing to pay for all the subscribers covered, and LCOs are running out of choice.

These are the best times for MSOs as they will have the opportunity to own the last mile without actually paying for anything. We are of the opinion that instead of buying out the LCO networks, which is very costly, MSOs will simply wait until the LCOs themselves offer their networks in return for a revenue sharing agreement.

Digital Network creates dependency - raises switching costs

The analogue networks are fraught with very high churn rate because of very low switching costs from one MSO to another for the LCO. This is the sole reason for dismal financial performance of the MSOs. However, this is set to change with the penetration of digital cable for two reasons.

One, it is not easy to replace an MSO in the digital mode as it requires replacing the digital head-end, backbone fiber, and the set top boxes for the entire subscriber base. Two, since the set top boxes are installed at the customer premises, changes are required at the customer's end also, complicating the operation further. These two reasons will bring the churn rate down substantially, encouraging MSOs to invest in the infrastructure.

Opportunity in adversity for MSOs

We believe that there exists great scope for MSOs to capitalize on the current opportunity that the changing business model of the cable TV distribution space is offering. However, only those players who have the required capital to digitize the existing cable infrastructure and the technology to counter the DTH offerings will have a shot at the current opportunity. It is estimated that Rs1000 per subscriber is required to subsidize the digital box and another Rs2000 to make the cable network two-way (required to offer broadband through cable).

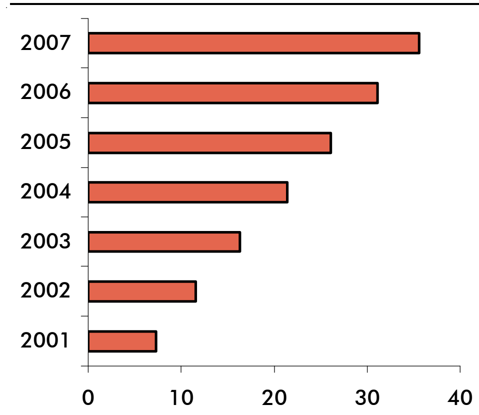
MSOs with deep pockets and the capability of managing large B2C networks will emerge as winners after the consolidation phase is over

This is where deep pockets will differentiate the winners from the laggards. Acquiring direct customers, seeding STBs for digital services, and upgrading networks to make it two-way for broadband offerings require huge investments and long payback period. MSOs with the required financial muscle and the ability to manage large B2C networks (as against the earlier B2B business model) will emerge as the winners in this race.

Last mile ownership - the real jewel

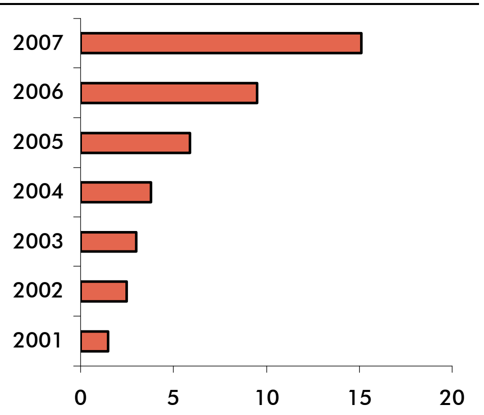
Digital cable has a significant advantage over satellite TV (DTH) mainly because of its ability to offer true two way connectivity, which is required for offering value added services like video on demand, broadband, pay per view and Voice over Internet Protocol. In the US for example, the subscriber base for value added services through cable, has witnessed a sustained growth over the years leading to rising digital cable subscriber base.

Cable High-speed Internet Customers (US)



Source: NCTA

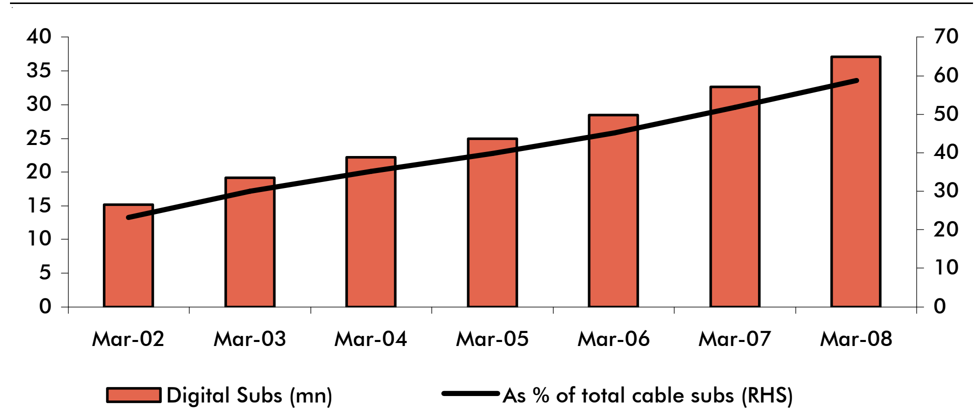
Cable voice Customers (US)



Source: NCTA

Cable scores over other modes of video transmission because of its ability to offer triple play on the same pipe, which helps it price its services in a highly competitive manner.

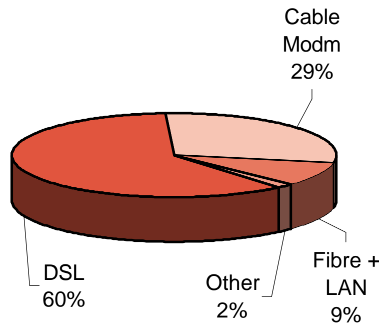
US - Digital cable penetration rising despite competition from Telcos and DBS players



Source: NCTA

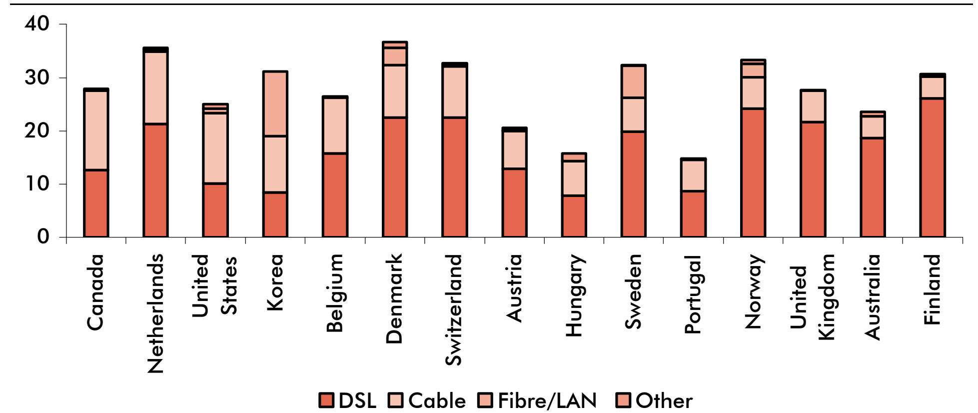
The greatest competitive edge that digital cable holds is its ability to offer bundled up services at a lower rate when compared to the Telcos or the satellite TV players. Since digital cable can offer all three value added services e.g. broadband, VoD, and VoIP, also called triple play, over the same infrastructure, it has effectively countered the threat from telcos, ISPs and satellite TV players allowing it to retain its market share and also expand its bouquet of services in other countries.

OECD Broadband subscriptions, by technology



Source: OECD

OECD Broadband subscribers per 100 inhabitants, by technology, June 2008



Source: OECD

Conclusion

Price based competition in the medium term

The C&S space is expected to witness lots of low priced service offerings in the initial phase leading to subdued ARPU growth. However, low ARPUs will be compensated partially through declining content costs as the operators gain scale.

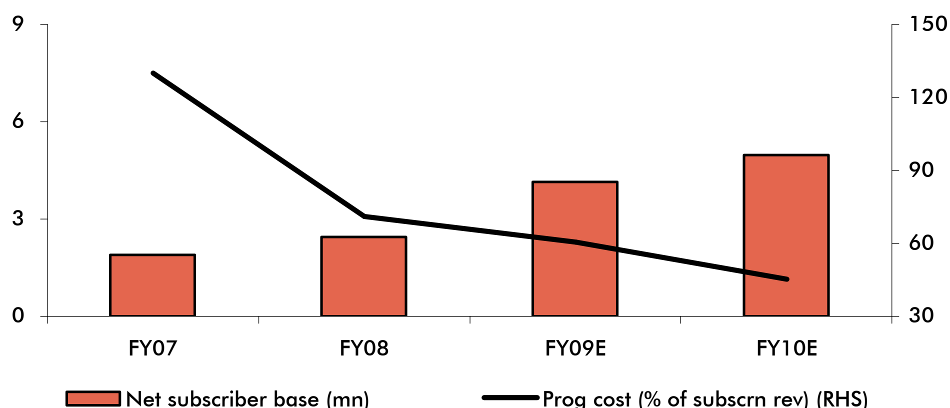
We believe that the cable and DTH space is all set for a prolonged price war for the next 3-4 years. As highlighted earlier, cable and DTH space have a low entry barrier and a large number of players offering the same product i.e. content. This kind of industry is an ideal battleground for price war especially when the players are financially strong and need to build subscriber base to break even.

The price war, started by DTH operators, will spread to the cable space too as the newly emergent MSOs try to defend their turfs (especially more so once they have invested in the digitization of networks). Assessing the current scene in the TV distribution space, we expect that ARPU growth to remain subdued in the next 4-5 years. We would also like to highlight here that ARPUs in other countries have gone up mainly because of exclusive content and value added offerings like video on demand, broadband, pay per view and VoIP.

Broadcasters will compensate for low ARPUs by subsidizing digital platforms

The DTH business model works on a very simple basis; offer STB for free and recover the investment through selling content at a high gross margin. However, we believe that the ongoing fierce price based competition will force DTH players to offer channel packages at highly reduced gross margin, which will delay the break even period to 5-6 years. As the DTH players cannot sustain content subsidy, it becomes imperative for the broadcasters to lower the content costs for this platform. As compared to the analogue mode where content costs are almost equal to the subscription revenues, broadcasters are already subsidizing the DTH players and this will continue for two main reasons;

Content subsidies emerging from scale



Source: Company, Ambit Capital Research

1. The DTH platform is offering broadcasters addressability, something they never got earlier under the analogue mode. If content costs are not lowered to protect DTH margins, DTH platform will lose its appeal and become defunct. Hence, in order to avoid going back to the old under-reporting regime of analogue mode, broadcasters have no choice but to lower the content costs for DTH players.

2. The loss incurred through lower content costs can be offset through higher ad income as the clarity on the exact number of subscribers emerges for broadcasters.

We believe that content costs as a % of subscription revenues are set to slide down for the DTH/ digital cable players and will settle around 40%-45% levels.

Ultimate competition through better offerings and technology

We believe that by 2015, DTH subscriber base will be at 41mn and all 5 existing players would have built up significant scale. Digital cable is expected to reach 24mn subscribers by the same time. As the dust settles and the industry enters a consolidation phase, we believe that ARPUs have a chance to improve through value added offerings. Ultimately, competition will be on the basis of quality of content (we assume that content exclusivity will be allowed), offerings like high definition content (HD channels), digital video recorders, broadband and VoD etc.

Broadcasters, content producers, government and consumers the ultimate winners

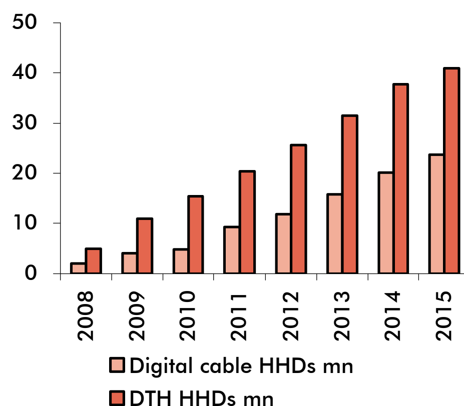
The ultimate beneficiaries of this revolution will be broadcasters and consumers. Broadcasters will benefit through complete addressability which will help them in two ways.

1. The higher revenues generated through better addressability will be fed back into content creation resulting in much improved content pipeline and variety.
2. High number of subscribers will increase advertising revenues and also effectiveness of TV as an advertising vehicle.

Higher disclosure throughout the value chain will result in substantially higher tax revenues for the government. Consumer will be the real king of all, getting huge variety of content at world class quality at highly reduced costs.

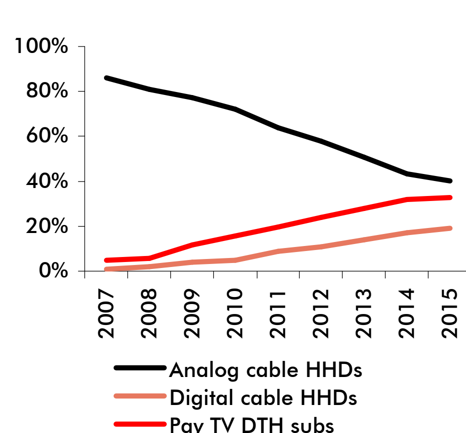
The digital shift is going to be a long drawn and expensive affair involving huge amount of learning for the players. At the end of this, we are likely to a far more consolidated C&S industry with complete clarity on the revenue flow, and emergence of few, very strong MSOs and DTH players.

Digital subscriber base - India (mn)



Source: Ambit Capital Research

Share of subscribers by technology (%)



Source: Ambit Capital Research

Dish TV

'Dish' Karo

Buy

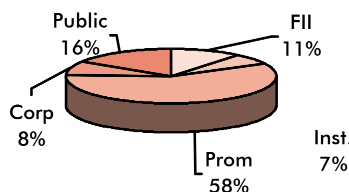
Price	Rs 15.0
Target Price	**%upside**
Rs20.3	36 ↑
Market Capitalisation	
Rs14,148mn	(US$282mn)
52 week range H/L (Rs)	106/12
Shares o/s (mn)	**Daily vol (3m avg)**
946.37	3.38
Reuters	**Bloomberg**
DSTV.BO	DITV IN

Perfm(%)	1M	3M	12M	YTD
Absolute	1.4	(60.8)	(81.8)	(85.4)
Rel. to Sensex	13.5	(32.5)	(59.6)	(66.1)

BSE Sensex	Nifty
8,739	2,658

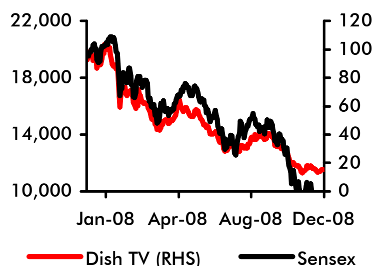
Source: Bloomberg

Shareholding pattern



Source: Capitaline

Price performance



Source: Capitaline

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AMBIT
Acumen at work

Dish TV (India) (Dish TV) is India's largest player in the direct-to-home (DTH) space with a pan-Indian presence in 6,500 cities and a subscriber base close to 4mn. In a market that has recently witnessed the entry of biggies Reliance ADAG and Bharti Airtel, Dish TV has just had its best month in terms of subscriber addition with over 400,000 subscribers added during October.

Investment Rationale

Market leader in an expanding market: We believe that the DTH space will witness explosive growth from 8mn households (as of Oct'08) to 26mn households by FY12E and further to 41mn households by FY15E, resulting in a DTH penetration of 33% of the total C&S households by FY15E. As a market leader within the space, we expect Dish TV to benefit from the growing pie. Despite losing its market share in a furious growth phase, we expect Dish TV to gross a subscriber base of 6.3mn households by FY12E and 8.7mn households by FY15E.

Sound competitive positioning in homogeneous market: We expect the battle for turf on the DTH space to revolve around four critical factors viz brand, technology, reach and pricing. Our comparative analysis of the offerings of all the DTH players suggests that Dish TV is satisfactorily positioned on all four parameters to counter this phase of intense competition while simultaneously maintaining its market share over 20%.

Revenues to multiply 4x over FY08-FY12E: We expect Dish TV revenues to exhibit a 33% CAGR over the period FY09E-FY12E followed by a 18% CAGR during the period FY12E-FY20E, primarily on account of robust net subscriber addition. During the more highly competitive phase between FY09E-FY12E, we expect ARPU growth to be subdued followed by an accelerated ARPU growth (in absolute terms) over the period FY12E-FY20E. Over the period FY08-FY12E, we expect Dish TV revenues to multiply ~4 times from Rs4.1bn to Rs16.5bn.

Valuation and recommendation: The stock has witnessed a steep correction in excess of 80% over the last 12 months as the space has become increasingly crowded. Our numbers also factor in these concerns as far as the competitive nature of the DTH space is concerned. However, we believe that the current market price lends enough comfort from a valuation perspective. We adopt the DCF methodology to value Dish TV with a WACC of 14.5%. We initiate coverage on the stock with a **BUY** recommendation and a DCF-based target price of Rs20.3, indicating an upside of 36%.

Key financials

Year to March (Rs mn)	FY08	FY09E	FY10E	FY11E	FY12E
Operating income	4,122	6,983	10,868	13,743	16,511
EBITDA	(2,090)	(1,820)	156	1,216	1,998
EBITDA mgn (%)	(50.7)	(26.1)	1.4	8.9	12.1
PAT	(4,141)	(4,848)	(3,814)	(3,620)	(3,195)
PAT mgn (%)	(100.5)	(69.4)	(35.1)	(26.3)	(19.3)
EPS (Rs)	(9.7)	(5.1)	(4.0)	(3.8)	(3.4)
P/E (x)	NM	NM	NM	NM	NM
EV/EBITDA (x)	NM	NM	138.7	17.7	10.8
EV/Sales (x)	5.2	3.1	2.0	1.6	1.3

Source: Company, Ambit Capital Research estimates

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Please refer to disclaimer section on the last page for further important disclaimer.

Key financials

Balance sheet

Year to March (Rs mn)	FY08	FY09E	FY10E	FY11E	FY12E
Cash & equivalents	511	956	590	402	345
Debtors	403	503	726	840	947
Inventory	58	70	117	158	201
Loans & advances	1,876	1,696	1,570	1,588	1,607
Fixed assets	9,599	12,218	12,785	11,995	11,293
Total assets	**12,448**	**15,443**	**15,788**	**14,983**	**14,393**
Current liabilities & provisions	11,706	8,932	8,940	8,753	9,355
Debt	5,445	8,284	8,284	11,284	13,284
Other liabilities	8	12	18	20	23
Total liabilities	**17,159**	**17,228**	**17,242**	**20,057**	**22,662**
Shareholders' equity	428	946	946	946	946
Reserves & surpluses	(5,138)	(2,732)	(2,400)	(6,020)	(9,215)
Total networth	**(4,710)**	**(1,786)**	**(1,454)**	**(5,074)**	**(8,269)**
Net working capital	(9,368)	(6,663)	(6,527)	(6,167)	(6,600)
Net debt (cash)	4,934	7,328	7,694	10,882	12,939

Source: Company, Ambit Capital Research estimates

Income statement

Year to March (Rs mn)	FY08	FY09E	FY10E	FY11E	FY12E
Operating income	4,122	6,983	10,868	13,743	16,511
% growth	*115.1*	*69.4*	*55.6*	*26.5*	*20.1*
Operating expenditure	6,212	8,803	10,713	12,527	14,514
EBITDA	(2,090)	(1,820)	156	1,216	1,998
% growth	*-22.5*	*12.9*	*108.5*	*681.9*	*64.3*
Depreciation	1,570	2,404	3,013	3,717	3,781
EBIT	(3,660)	(4,224)	(2,857)	(2,500)	(1,783)
Interest expenditure	513	686	1,056	1,247	1,566
Non-operational income / Exceptional items	39	70	109	137	165
PBT	(4,134)	(4,840)	(3,805)	(3,611)	(3,184)
Tax	7	8	9	10	11
PAT / Net profit	(4,141)	(4,848)	(3,814)	(3,620)	(3,195)
% growth	*(72.5)*	*(17.1)*	*21.3*	*5.1*	*11.7*

Source: Company, Ambit Capital Research estimates

Cash flow statement

Year to March (Rs mn)	FY08	FY09E	FY10E	FY11E	FY12E
EBIT	(3,660)	(4,224)	(2,857)	(2,500)	(1,783)
Other income (expenditure)	39	70	109	137	165
Depreciation	1,570	2,404	3,013	3,717	3,781
Interest	(513)	(686)	(1,056)	(1,247)	(1,566)
Tax	(7)	(8)	(9)	(10)	(11)
Incr (decr) in deferred tax liability	1	4	6	3	3
Incr (decr) in net working capital	(2,323)	2,705	135	361	(434)
Cash flow from operating activities	**(247)**	**(5,145)**	**(931)**	**(262)**	**1,022**
Incr (decr) in capital expenditure	(2,885)	(5,023)	(3,581)	(2,926)	(3,080)
Incr (decr) in investments	0	0	0	0	0
Cash flow from investing activities	**(2,885)**	**(5,023)**	**(3,581)**	**(2,926)**	**(3,080)**
Incr (decr) in borrowings	3,515	2,839	0	3,000	2,000
Issuance of equity	0	7,773	4,145	0	0
Dividend paid	0	0	0	0	0
Others	0	0	0	0	0
Cash flow from financing activities	**3,515**	**10,612**	**4,145**	**3,000**	**2,000**
Net change in cash	383	444	(366)	(188)	(57)
Closing cash balance	511	955	589	401	344

Source: Company, Ambit Capital Research estimates

Ratio analysis

Year to March (%)	FY08	FY09E	FY10E	FY11E	FY12E
EBITDA margin	(50.7)	(26.1)	1.4	8.9	12.1
EBIT margin	(88.8)	(60.5)	(26.3)	(18.2)	(10.8)
Net profit margin	(100.5)	(69.4)	(35.1)	(26.3)	(19.3)
Return on capital employed	NM	NM	NM	NM	NM
Return on equity	NM	NM	NM	NM	NM
Dividend payout ratio	NM	NM	NM	NM	NM

Source: Company, Ambit Capital Research estimates

Valuation parameters

	FY08	FY09E	FY10E	FY11E	FY12E
EPS (Rs)	(9.7)	(5.1)	(4.0)	(3.8)	(3.4)
Diluted EPS (Rs)	(9.7)	(5.1)	(4.0)	(3.8)	(3.4)
Book value per share (Rs)	NM	NM	NM	NM	NM
P/E (x)	NM	NM	NM	NM	NM
P/BV (x)	NM	NM	NM	NM	NM
EV/EBITDA (x)	NM	NM	138.7	17.7	10.8
EV/Sales (x)	5.2	3.1	2.0	1.6	1.3

Source: Company, Ambit Capital Research estimates

Risks and concerns

High funding requirement: Value creation in the DTH space is highly dependent on the pace at which a company seeks to add subscribers. Given the fact that we are likely to witness a phase of intense price-based competition, Dish TV would need to continue burning cash over the next few years while simultaneously building scale. Our subscriber addition assumptions for Dish TV are contingent to the company being able to raise debt to the tune of Rs7.9bn between FY09E and FY13E in addition to the rights issue going through, which is likely to infuse equity to the tune of Rs11.9bn.

Protracted price war: We have built in a 35% increase in set top box subsidies from Rs760 during the current fiscal to Rs1,040 next year. Subscriber addition in excess of our assumptions causing a protracted price war scenario that forces Dish TV into further subsidizing consumer equipment would be a key risk to our valuation thesis.

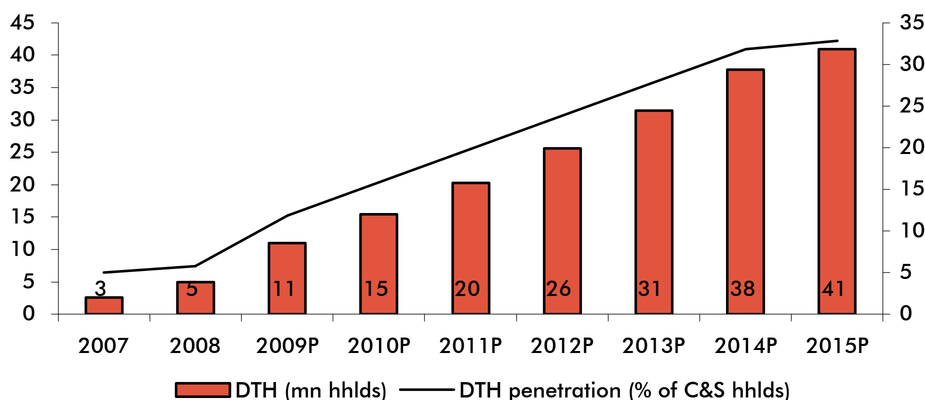
High risk to ARPU growth: Our numbers build in an increase in ARPUs from Rs139 in FY09E to Rs201 by FY12E and further to Rs262 by FY15E. However, ARPUs for Dish TV are not likely to move in isolation and would be a function of competition within the DTH space as well as other competing platforms. Going forward, we firmly believe that Dish TV's ARPUs will also be capped by the movement of ARPUs in digital cable. Though we believe that our assumptions for ARPU movement are conservative, actual ARPUs coming in at even lower levels would be negative for the stock.

Market leader in an expanding market

The DTH market is currently undergoing an explosive growth phase because of the presence of 5 big players with highly aggressive expansion plans. Before the entry of biggies such as Big TV and Digital TV, the DTH market was adding 50,000-60,000 subscribers every month. According to industry estimates, DTH players added 1.2mn subscribers during the month of October, with Dish TV adding 431,253 subscribers, the highest monthly addition in the company's history.

Overall DTH penetration expected to jump from ~8% (as of Sep'08) to 33% by FY15E

DTH penetration - slated for spectacular take-off



Source: TRAI, Ambit Capital Research estimates

No. of DTH HHDs is expected to grow from the current 8mn to 26mn by FY12E and further to 41mn by FY15E.

While we expect to witness a linear CAGR of just over 5% in the television household universe, we believe that the DTH space would kick off at a fairly accelerated pace. We expect the number of DTH households to expand from the current 8mn to 26mn households by 2012 and further to 41mn households by 2015. We also expect DTH penetration to increase from the current single-digit levels to ~24% of the total C&S households by FY12E and further to 33% by FY15E.

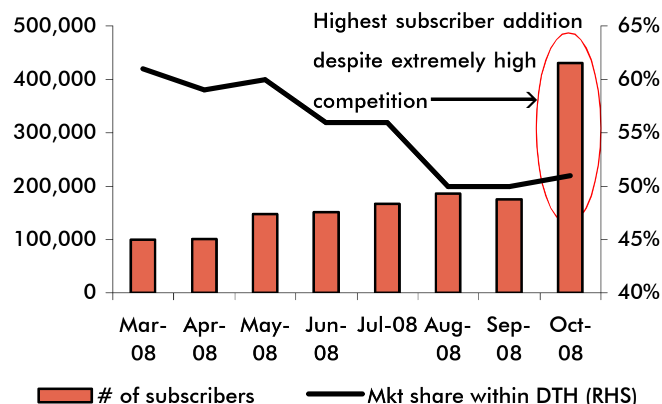
CAGR growth in subscriber base (%)

	FY09E-FY12E	FY12E-FY20E
Total households	2.0	2.0
TV households	4.0	4.0
C&S households	5.0	5.0
DTH households	32.6	10.1

Source: Ambit Capital Research estimates

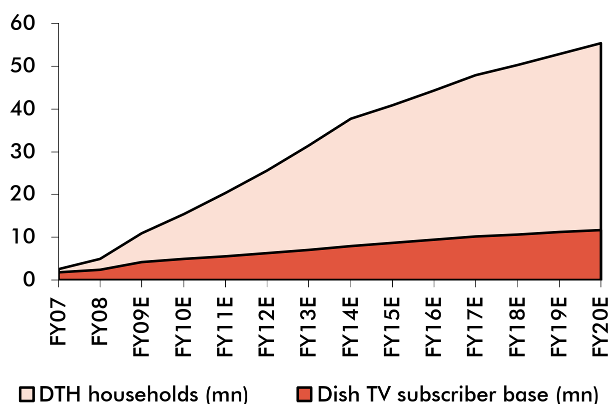
We expect Dish TV to benefit from its leadership positioning and competitive offerings during the market expansion phase over the next 3-4 years. Given the strong competition, however, we expect Dish TV's market share to come down from the current 51% (as of Oct'08) to 24% by FY12E. We expect the Dish TV subscriber base to exhibit an accelerated 15% CAGR over the period FY09E-FY12E followed by a comparatively subdued 8% CAGR over the period FY12E-FY20E.

Dish TV monthly subscriber addition



Source: Company

Dish TV subscriber addition vis-a-vis overall DTH market



Source: Company, Ambit Capital Research estimates

Well placed to counter competition

DTH, being a pull market product, competes on all four Ps in order to get customer attention viz product, place, promotion and most importantly price. We believe that in the medium term, the former three are going to be mere hygiene factors for the consumer. To get the first buy-in, all players need to match one another's offerings on these points without expecting any competitive edge. As a direct result of this, there will be more and more competition based on the fourth P, i.e. Price. We expect more and more subsidized offerings coming in the market in the medium term as the players strive to achieve scale.

DTH offerings - a comparison

		Dish TV	Tata SKY	BIG TV	Digital TV
Brand	Potential for ad spend	Medium	Medium	High	High
	Celebrity	Shah Rukh Khan	Aamir Khan	No celebrities	A galaxy of stars
Sales & distribution	Reach	6,500 cities		100,000 outlets	62 cities
				across 6,500 towns	
Content	# of channels	205	160	200	130
Technology		MPEG2	MPEG2	MPEG4	MPEG4
Pricing	Entry level - basic plan (Rs)	1,490	1,300	1,490	2,000
	High-end premium plan (Rs)	4,290	5,000	4,990	3,500

Source: Companies

Service offerings across the industry are fairly homogeneous and easily replicable - hence, DTH operators are forced to compete on price alone, resulting in a price war

As can be seen from the table above, there are limited levers available with the DTH operators to differentiate their service offerings. Since the service offerings are fairly homogeneous, DTH operators are forced to compete on price alone. Any new price point offered by an incumbent forces other operators to match the pricing, essentially leading to a price war within the industry.

Overall, Dish TV fares well on all four counts while countering competition. We believe that Dish TV's offerings are competitive and hence do not foresee significant churn in its subscriber base beyond the 4% factored in our numbers.

Dish TV schemes - a comparison

	Silver	Gold	Diamond	Platinum
# of channels & services	110	125	140	165
Price (Rs/month)	99	160	220	275

Source: Company

We expect Dish TV to add 1.7mn subscribers (factoring in a higher churn) during FY09E. We draw comfort from the fact that the company has already added 1.3mn subscribers during the first seven months this fiscal.

On the back of these fairly competitive service offerings, we expect Dish TV to add 1.7mn subscribers (factoring in a higher churn) during FY09E, thus ending with a net subscriber base of 4.2mn by FY09E. We draw particular comfort from the fact that the company has already added 1.3mn subscribers during the first seven months this fiscal. We expect Dish TV's net subscriber base to exhibit an accelerated 14.7% CAGR over the period FY09E-FY12E followed by a subdued 8.1% CAGR over the period FY12E-FY20E.

Revenues to exhibit a CAGR of 33% over the period FY9E-FY12E

Consistent subscriber addition expected from current fiscal

Aggressive subscriber addition would impose an enormous burden on Dish TV's funding requirements. Our sense is that the company would slow its pace of subscriber acquisition beyond the immediate near-term.

Dish TV is currently the largest player within the domestic DTH space with just over 4mn subscribers as of Oct'08 (at a gross level). We expect the company to add about 1.7mn subscribers (net of churn) during the current fiscal and end FY09E with a net subscriber base of 4.2mn. We draw comfort from the fact that Dish TV has already added 1.3mn subscribers during the first 7 months this fiscal.

Over the next 3 years (FY09E-FY12E), we build in a higher churn (at 4% as against a historical churn of less than 2%) to arrive at our subscriber base estimates for Dish TV. Given the fact that the DTH space has just entered into a highly competitive phase, we believe that aggressive subscriber addition would impose an enormous burden on the company's funding requirements.

Our sense is that Dish TV would be inclined towards slowing down on the pace of subscriber acquisition beyond the immediate near-term as a result of the funding constraints that this might impose. In fact, we already see some semblance of sanity prevailing in how Dish TV has reduced the honeymoon period from 12 months to 3 months through its latest Combo pack offering.

Dish TV - net subscriber addition FY08-FY15E

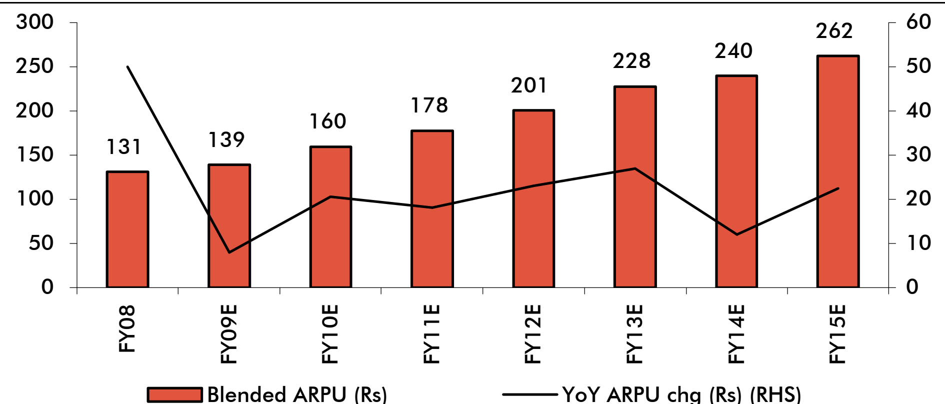
Source: Company, Ambit Capital Research estimates

ARPU growth to gradually migrate to higher trajectory

In an intensely competitive environment, we expect the DTH space to witness a subscriber-grab syndrome over the period FY09E-FY12E. We also believe that operators who create genuine value would be the ones who can get a higher proportion of their subscriber base migrating towards premium pricing plans. We expect Dish TV's ARPUs to gradually migrate to a higher growth trajectory.

We expect Dish TV's ARPUs to gradually trend to a higher growth trajectory as a larger proportion of the existing subscriber base migrates towards premium pricing plans.

Blended ARPU growth (in absolute terms) likely to move to a higher trajectory



Source: Company, Ambit Capital Research estimates

Having reduced the subscribers' honeymoon period from 12 months to 3 months, Dish TV has ensured that the migration to non-basic plans happens sooner.

We believe that every DTH operator would seek to build scale and wait until reaching a critical size (in terms of subscriber base) before upping the ante with high-ARPU schemes. Given their headstart, we believe that Dish TV is relatively closer to attaining this critical scale than the other operators.

As we discussed in the earlier section, Dish TV has a presence across 4 attractive pricing points (monthly rentals ranging from a minimum at Rs99 to a maximum of Rs275). Also, having effectively reduced the subscribers' honeymoon period from 12 months to 3 months (through the Combo Pack offer), Dish TV has ensured that the migration to non-basic plans happens sooner.

We expect absolute growth in ARPUs to be subdued during the next three years (from Rs139 during FY09E to Rs201 by FY12E) followed by a period of pronounced ARPU growth thereon. We expect Dish TV's ARPUs to trend up and settle at Rs262 by FY15E. We believe this would come about as a combination of two factors:

We expect ARPUs to move from Rs139 in FY09E to Rs262 by FY15E as a result of two factors:

- Absolute increase in basic plan pricing

- Higher proportion of subscribers migrating towards premium plans

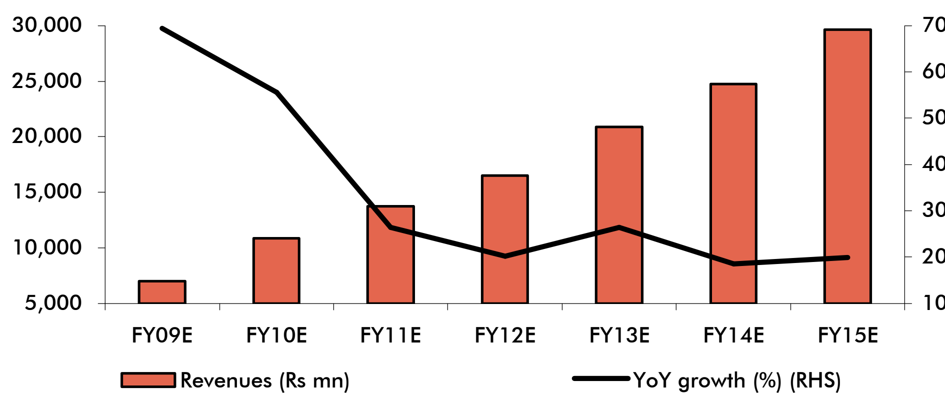
a) Absolute increase in pricing of the basic plan

b) Higher proportion of subscribers moving towards premium pricing plans

As a result of the combination of ARPU growth and subscriber base movement, we expect Dish TV's revenues to multiply 4x times from Rs4.1bn as of FY08 to Rs16.5bn by FY12E and further to Rs29.7bn by FY15E. We expect Dish TV revenues to exhibit a CAGR of 33% over the period FY09E-FY12E followed by a 18% CAGR during the period FY12E-FY20E, primarily on account of robust net subscriber addition. During the more highly competitive phase between FY09E-FY12E, we expect ARPU growth to be subdued followed by an accelerated ARPU growth (in absolute terms) over the period FY12E-FY20E.

We expect Dish TV's revenues to grow from Rs4.1bn as of FY08 to Rs16.5bn by FY12E and further to Rs29.7bn by FY15E.

Strong revenue traction FY09E-FY15E



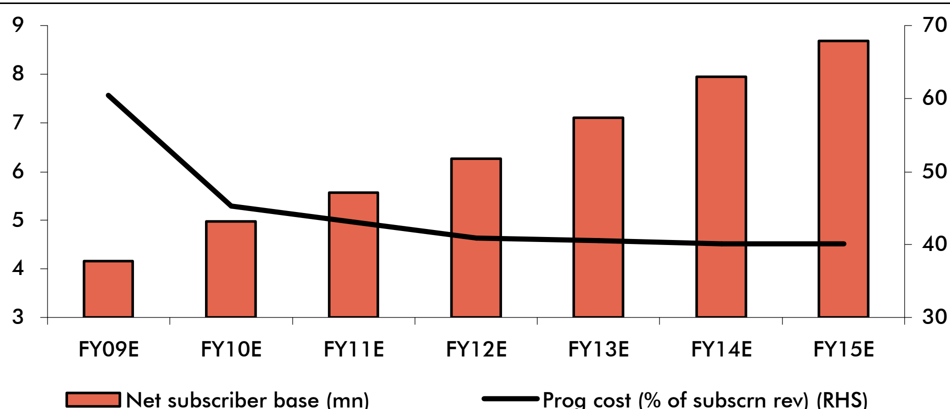
Source: Ambit Capital Research estimates

Dish TV to turn EBITDA positive in FY10E

The two major drags on operations are promotional expenses and content costs. As the DTH platform becomes more significant for broadcasters, we expect content costs to begin trending downwards

We expect Dish TV to turn black at the EBITDA level not before FY10E given the current intense competition requiring large content subsidies (something which was not there in the initial phase) and high promotional expenditure. The content cost subsidy is captured within programming costs while dealer commission directly varies with the number of subscribers added. As the DTH platform matures and becomes increasingly meaningful for broadcasters, we expect the cost of content for DTH operators to begin trending downwards.

Content subsidy - to stay over 40% until FY15E



Source: Ambit Capital Research estimates

As new subscriber acquisition subsides, promotional expenses (a direct variable cost) would decline

Moreover, Dish TV spends heavily on dealer incentives as its products compete with others on the same shelf. These two counts of expenditure are expected to keep the operational costs high until FY10E, leading to significant EBITDA positive P&L only in FY11E as new customer acquisition subsides, ARPUs start trending up and content cost comes down as a proportion of revenues. We do not see the company clocking a positive PAT before FY15E either because of high depreciation.

As higher ARPUs push revenues upwards, content costs would begin trending down as well because of the in-built sliding scale mechanism

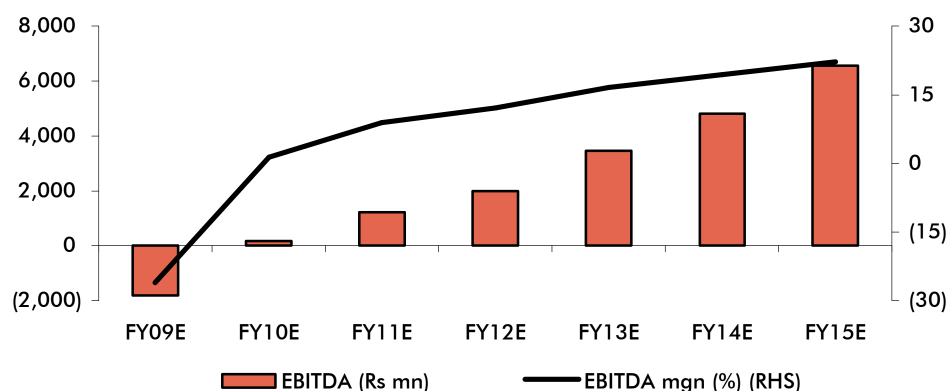
Key opex items common-sized (% of revenues)

	FY09E	FY12E	FY15E	FY20E
Cost of goods sold	4.9	3.1	2.4	1.5
Operating expenses	68.6	56.0	53.6	54.0
Programming and other costs*	60.5	40.9	40.1	40.1
Selling and distribution expenses	32.5	16.7	13.3	10.0

Source: Ambit Capital Research estimates *as a % of subscription revenues

As the pace of subscriber acquisition subsides, ARPUs start trending up and content costs drop, we expect Dish TV to move into positive EBITDA territory from FY10E onwards

EBITDA positive by FY10E - however, meaningful EBITDA contribution from FY11E



Source: Ambit Capital Research estimates

Competitive pressures to limit absolute ARPU growth over the near-term...

Competitive pressures would limit absolute ARPU growth in near-term because of two reasons:

- Low ARPU schemes would drive subscriber growth to an extent

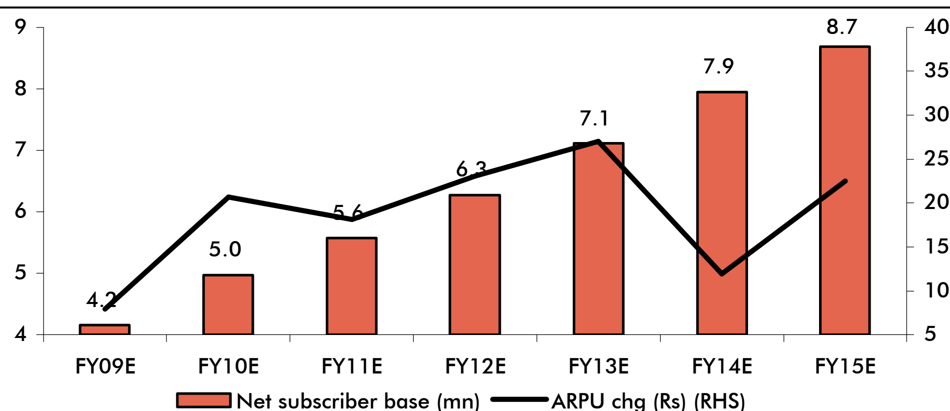
- Only 20% of first-time subscribers are expected to opt for premium plans between FY09E and FY12E

We believe that Dish TV will have to keep offering low ARPUs service packs in the medium term because of two reasons:

1. The company will need to offer highly subsidized pricing points in order to counter strong competition and lure in new customers. Dish TV has scored a great hit with its offering of free STB with 12 months' subscription for Rs1,999 (offered last month). However, of this, only Rs500 was booked towards content (translating into a monthly ARPU of Rs42) while the rest set off against the cost of the STB and towards dealer incentives.

2. During the period FY09E-FY12E, Dish TV is expected to add 3.8mn subscribers. We believe that of the new subscribers, 80% will opt for the basic offerings with low ARPUs while only 20% will go for the premium offerings. We expect ARPUs from new customers to remain sub Rs100 levels until FY13E.

Limited absolute growth in ARPU to be offset by robust subscriber addition



Source: Ambit Capital Research estimates

We expect ARPUs to move up faster (in absolute terms) beyond FY12E as operators stop offering basic plans and begin focusing on enhancing ARPUs from their existing subscriber base

These two factors would result in the weighted average ARPUs exhibiting a subdued growth in absolute terms over the period FY09E-FY12E. However, we expect ARPUs to move up faster during the consolidation phase where none of the players will be offering very low entry level offerings and would rather be focusing on increasing ARPUs from their existing subscriber base.

... to be partially offset by content costs sliding down

Basic entry-level offerings force DTH operators into pricing content at close to their cost, resulting in lower gross margins. DTH operators would need to stop undercutting each other in order to stop the heavy bleeding

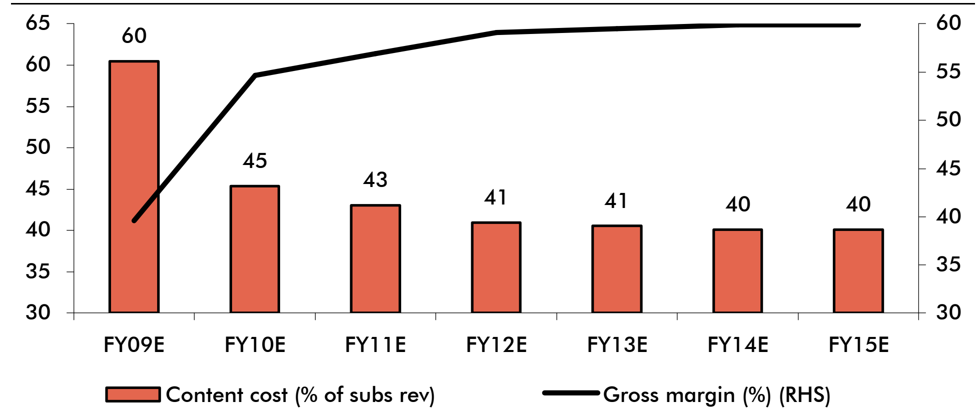
The low ARPU offerings introduced for the new customers are resulting in a huge hit being taken by the DTH players on the P&L side. The channel packages are announced at not very far off from their content cost, resulting in lower gross margins. Though it is true that there will be a sliding scale mechanism, which will help in lowering the content costs as the subscriber base builds up, we believe that it will only partially offset the subsidized costs, as broadcasters can not keep on lowering their content costs just to accommodate DTH players' subsidies at all levels. Hence, the loss on the P&L side will only be partially offset by lower content costs, and the DTH players will have to stop undercutting each other in channel pricing.

As Dish TV's subscriber base reaches 5mn by FY10E, we believe that its content cost as a % of subscription revenues will come down to about 41% by FY12E from 71% as of FY08. We expect the company's programming cost to settle at ~40% of subscription revenues beyond the medium-term.

Merely because DTH operators are resorting to price competition, we do not believe that broadcasters would correspondingly bring down content cost. Content cost can only reduce (as a proportion of subscription revenues) on the back of larger revenue flow

As highlighted earlier, it is in the broadcaster's interest to keep the DTH platform viable because of the inherent addressability. However, merely because the DTH space is witnessing large-scale price competition between FY09E-FY12E, we do not believe that broadcasters would correspondingly bring down content costs. We expect content costs to settle around 40%-42% of the subscription revenues unless exclusive content is allowed.

Gross margin expansion corresponding to content costs subsiding

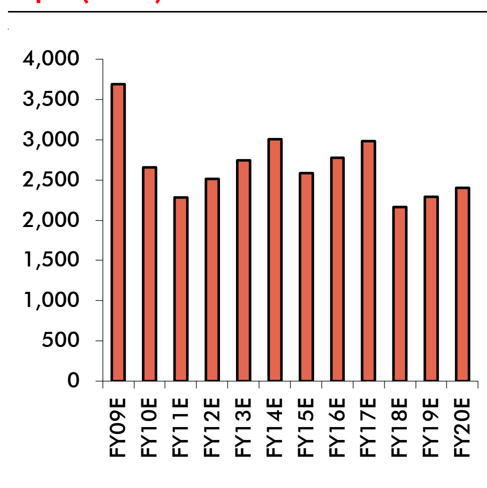


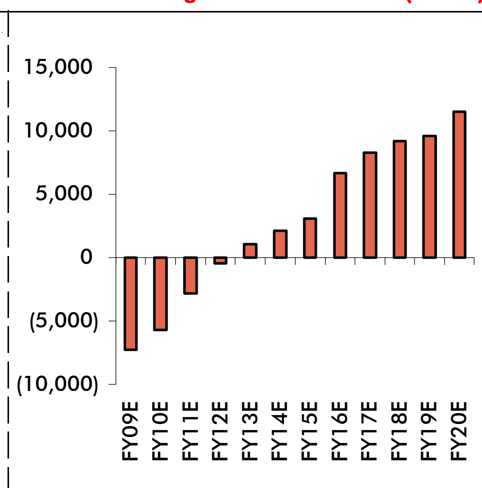
Source: Ambit Capital Research estimates

Though content costs for global DTH players range from 35-40% of their subscription revenues, we do not foresee a sub-40% scenario in the Indian context, essentially on account of the intense price-based competition.

Customer acquisition cost a major constraint on growth

Capex (Rs mn) **... a drag on free cash flows (Rs mn)**





Source: Ambit Capital Research estimates

Demand side is likely to remain robust for growth. However, funding requirements for subscriber acquisition are likely to escalate and will act as a major constraint for Dish TV's growth on two counts:

- Operational drag due to need for higher subsidies

- Working capital squeeze from a reducing broadcaster's credit days

Dish TV spends ~Rs2600 on customer acquisition, spending on the box, content, marketing expenses, dealer incentive and content subsidy. We believe that recent data points demonstrate the high price elasticity of DTH products. We have observed Sun garnering over 1mn subscribers shortly after its Rs999 pack and Dish TV adding over 0.4mn subscribers in a single month post its free STB offer. Hence, demand side is fairly robust as far as growth dynamics are concerned. However, funding requirements are very high for customer acquisition and will act as a major constraint for the company's growth on two counts.

Firstly, Dish TV already has a negative networth and debt of Rs8.28bn having recently added Rs4.1bn in debt. Due to the higher subscriber addition targets for FY09E and FY10E, we expect funds raised through debt and rights issue (Rs11.4bn in three tranches) to be deployed by FY10E and believe that Dish TV will require further funding post FY10E.

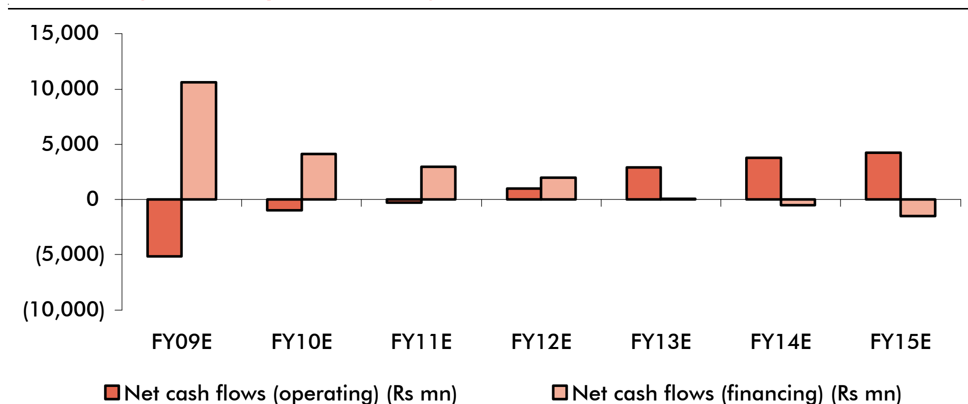
Fund raising (Rs mn)

	FY09E	FY10E
Issue / dilution of equity	7,773	4,145
Increase (decr) in debt	2,839	0

Source: Company, Ambit Capital Research estimates

The more protracted the price war, the longer it would take for Dish TV to breakeven and hence, higher the need for funding

Debt funding to offset operational drag



Source: Ambit Capital Research estimates

Creditor days for payment due to the broadcasters are abnormally high at 447 days in FY08 (resulting in high current liabilities and a negative working capital) and should decline to 120 days by FY15E.

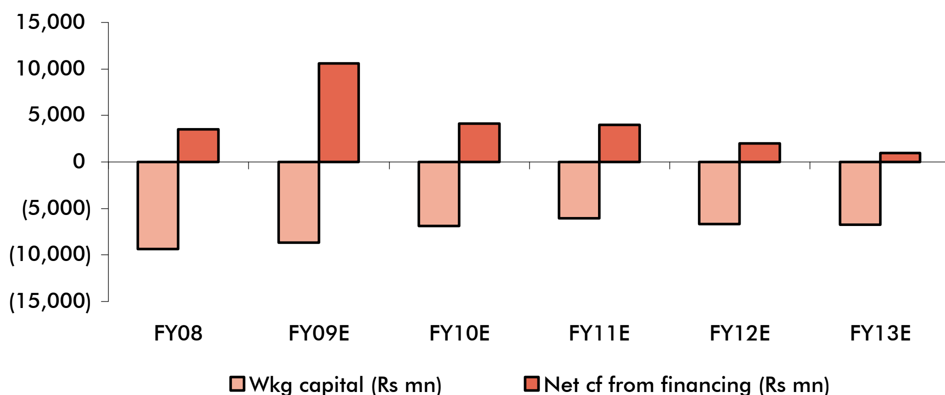
Secondly, Dish TV has a negative working capital predominantly due to its very high current liabilities (Rs11.7bn as of FY08). Current liabilities are high mainly on account of delayed payment of programming costs and deposits received from new customers, which are expensed against set top box rentals and subscription revenues.

We believe that creditor days for the payment due to the broadcasters are abnormally high at 447 days in FY08 and should come down to 100 days over the years leading to a decline in this sub-head. As deposits/advance received are driven by subscriber addition, this subhead is also bound to come down from current levels as subscriber addition slows down.

The above two changes will increase funding requirements for Dish TV as working capital stops financing the company over the coming years. Dish TV was financed to the tune of Rs9.4bn through working capital in FY08, we expect this to come down to Rs3bn by FY12E, leading to higher funding requirements.

As the working capital cycle moves from negative to positive territory, funding requirement is likely to increase

Debt funding to substitute for working capital squeeze



Source: Company, Ambit Capital Research estimates

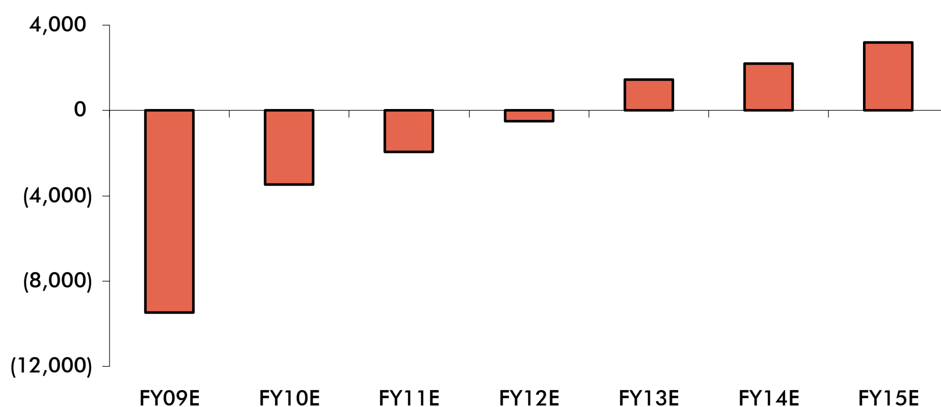
We believe that Dish TV's growth will considerably moderate due to high capex requirements over the coming years as it becomes difficult to raise funds on a stretched balance sheet. We are optimistic about the company's subscriber addition to accommodate funding only to the tune of Rs7bn in the period FY10E-FY13E.

Valuation and Recommendation

Dish TV is expected to start throwing positive free cash flows from FY13E onwards, primarily on the back of high depreciation. Operations start contributing meaningfully to free cash flows from FY14E.

We have used the DCF method to value Dish TV based on the assumptions given below. We believe that the WACC for the company has to be higher given the high debt requirements in the medium terms. Dish TV is expected to start throwing positive free cash flows from FY13E onwards, primarily on the back of high depreciation. Operations start contributing meaningfully to the free cash flows only post FY14E. Our DCF model gives us a 1-year forward price target of Rs20.3, leading to an upside of 36% from current levels. The stock currently trades at a 1-year forward market cap to sales multiple of 1.3x (FY10E).

FCFF (Rs mn) - turning positive from FY13E



Source: Ambit Capital Research estimates

The stock has corrected to a large extent due to concerns over entry of new players with deeper pockets, threatening the advent of price competition, thereby delaying EBITDA breakeven, high funding requirements and pending dilution.

The stock has taken a considerable beating due to concerns over entry of new players with deeper pockets, thus threatening the advent of price competition, thereby delaying EBITDA breakeven, high funding requirements and pending dilution. The management has successfully addressed the funding concerns by tying up debt to the tune of Rs4.1bn at 12.75% with a moratorium period till FY13E. Dish TV has also filed a rights issue to the tune of Rs11.4bn at Rs22 per share. The promoters have not arranged for any underwriting facility, and are willing to underwrite to the extent of 90% of the rights issue in the event of devolving the issue. The ability of the management to raise required funds and the willingness to invest further in the company provides some comfort on funding issues in the future.

We believe that our price target is highly conservative, factoring in the challenges faced by the company. At the CMP of Rs15.0, most of these concerns are priced in the stock and the risk/rewards relationship is favorable from hereon. We initiate coverage on Dish TV with a '**BUY**' recommendation on the basis of sound fundamentals and comforting valuations.

DCF value sensitivity to WACC (LHS) and terminal growth

	1.0%	2.0%	3.0%	4.0%
12.5%	28.0	31.4	35.5	40.6
13.5%	21.3	23.9	27.1	30.9
14.5%	15.8	17.8	20.2	23.1
15.0%	13.3	15.2	17.3	19.8
15.5%	11.1	12.7	14.6	16.9

Source: Ambit Capital Research estimates

DCF Model Assumptions

Tax rate	12.3%
Risk-free rate	8.25%
Risk premium	7.0%
Adj Beta	1.10
Cost of equity	16.0%
Cost of debt	11.5%
Post-tax cost of debt	10.1%
WACC	14.5%

Source: Ambit Capital

DCF table

(Rs mn)	FY09E	FY10E	FY11E	FY12E	FY13E	FY14E	FY15E	FY16E	FY17E	FY18E	FY19E	FY20E
EBIT-tax	(4,232)	(2,866)	(2,510)	(1,794)	(711)	849	2,561	3,901	5,639	8,034	7,553	9,293
Depreciation	2,404	3,013	3,717	3,781	4,163	3,949	3,843	3,898	3,973	3,667	3,596	3,656
Delta working capital	2,705	135	361	(434)	(980)	(440)	728	(113)	(1,159)	629	(675)	(1,131)
Capital expenditure	(5,023)	(3,581)	(2,926)	(3,080)	(3,201)	(3,306)	(2,649)	(2,850)	(3,057)	(2,216)	(2,344)	(2,459)
Free cash flow to firm	(9,486)	(3,460)	(1,943)	(494)	1,439	2,180	3,175	5,236	7,920	9,095	9,753	11,934
FCF Growth rate (%)		(64.0)	(44.0)	(75.0)	(392.0)	51.0	46.0	65.0	51.0	15.0	7.0	22.0
Discounted value	(8,865)	(2,825)	(1,385)	(307)	783	1,036	1,318	1,899	2,509	2,516	2,357	2,519

Total Discounted value	1,553
Terminal value (Rs mn)	22,596
Total value (Rs mn)	24,149
Debt (Rs mn)	8,284
Cash (Rs mn)	956
Total shareholders' value (Rs mn)	16,821
No. of shares (post dilution) (mn)	946
Present fair value, Rs	18
1-yr forward value per share (Rs)	20.3
CMP	15.0
Upside (%)	36

Source: Ambit Capital Research

Wire and Wireless India

Buy

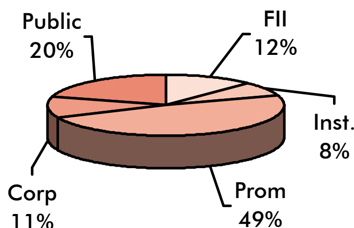
Price	Rs 9.3
Target Price	**%upside**
Rs15.3	64 ↑
Market Capitalisation	
Rs2,009mn	(US$40mn)
52 week range H/L (Rs)	107/8
Shares o/s (mn)	**Daily vol (3m avg)**
217.22	2.47
Reuters	**Bloomberg**
WIWI.BO	WNW IN

Perfm(%)	**1M**	**3M**	**12M**	**YTD**
Absolute	1.6	(60.4)	(86.8)	(90.7)
Rel. to Sensex	13.8	(31.8)	(70.8)	(78.4)

BSE Sensex	**Nifty**
8,739	2,658

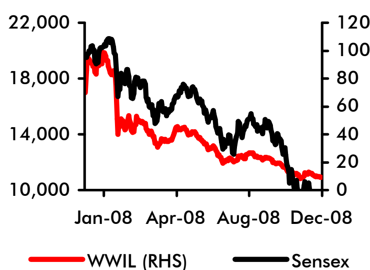
Source: Bloomberg

Shareholding pattern



Source: Capitaline

Price performance



Source: Capitaline

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Its all 'HITS'

Investment Rationale

C&S Industry all set for digitization & consolidation: The cable industry is all set for a phase of sustained consolidation driven by increasing appeal of digital platforms and rising penetration of DTH. This is expected to significantly shift the bargaining power in the C&S value chain from local cable operators to large multi system operators. WWIL, being the leader in this space, is expected to benefit the most from this favorable shift in the sector fundamentals.

Best placed to ride the digital boom through HITS: We believe that Head-end-in-the-sky (HITS) technology is the quickest and most cost-effective way to digitize cable networks pan India. Currently, WWIL is the only MSO with a HITS licence. We believe that this gives the company considerable competitive headstart over others in building direct digital subscriber base by entering into participations with the local cable operators. We expect that the HITS platform will help WWIL to reach a digital subscriber base of 5mn by FY15E, from 0.25mn at present.

Sales and EBITDA to show a CAGR of 33% and 39% in FY09E-FY15E: The direct result of increasing addressability of subscriber base in the digital mode is expected to fuel a sales CAGR of 33% and EBITDA growth of 39% for the company in the period FY09E-FY15E. We expect WWIL to report a positive EBITDA by FY11E and positive PAT by FY13E on a very conservative basis.

Rights issue to repair balance sheet: The company is in the process of finalizing a rights issue to the tune of Rs4.5bn. We have assumed the rights issue price at Rs10, resulting in equity dilution to the tune of 450mn shares. The funds raised through this will be used to invest in the HITS platform and retire debt. The flow of funds though the issue will repair the balance sheet for further debt raising in FY10E-FY12E to the tune of Rs4bn. We believe that this takes care of our assumed subscriber addition during the period FY09E-FY15E, and hence do not see funding as a constraint for our assumed growth rate.

Valuations based on new initiatives; hence risks are high: We have used the DCF methodology to value WWIL, which gives us a 1-yr price target of Rs15.3, indicating an upside of 64% from the current levels. Our sensitivity analysis for subscriber addition and without HITS scenario suggests that WWIL's valuation depends entirely on the HITS success and hence has high execution risks. We build high execution risk for the company in our operational and valuation assumptions and are confident of fundamentals of the company leaving enough room for upside from these levels. We initiate coverage on the stock with a '**BUY**' recommendation.

Key financials

Year to March (Rs mn)	FY08	FY09E	FY10E	FY11E	FY12E
Operating income	2,710	3,331	5,483	7,724	10,062
EBITDA	(183)	5	(207)	567	1,577
EBITDA mgn (%)	(6.8)	0.1	(3.8)	7.3	15.7
PAT	(1,529)	(873)	(1,242)	(1,043)	(590)
PAT mgn (%)	(56.4)	(26.2)	(22.7)	(13.5)	(5.9)
EPS (Rs)	(7.1)	(1.3)	(1.9)	(1.6)	(0.9)
P/E (x)	NM	NM	NM	NM	NM
EV/EBITDA (x)	NM	NM	NM	21.9	7.9
EV/Sales (x)	4.6	3.7	2.3	1.6	1.2

Source: Company, Ambit Capital Research

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Please refer to disclaimer section on the last page for further important disclaimer.

Key financials

Balance sheet

Year to March (Rs mn)	FY08	FY09E	FY10E	FY11E	FY12E
Cash & equivalents	205	99	302	217	283
Debtors	1,039	1,233	1,579	1,801	1,944
Inventory	900	997	1,477	1,872	2,195
Loans & advances	431	358	641	876	1,068
Investments	0	0	0	0	0
Fixed assets	1,707	1,268	2,952	4,148	4,862
Other assets	9	0	0	0	0
Total assets	**4,291**	**3,956**	**6,951**	**8,914**	**10,352**
Current liabilities & provisions	1,491	1,555	2,534	3,534	4,558
Debt	3,738	1,958	2,958	4,958	5,958
Other liabilities	72	69	64	60	57
Total liabilities	**5,301**	**3,582**	**5,556**	**8,552**	**10,573**
Shareholders' equity	217	667	667	667	667
Reserves & surpluses	(1,229)	(293)	728	(305)	(889)
Total networth	**(1,012)**	**374**	**1,395**	**363**	**(221)**
Net working capital	879	1,034	1,162	1,015	649
Net debt (cash)	3,533	1,859	2,656	4,741	5,675

Source: Company, Ambit Capital Research estimates

Income statement

Year to March (Rs mn)	FY08	FY09E	FY10E	FY11E	FY12E
Operating income	2,710	3,331	5,483	7,724	10,062
% growth	*30.3*	*22.9*	*64.6*	*40.9*	*30.3*
Operating expenditure	2,894	3,326	5,690	7,157	8,484
EBITDA	(183)	5	(207)	567	1,577
% growth	*-21.5*	*-102.5*	*-4617.3*	*-373.7*	*178.1*
Depreciation	309	600	834	1,271	1,691
EBIT	(493)	(595)	(1,042)	(704)	(113)
Interest expenditure	372	328	283	455	628
Non-operational income / Exceptional items	(651)	67	110	154	201
PBT	(1,515)	(856)	(1,215)	(1,004)	(540)
Tax	13	17	27	38	50
PAT / Net profit	(1,529)	(873)	(1,242)	(1,043)	(590)
% growth	*42.4*	*-42.9*	*42.3*	*-16.1*	*-43.4*

Source: Company, Ambit Capital Research estimates

Cash flow statement

Year to March (Rs mn)	FY08	FY09E	FY10E	FY11E	FY12E
EBIT	(493)	(595)	(1,042)	(704)	(113)
Other income (expenditure)	(630)	57	110	154	201
Depreciation	309	600	834	1,271	1,691
Interest	(372)	(328)	(283)	(455)	(628)
Tax	(13)	(17)	(27)	(38)	(50)
Incr (decr) in deferred tax liability	45	23	7	6	4
Incr (decr) in net working capital	(429)	154	129	(148)	(366)
Cash flow from operating activities	**(724)**	**(414)**	**(529)**	**382**	**1,470**
Incr (decr) in capital expenditure	(419)	(162)	(2,518)	(2,467)	(2,405)
Incr (decr) in investments	0	0	0	0	0
Cash flow from investing activities	**(419)**	**(162)**	**(2,518)**	**(2,467)**	**(2,405)**
Incr (decr) in borrowings	1,091	(1,780)	1,000	2,000	1,000
Issuance of equity	98	2,250	2,250	0	0
Dividend paid	0	0	0	0	0
Others	0	0	0	0	0
Cash flow from financing activities	**1,188**	**470**	**3,250**	**2,000**	**1,000**
Net change in cash	45	(106)	203	(85)	66
Closing cash balance	205	99	302	217	283

Source: Company, Ambit Capital Research estimates

Ratio analysis

Year to March (%)	FY08	FY09E	FY10E	FY11E	FY12E
EBITDA margin	(6.8)	0.1	(3.8)	7.3	15.7
EBIT margin	(18.2)	(17.9)	(19.0)	(9.1)	(1.1)
Net profit margin	(56.4)	(26.2)	(22.7)	(13.5)	(5.9)
Return on capital employed	NM	NM	NM	NM	NM
Return on equity	NM	NM	NM	NM	NM
Dividend payout ratio	NM	NM	NM	NM	NM

Source: Company, Ambit Capital Research estimates

Valuation parameters

Year to March	FY08	FY09E	FY10E	FY11E	FY12E
Diluted EPS (Rs)	(7.1)	(1.3)	(1.9)	(1.6)	(0.9)
Book value per share (Rs)	(4.7)	0.6	2.1	0.5	(0.3)
P/E (x)	NM	NM	NM	NM	NM
P/BV (x)	NM	NM	NM	NM	NM
EV/EBITDA (x)	NM	NM	NM	21.9	7.9
EV/Sales (x)	4.6	3.7	2.3	1.6	1.2

Source: Company, Ambit Capital Research estimates

Risks & Concerns

Funding essential for growth: We believe that the shift from analogue to digital driven by consumer preferences will happen only if it is made affordable to the consumer. In order to receive digital signals, consumers will have to install set top boxes (also called consumer premise equipments) on their TV sets. The cost of set top box is quite prohibitive and hence it is necessary to provide it at highly subsidized rates to the consumer. This requires spending on subscriber acquisition cost (SAC), along with advertising spend and discounted programming packs. The presence of strong DTH players further accentuates the need to spend on freebies in order to win the customer over. We have built in SAC to the tune of ~Rs2800 per subscriber for WWIL, which results in funding requirements of Rs4bn post the rights issue for our assumed subscriber levels. Any escalation over and above this cost will result in further funding requirements which might not be easy to obtain considering the red P&L and stretched balance sheet during initial years. We believe that funding requirements higher than those assumed by us will result in lower subscriber addition and is a risk to our valuation thesis.

Business growth dependent on a new technology: WWIL's fortunes depend on a successful HITS launch, which will help the company emerge as the most preferred MSO for the LCOs because of low investment requirements and pan India reach. Our valuation exercise shows that the upside potential for the company lies only with its success in HITS. Even though there exists considerable experience at the top level in the company, HITS is a new product for the company as well as the consumer. Lack of success in this initiative will cap the upside for the company as this will be the focus of the management from hereon. We do note the success of the promoter group in emerging as a leader in another new technology in the TV distribution space (Dish TV). WWIL has completed the trial runs for HITS and targets an addition of over 1mn subscribers every year through it. However, since the valuations are highly sensitive to subscriber addition, we still believe that there exists significant execution risk for the company.

Pending HITS regulation: The government is yet to finalize its HITS policy which will govern the license issue mechanism for HITS players. As of now, WWIL is the only player with a HITS license. We do not expect HITS policy to be in place before the pending general elections, giving the company a headstart in building a sizeable subscriber base. However, as soon as the government starts issuing fresh licenses, there will be increased competition for the company. We do note WWIL's history of facing competition in the analogue mode and emerging as the leader. However, we have still moderated our business growth assumptions in order to reflect heightened competition in the space.

Pending dilution: WWIL has filed for a rights issue to the tune of Rs4.5bn, for raising funds for future expansion and retiring debt to the tune of Rs2bn. The price band of the issue is not fixed as yet. We are assuming that the issue will be priced at Rs10 per share; payable in two equal installments of Rs5 each in FY09E and FY10E. This will result in a dilution to the tune of 450mn shares. We have assumed the issue price at a very conservative level of Rs10, resulting in subdued upside for the company because of steep dilution. We believe that any improvement on this front will substantially improve the upside potential for the stock and hence poses a positive risk to our target price.

C&S Industry all set for digitization & consolidation

As highlighted in our theme report on the TV distribution space, we believe that the cable industry is all set for a phase of sustained consolidation driven by increasing appeal of digital platforms and rising penetration of DTH. The cannibalization of cable homes by the DTH platform is rendering the LCO existence increasingly irrelevant.

Having seen the customer pull phenomenon actually playing out in the case of DTH, the LCOs realize that the only way to counter the DTH threat is to offer digital cable, which is capex intensive and hence, out of reach for standalone LCOs. We believe that these changing dynamics are gradually resulting in LCOs losing their bargaining power, making them increasingly dependent on the larger MSOs who have the ability to invest in digital upgradation of cable networks. We foresee that in the near future, there will be no need to buy out LCOs by paying 2-2.5x the revenues as is being done at present, as LCOs would have no choice but to collaborate with MSOs in order to survive this paradigm shift.

WWIL - The largest player best placed to benefit from this trend.....

WWIL industry presence

Analogue Subscribers	6.7 mn
Digital Subscribers	0.25 mn
Presence	43 cities

Source: Company

With its presence in 45 cities across India including the 3 metros (Mumbai, Delhi and Kolkata), WWIL is the largest MSO with ~6.7mn indirect subscribers and ~0.25mn direct cable subscribers. The company operates through 8 regional offices and has ~4000 franchisee LCOs with over 700 employees. With the recent launch of digital cable in Kerala, WWIL now has digital presence in 8 locations in addition to 73 analogue head-ends. Being a market leader within this space, WWIL is expected to benefit the most from this paradigm shift in the sector fundamentals.

With HITS at the forefront of its digital strategy

There are two ways to digitize a cable network viz. either through a digital head-end installed on the ground or through a digital head-end placed on a commercial satellite (HITS). Our comparative analysis of these two models suggests that HITS is more cost effective and a faster mode of digitizing the networks (See Appendix: What is HITS).

Going forward, WWIL plans to adopt HITS as the preferred mode of its digital growth strategy and expects to add 1mn direct subscribers per year.

Given the fact that WWIL is the only MSO with a license to offer HITS services, we believe that WWIL is best positioned to ride the current digitization boom. The company has finished trial runs of HITS services, and is in the process of formally launching HITS in 40 cities during the initial phase. WWIL expects to end with 50,000 HITS subscribers in FY09E and is looking to add over 1mn subscribers per year going forward. The company has booked 7 transponders on the C-Band, which would enable it to deliver more than 100 digital channels.

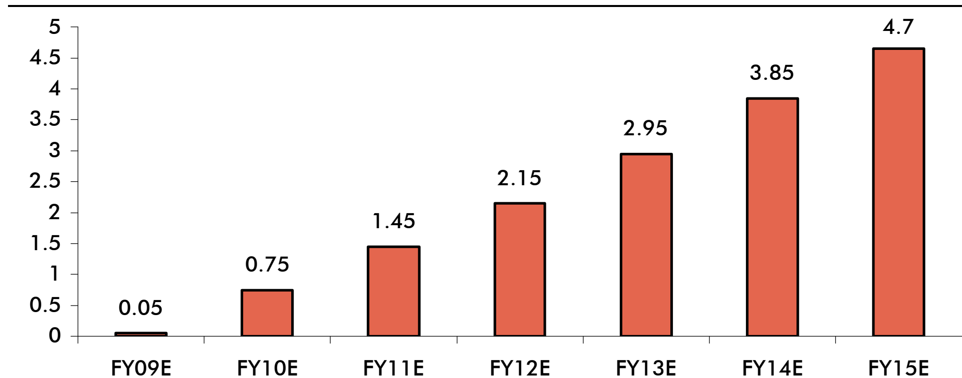
WWIL has ~0.25mn direct subscribers acquired through digital head-ends in 8 cities, 4 metros and 4 non-metros. Going forward, the company plans to stop this mode of digitization because of higher costs in the receiving units and limited reach. Hence, apart from offering digital services in these 8 cities, the rest of the cities will be covered by the HITS distribution mode.

Direct subscribers to increase to 5mn by FY15E

We expect WWIL to increase its direct digital subscriber base from the current 0.25mn customers to 2.5mn customers by FY12E and to 5mn by FY15E, at the very minimum. Going forward, our numbers factor in a low annual subscriber addition rate against management targets of adding 1mn subscribers each year, for two main reasons:

We expect WWIL to garner 4.7mn direct subscribers through HITS by FY15E and 0.35mn through digital cable. Analogue subscriber base is expected to shrink from 6.7mn at present to 3.2mn by FY15E.

WWIL's HITS subscriber base (mn)



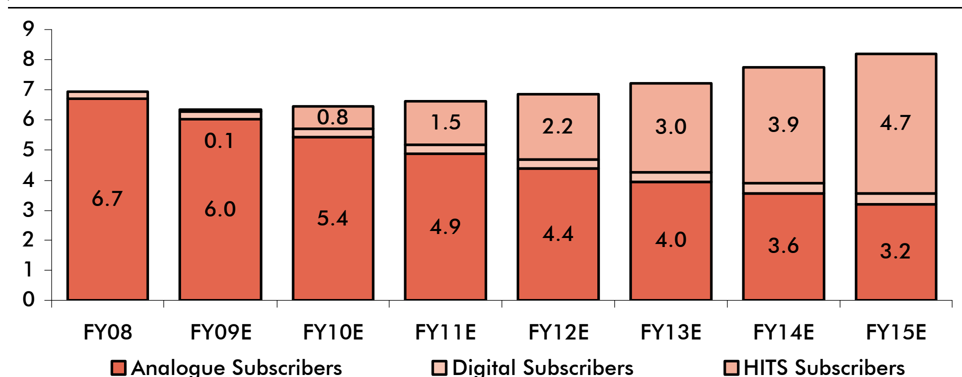
Source: Ambit Capital Research

- HITS is a new product for the company as well as the subscriber. Two critical Ps regarding the product, viz pricing and promotion are yet to be decided. Given the lack of clarity in terms of how this space would evolve, the buy-in that the platform generates remains to be seen. We believe that WWIL and the LCOs who adopt the HITS platform would go through a learning curve on the technical front as well as the operational front, resulting in slower customer acquisition during the initial years.

- How the turf battle unfolds between the LCOs and the MSOs is yet another crucial factor that would determine the pace at which the HITS platform expands. A key determinant of the growth trajectory for the platform would be the extent to which the LCO is willing to allow the MSO to digitize its network. Given the LCO's access to the last mile, HITS will be a non-starter without LCO buy-in in terms of digitization of its network. The degree of LCO's eagerness to collaborate with the MSO will depend on the level of perceived DTH threat in his mind, as he stands to lose revenues by collaborating with the MSO. Given the unpredictability in terms of how the inter-play pans out, our numbers factor in a low HITS penetration.

We believe that the number of digital subscribers added through terrestrial digital head-ends will grow at a very slow place of 0.015 million per year primarily due to the focus shifting towards HITS. The company's analogue subscriber base is expected to diminish from the present 6.7mn to 3.2mn by FY15E as WWIL seeks to migrate more subscribers from this pool towards their HITS platform.

WWIL subscriber composition by technology



Source: COmpany, Ambit Capital Research

HITS model assumptions

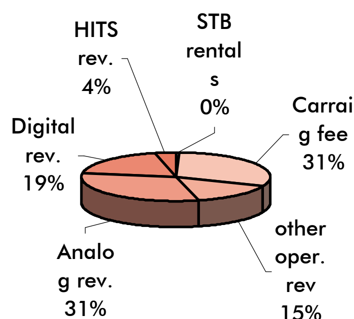
As the company is yet to formalize the pricing of its HITS offer, we have assumed a pricing environment similar to the one being offered under the digital platform. Our numbers factor in an initial set top box offer priced at Rs699 (similar to what the company is offering in its latest digital cable launch in the 8 cities at present). ARPUs will be similar to what the customer is already paying in the analogue mode, assumed at Rs200 at present and growing by ~2% every year. The box cost is assumed at Rs2000, resulting in box subsidy of Rs1301 during the initial phase.

HITS Model Assumptions

Capex for digital head-end on the ground (Rs mn)	350
No of digital head-ends required	1
Price of signal receiving units at LCO's end (Rs mn)	0.35
Capex for receiving units till FY15E (Rs mn)	881
ARPU (Rs)	200
Price of STB (Rs)	699
Cost of STB (Rs)	2,000
Content cost (% of subscription revenues)	45.0
LCO's share (distribution charges) (% of subscription charges)	25.0
Gross margin (%)	30.0

Source: Ambit Capital Research estimates

Revenue Break-up FY09E



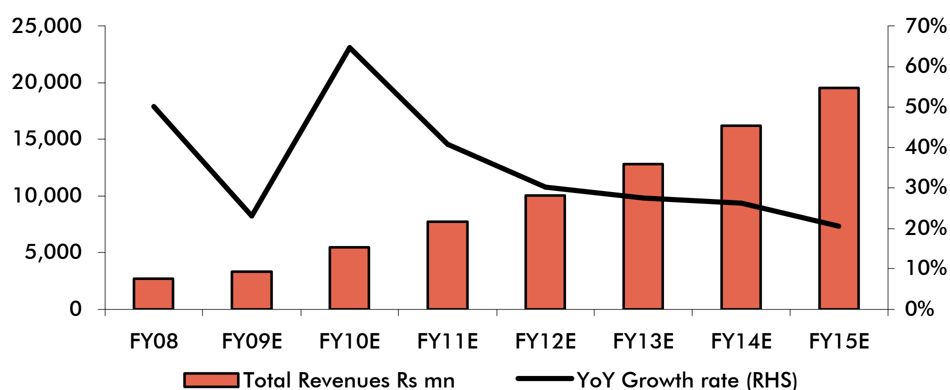
Source: Ambit Capital Research

On the opex front, WWIL is expected to incur annual rental costs at $1mn for every transponder. The capex on receiving units at the LCO's end is expected to clock in at Rs0.35mn per LCO, for which WWIL will take a deposit of Rs0.1mn from the LCO.

Sales to show a CAGR of 33% in FY09E-FY15E

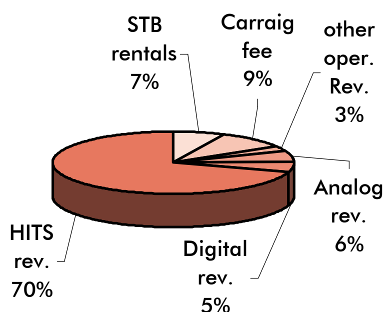
We expect WWIL to show a revenue CAGR of 33% in the period FY09E-FY15E, purely on the back of HITS subscriber additions. Contribution of HITS to WWIL's total revenue is expected to grow from 4% in FY09E to 54% by FY12E and 70% by FY15E.

Revenue to grow 7x in 7 years



Source: Company, Ambit Capital Research

Revenue Break-up FY15E



Source: Ambit Capital Research

EBITDA to turn positive in FY11E

The increasing economies of scale will bring down operational costs for WWIL resulting in a positive EBITDA by FY11E. Major cost savings will happen on two fronts;

Distribution charges and content cost are 2 biggest components of the total operational expenditure for WWIL. Both are expected to come down as a % as the company builds scale through the digital mode.

1. The company pays distribution charges to LCOs, which include carriage fee sharing with them. This sharing is based on analogue revenues and is very high, at ~32% in FY08. This payment forms almost 70% of the analogue revenues in FY07, indicating the bargaining power of LCOs. However, this is all set to come down from the current levels because of;

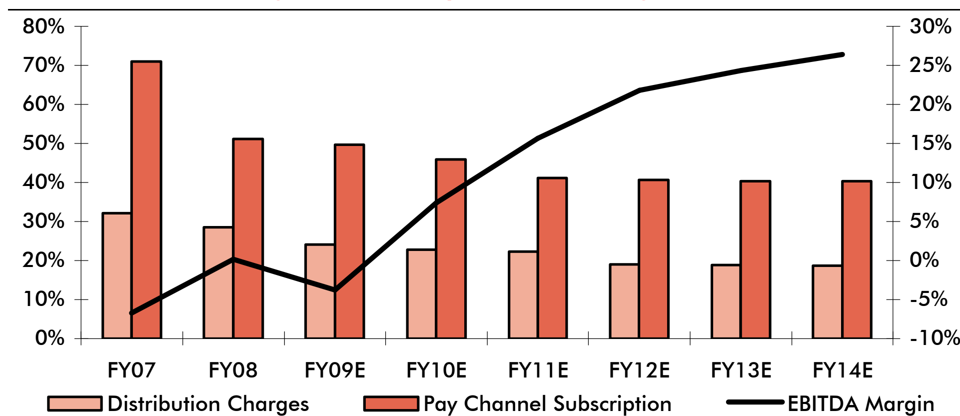
   a) Decreasing share of analogue revenues in the total revenues

   b) Increasing share of digital platforms in total revenues; where the revenue share with the LCOs is 25%.

We expect distribution charges as a % of total revenues to come down to 22% in FY12E and to 19% in FY15E, from the current level of 32%.

2. Programming costs as a % of subscription revenues formed 46% and 71% of the subscription revenues in FY07 and FY08. This is because there is no scientific basis for charging content cost in the analogue mode because of lack of addressability. Content cost under the analogue mode is dependent on negotiated subscriber base and depends upon the bargaining power of broadcaster. However, as the company moves towards digital platforms, content cost as a % of revenues is expected to come down to 44% in FY12E and to 41% in FY15E.

Lower variable cost in digital mode to expand EBITDA margins



Source: Company, Ambit Capital Research estimates

These two factors will result in EBITDA margin expansion from the current -7% to 15.7% by FY12E and 26.4% by FY15E.

Rights issue to repair balance sheet

Equity infusion will strengthen the balance sheet for further fund raising during FY10E - 12E

WWIL has filed for a rights issue to the tune of Rs4.5bn, for raising funds for future expansion and retiring debt to the tune of Rs2bn. The price band of the issue is not fixed as yet. We are assuming that the issue will be priced at Rs10 per share; payable in two equal installments of Rs5 each in FY09E and FY10E. This will result in a dilution to the tune of 450mn shares. The flow of funds will repair the weak balance sheet of WWIL and take care of funding requirements for the next two years, after which the company is again required to raise funds, based on our assumed level of operations.

We believe that WWIL would need further debt funding to the tune of Rs4bn during FY10E-FY12E. We believe that by then, the company would have garnered enough subscribers to comfort the lenders and hence should not face any problem in raising funds.

Valuations based on new initiatives; hence risks are high

Our DCF model gives a 1-year forward price target of Rs15.3, indicating an upside of 64% from current levels

We have used the DCF methodology to value WWIL as we believe that the value creative potential of the new initiatives lies in the long term, and hence will be better captured through DCF as it takes the operational value into account as the company builds its subscriber base. Our DCF model indicates a one year price target of Rs15.3 for WWIL, resulting in an upside of 64% from current levels. The stock has taken a huge beating due to lack of clarity over funding and absence of monitorable performance drivers in the analogue mode. We believe that with the successful funding through rights issue and HITS launch bringing in clarity regarding business drivers, the stock will start reacting positively as progress is made on these two fronts. We initiate coverage on the stock with a '**BUY**' recommendation

DCF Model Assumptions

Tax rate	12.3%
Risk-free rate	8.5%
Risk premium	7.0%
Adj Beta	1.30
Cost of equity	17.6%
Cost of debt	11.8%
Post-tax cost of debt	10.3%
D/E	0.67
WACC	14.7%

Source: Ambit Capital

DCF Model (Rs mn)

	FY09E	FY10E	FY11E	FY12E	FY13E	FY14E	FY15E
EBIT-tax	(612)	(1,069)	(742)	(163)	587	1,269	2,256
EBIT Growth rate		75%	-31%	-78%	-459%	116%	78%
Depreciation	600	834	1,271	1,691	2,147	2,600	2,575
Delta working capital	(154)	(129)	148	366	490	654	847
Capital expenditure	(162)	(2,518)	(2,467)	(2,405)	(2,605)	(2,766)	(2,400)
Capex Growth rate		1456%	-2%	-3%	8%	6%	-13%
Free cash flow to firm	(262)	(2,772)	(1,636)	(310)	876	2,081	3,669
FCF Growth rate		960%	-41%	-81%	-382%	138%	76%
Discounted value	(244)	(2,257)	(1,162)	(192)	473	980	1,506

Upside capped due to steep dilution

Total Discounted value	(894)
Terminal value (Rs mn)	13,302
Total value (Rs mn)	12,408
Debt (Rs mn)	3,738
Cash (Rs mn)	205
Total shareholders' value (Rs mn)	8,875
No. of shares (post dilution) (mn)	667
Present fair value (Rs)	13
1-yr forward value per share (Rs)	15.3
CMP (Rs)	9.3
Upside (%)	64

Source: Ambit Capital Research

Valuation with and without HITS

We have built in valuation scenario for WWIL with and without HITS. Our numbers suggests that the upside to WWIL's current market price depends entirely on a successful HITS launch and hence we note the risks involved.

Valuation difference with and without HITS

	HITS	Without HITS
No of subscribers by FY15E (mn)	5.0	0.49
Revenue CAGR FY08-FY15E (%)	32.6	14.9
EBITDA Positive	FY11E	FY09E
Debt required in FY10E-FY12E Rs mn	4,000	0
1-yr forward value per share (Rs)*	15.3	8.5

*assuming dilution for HITS and No dilution for without HITS
Source: Ambit Capital Research estimates

The entire upside from the current levels lies with sucessful execution of the HITS strategy

Our valuation exercise shows that the upside potential for the company lies only with its success in HITS. Even though there exists considerable experience at the top level in the company, HITS is a new product for the company as well as the consumer. A lack of success in this initiative will cap the upside for WWIL as this will be the focus of the management from hereon. We do note the success of the promoter group in emerging as leader in another new technology in the TV distribution space (Dish TV). However, since valuations are highly sensitive to subscriber addition, we still believe that there exists significant execution risk for the company.

Valuation Sensitivity to subscriber addition

Direct subs base by FY15E (mn)	Subs addn per annum (mn)	Target Price(Rs)
0.50	0.1	3
1.00	0.2	4
2.50	0.5	10
4.00	0.8	16
5.00	1.0	19

Source: Ambit Capital Research

Our valuation is also highly sensitive to the rights issue price that the promoters will fix for WWIL, as this would determine the extent of dilution. The higher the price, the lesser the number of shares to be issued to fund Rs4.5bn of rights issue and hence, more the upside from current levels due to lesser dilution to that extent. We have assumed Rs10 as the rights issue price, resulting in a dilution of 450mn new shares. Any improvement from this will be a positive for the stock, and vice versa.

Valuation Sensitivity to subscriber addition

Rights issue Price (Rs)	Resulting Dilution (mn shares)	Target Price (Rs)
9	500	14.2
10	450	15.3
11	409	16.3
12	375	17.2
13	346	18.1
14	321	18.9

Source: Ambit Capital Research

Excluding HITS, WWIL is fairly valued at current levels.

WWIL Relative Valuation

Analogue Subscription fee (Rs mn)	1,031
Analogue Carriage fee (Rs mn)	937
Analgoue revenues (Rs mn)	1,968
Analogue ARPU (Rs)	180
Analogue Subscribers (mn)	0.9
Digital Subscriber acquisition cost (Rs)	1,000
Digital Subscribers (mn)	0.25
Acquisition cost	
Analogue Price/sales Multiple (x)	2.0
Analogue Mcap (Rs mn)	2,062
Carriage fee multiple @1	937
Digital Subs Mcap (Rs mn)	250
Total Market Cap (Rs mn)	3,249
No of shares (Pre dilution)	217
Share Price (Rs)	15
Price to sales FY08 (x)	1.2
Price to sales FY09E (x)	1.0

Source: Ambit Capital Research

Appendix- HITS

What is HITS?

Basically there are two ways in which one can digitize the cable networks; viz. via digital head ends (big dishes needed to receive signals from the satellites) at the MSOs end, and through Head-End-In-The-Sky (HITS).

In the on-the ground digital head-ends, in order to digitize one city for example, the MSO will have to install one digital head-end in that city, (which will cost ~Rs25mn-40mn). The digital head-end will receive the signals from different broadcasters and convert them to digital. These digital signals will then be sent to the local cable operators' offices in that city through a coaxial or fiber optical wire. The local cable operator will receive these digital signals and distribute them to the consumer homes in his network through his cable. The consumers will have to use a set-top-box to decode the digital signals which are encrypted so as to allow the consumer to view only those channels that the consumer has paid for (this is managed through smart card installed in the STB).

Digital cable makes converting large and scattered cable networks into digital cumbersome and costly because of the following reasons;

1. All the operations are decentralized and city based. Hence, one needs to install a digital head-end in each of the city in which services are to be offered. This raises the fixed costs.
2. More head-ends are required if the channels to be received are hosted by different satellites, as the dish has to aim at the satellite in order to receive signals from it.
3. Presence of technical team is required in each city in which the digital head-end is installed.
4. The cost of laying fiber from the MSO's city office to the LCO's office increases if LCOs are highly dispersed and more than one per city.
5. subscriber management is city-wise.

HITS is an improvement to this technology which avoids many of these costs associated with digital cable with digital head-ends. Under HITS, instead of receiving T.V. channels through on-the ground digital head-ends, all channels are received by one big dish (which costs Rs350mn), encrypted and then sent to transponders leased on a satellite, which then becomes a digital head-end-in-the-sky. Now, these channels can be received anywhere in the country through small receiving units (which cost Rs0.35-Rs0.4mn as against Rs25mn-Rs40mn per city under digital head-end mode), at the LCO's end. The LCO receives digital signals directly through satellite and hence there is no need to connect to him through wire. Thus, HITS gives the MSO the capability to digitize the entire country with one digital head-end on the ground and transponders on the satellite. This makes the subscriber management throughout the country highly centralized and easy to manage.

It can be said that HITS is actually a DTH technology, with the only difference that the receiving dish is installed at the LCO's office instead of at the consumer homes as is the case in DTH technology.

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