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FOR PRIVATE CIRCULATION

Saurabh Gurnurkar
saurabh.gurnurkar@kotak.com
+91 22 66341273

Dipen Shah
dipen.shah@kotak.com
+91 22 66341376

UTV Software Communication Ltd.

Price: Rs.157 | **Recommendation: BUY**

Price target: Rs.221

We see UTV Software Communication Ltd. (UTV) as an integrated player in the television and film segments of the Indian media industry, with significant interests across different segments like TV content, airtime sales, movie production, movie distribution, animation, ad film making, dubbing and post production. In addition to these segments the company also owns a 49% stake (through a JV) in Hungama TV, a kids' segment broadcasting channel. Given our macro-expectation of strong growth in the media space, we believe, UTV could be among the gainers with its presence across different segments. While movie revenues are expected to accrue in tune with the pipeline, we expect revenues from the television segment to jump in FY07 with increasing content supply, more profitable air time sales and contribution from the animation segment. We are of the opinion that the significant investments across businesses in the past fiscal are expected to start paying off in terms of the improving margin profile for the company going forward. We expect UTV to report an EPS of Rs.7.8 in FY07 and Rs.12.1 in FY08. At the current levels the stock is available at 13x FY08E earnings and 1x FY08E book value. Our DCF analysis throws up a fair value of Rs.221. We recommend a BUY.

Investment argument

- **Diversified presence in a growth domain:** The media & entertainment (M&E) industry in India is expected to be one of the fastest growing sectors in the Indian economy. According to a FICCI estimate, the sector currently earns revenues worth about Rs.201.3bn and is expected to grow at a CAGR of 17.7% over the coming five years. With revenue contributions from different segments in media like television, movies, animation and post production, UTV has a reasonably diversified revenue base and could shield itself on the downside from a significant downturn in any particular segment.
- **Higher revenue growth and profitability from Television:** UTV plans to ramp up its quantum of content supply to various channels significantly over the coming quarters, which is expected to drive profitable revenue growth from this business. The expected increase in the modes and avenues for content delivery (platforms like DTH, broadband etc) is also expected to benefit content suppliers like UTV. We also expect greater revenues and profitability from the air time sales segment on the back of increasing popularity ratings and realizations for its 'managed' air time slots.
- **Continued scale up expected in movie business:** UTV is expected to scale up its movie business with continued investments in different projects that is expected to drive revenue growth going forward. For FY07 the company has lined up a couple of major releases in the Hindi and English spaces; though FY08 is expected to see a major chunk of releases from the existing pipeline. We are positive about UTV's emphasis on production, content selection/filtration ability and intent to scale up non-theatrical revenues. These factors are expected to provide margins of safety in an otherwise volatile business. The segregation of the creative and financial aspects in movie production has curtailed costs, making the business relatively more profitable as compared to the past.

Stock details

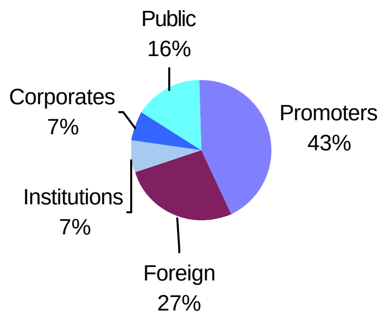
BSE code	: 532619
NSE code	: UTVSOF
Market cap (Rsm)	: 3120
Free float (%)	: 57.29
52-wk Hi/Lo (Rs)	: 259/130
Avg. Daily Volume (BSE+NSE)	: 41125
Shares o/s (mn)	: 19.50

Summary table (year end Mar)

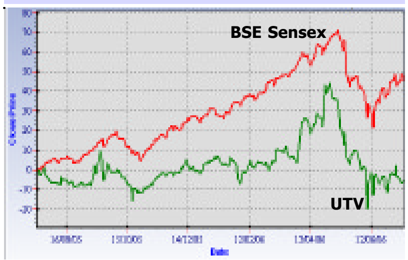
Rs mn	FY06	FY07E	FY08E
Sales	2,087	2,051	2,702
Growth (%)	18.0	(1.7)	31.8
EBITDA	108	309	422
EBITDA margin (%)	5.2	15.1	15.6
Net profit	92	152	237
Net cash	(92)	(622)	(1,243)
EPS (Rs)	4.7	7.8	12.1
Growth (%)	(43.4)	64.4	55.7
CEPS	7.1	10.6	15.4
DPS (Rs)	0.0	0.5	1.0
RoE %	5.8	7.1	8.3
RoCE %	5.4	8.9	10.2
EV/Sales (x)	1.4	1.2	0.7
EV/EBITDA (x)	27.5	7.9	4.3
P/E (x)	33.1	20.1	12.9
P/Cash Earnings	22.0	14.8	10.2
P/BV (x)	1.7	1.3	0.9

Source: Company & Kotak Securities - Private Client Research

Shareholding pattern



One-year performance (Rel to Sensex)



Source: Capitaline

- **Animation order-book and ramp up adds to optimism:** UTV has an order-book of close to $30mn executable over the next 36 months in this segment. With the completion of a new 250-seat facility and recent employee additions, this segment is expected to start contributing to revenues from FY07 onwards. The higher profit margins from this segment are also expected to improve the margin profile for UTV going forward.

- **'Hungama's improving performance is a positive:** UTV's 49% holding in the JV operated Hungama channel is a positive for shareholders given the improving performance of the channel. Operationally the channel enjoys good ratings in the target segment and is expected to break even by Q2FY07. Though Hungama's current valuation by the investor (Astro) places an additional Rs.30 of value per share for the UTV shareholder, we have not included this upside in our projections/ price target.

  We expect revenues to grow at a CAGR of 14% over FY06-FY08E; given the improving margin profile the profits are expected to grow at a CAGR of 60% over FY06 - FY08E. This would translate into earnings per share of Rs.7.8 and Rs.12.1 in FY07 and FY08 respectively on the current equity.

Valuations

- The stock is available at attractive valuations of 12x FY08E earnings and 1x FY08E book value. Our DCF valuations incorporate a 4% growth in perpetuity and a 12.5% WACC. Based on these, we arrive at a fair value of Rs.221 for UTV, a 42% gain from the current levels. BUY.

Key Risks

- **Earnings remain sensitive to the volatile movie segment:** We note that the movie segment contributed around 63% of revenues (Rs.1.31bn) and 55% of the EBIT (Rs.107mn) in FY06. Going forward we expect the movies segment to contribute significantly in terms of revenues and EBIT and expect this segment to contribute around 40-50% of revenues in FY07 and FY08.

  We note that due to good process development and project monitoring initiatives UTV's risks are lesser than most other producers but are of the opinion that returns from this business could remain volatile and depend on commercial fate of projects.

- **Further delays in animation segment:** A delay in ramp up or lesser than expected progress on the order book from the animation segment could impact our earnings estimated negatively.

COMPANY BACKGROUND

UTV Software Communications Ltd is one of India's integrated and diversified media houses with interests in Films, Television content, Broadcasting and other Allied services. UTV started of in 1990 as a content and ad film producer of eminence. The company's television content division found its place during the satellite television revolution in India when Zee TV was launched in 1992; the company produced four of the channel's shows. Subsequently in 1995 UTV pioneered a first by launching India's first daily soap, Shanti, on Doordarshan.

Over the years, UTV diversified (through a mix of organic and in-organic means) into post-production, airtime sales, broadcasting, dubbing, movie production and distribution and also into the animation space.

Time line

Activity	Time line
Incorporation of UTV	1990
TV Content for the newly launched Zee TV	1992
Post Production	1995
Movie Distribution	1996
Enters animation segment by acquisition	1998
Hungama TV through a JV	2004
Initial Public Offering	2005
Expansion of animation and post production facilities	2006

Source: Company

Subsidiaries and JV's

UTV has set up various subsidiaries across the USA, UK and Malaysia in line with the ramp up of its movie distribution activities and a joint venture that marks its foray into the broadcasting space. The company through it subsidiaries in the UK and USA caters to the lucrative overseas movie distribution segment. Over the years with the growing appeal of Indian movies amongst the sizeable Indian diaspora, these subsidiaries have contributed sizably to the company's financial performance.

Through its US subsidiary UTV also looks at international co-production deals (ex: Namesake, a co-production with Fox Searchlight Productions) and the animation space in addition to movie distribution.

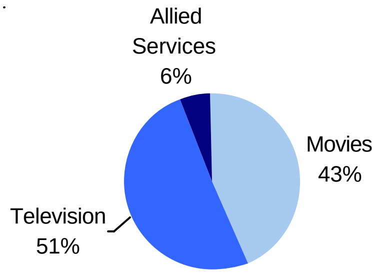
Subsidiaries and JV's

Subsidiary/JV	Comments
United Entertainment Solutions Private Limited	Post Production, SFX.
UTV Communications (USA) LLC	Movie distribution, International movie co-production and animation
UTV Communication (UK) Limited	Movie acquisition, syndication and distribution
UTV Communications (Mauritius) Limited	Movie acquisition, syndication and distribution
UTV International Holdings	Holding company for Malaysian Antah UTV communications
JV- United Home Entertainment Private Limited (UHE)	Broadcasting venture-Hungama TV

Source: Company

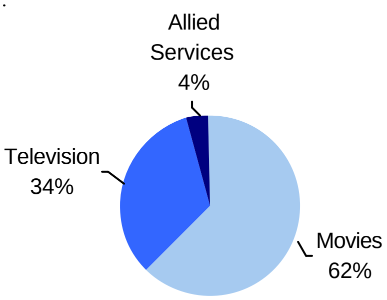
Business Segments

Revenue Break up FY05



Source: Company

Revenue break up in FY06



Source: Company

Movies

UTV currently has close to 4-5 movies that are under various stages of production or are ready for release across different points in this fiscal. It has distribution rights (local/international/both) for another 3 Hindi movies. UTV also drives growth in this segment through other allied revenue streams. In this context, the company recently acquired Miramax film library rights for the next 10 years across all platforms for almost 130 International films. The company is also likely to distribute a good number of English movies in India in FY07 and FY08 from the Miramax library.

We opine that UTV is one of the faster growing and professionally managed movie companies in India. It has developed strong systems for green-signaling and controlling movie projects that could help it adhere to production timelines in an otherwise unpredictable line of business. The distribution model, while currently based mainly on minimum guarantees, is slowly being changed to a lower risk percentage commission model that also could augur well for the company's business model.

Some of the movies that have been produced / distributed by UTV in the past are Swades, D, Rang De Basanti (productions) and distribution projects like Bluffmaster, Taxi 9211, Myth, Unleashed etc.

Television

UTV initially began as a content and ad film production house and over time has worked with most major broadcasters across genres. In FY06, it produced an average of 9.5-10 hours of television content across all major broadcasters. While Star has been the primary customer in FY06, accounting for a sizeable proportion of volumes and revenues, UTV has been diversifying its content clientele towards broadcasters like Sony, BBC, National Geographic etc.

Existing programs on different channels

Current Programs	Channel
Shanno ki shaadi	Star Plus
Gee Boom Ba	Gemini
Bhabhi	Star Plus
Kahaani Haq aur Haqeeqat ki	DD
Kehta hai dil	Star Plus
Shararat	Star Plus
Special Squad	Star One
Bollywood Inc.	BBC World India
Back to the Floor	BBC World India
Business Bites	BBC World India
CNN India dotcom	CNN
CNN South Asia Style	CNN
Pan Asia – Journey's in Asian Cuisine	Star World
Stuntmen of Bollywood	Nat Geo

Source: Company

Within the Television segment UTV is also an established player in the airtime sales (ATS) market in south India and a steady player in the dubbing field. In the air time sales segments, the company has 'managed' around 23 hours of programming in south India across pre dominantly the Sun network and in lesser proportion the Gemini and Udaya channels. In the airtime sales segment the company has gradually ramped up its quantum of 'managed' content across FY06 as shown in the table.

Addition in programming slots for ATS business

Quarter	Program slots managed in Air Time Sales, hours
Q4FY05	6.0
Q1FY06	11.5
Q2FY06	16.5
Q3FY06	22.0
Q4FY06	24.0

Source: Company

Animation

UTV ventured into animation way back in 1998 with the acquisition of Ram Mohan Biographics. The business, christened 'UTV Toons', has worked for many leading entities such as Fox, France 5 and ABC Toon Disney (US) over the years at different stages of engagement across the animation value chain. The business, which has been relatively small at present, is expected to expand rapidly on the back of outsourcing contracts won by the company. The business had revenues of Rs33mn and Rs.15mn in FY05 and FY06 respectively and has seen a change in the cost model from paying animators fixed salaries to paying per second of output generated.

Allied content services-Post-production

UTV has state-of-the-art integrated post-production and SFX facilities that give it a cutting edge advantage in this segment. This segment's business areas include Ad films (ex: Idea Cellular. Hutch Tata Safari), films for post- production and special effects (SFX) and music videos. We opine that SFX and digitization of films could be key growth areas in this segment and there also exists high potential for adopting an outsourcing model for overseas studios. The allied services segment currently contributes to around 4% of revenues i.e. Rs.83.4mn for FY06 and we expect this segment's share in the over all revenue pie to remain around the current levels given UTV's strategic focus towards the other businesses.

Broadcasting (Hungama TV)

In September 2004, UTV launched Hungama TV (through a JV with Astro; UTV's current stake at 49%), a 24-hour channel targeted at kids between the ages 4-14 years. Hungama TV airs a mix of 'live', animated and movie content that is targeted at the growing kids' segment of viewers. The kids' genre in India is a high growth segment that currently accounts for just around 3.2% total television viewership, significantly lower than the global trends. Over the quarters, Hungama has steadily climbed up the popularity ratings and improved its financial performance. The channel is expected to breakeven by Q2FY07.

INVESTMENT POSITIVES

An integrated player in the media sector - A potentially fast growth domain

The media & entertainment (M&E) industry in India is one of the fastest growing sectors of the economy. According to a FICCI estimate, the sector currently earns revenues worth about Rs.201.3bn and is expected to grow at a CAGR of 17.7% over the coming five years.

The industry consists of five major segments viz. filmed entertainment, television, music, radio and print (mainly newspapers & magazines).

Segmental revenues (Rs bn)

	2004	2009E	CAGR (%)
Television	128.7	295	18
Films	56.5	129.3	18
Music	6.7	7.8	3
Radio	2.4	6.5	21.9
Print	7	16	18
Total	**201.3**	**454.6**	**17.7**

Source: FICCI, PwC Study, 2004

...on the back of healthy economic growth expectations

The media & entertainment industry has evidently been riding on the healthy economic growth registered by India over the past few years. The attendant benefit of this steady economic growth has been strong job creation in the new economy sectors and the buoyant services sector. It is this creation of jobs that has led to the rising income levels that India has been experiencing over the past few years.

We believe that this is a trend that is expected to consolidate in the coming years leading to benefits for industries catering to the rising disposable incomes of Indians like telephony (mobile phones), entertainment (F&B, movies, multiplexes, TV channel broadcasters) and the retail sector.

We believe UTV is an integrated player in the Indian television and film industry, with significant interests in segments like TV content, airtime sales, movie production, movie distribution, animation, ad film making, dubbing and post production. In addition to these segments the company also owns a 49% stake (through a JV) in Hungama TV, a kids' segment broadcasting channel. The company's revenue is split reasonably between TV content, airtime sales, movie production and distribution. Thus we believe that the company is shielded on the downside from a significant downturn in any one particular segment. Also, given our macro-expectation of expected strong growth in the media space, we believe, UTV could be among the bigger gainers.

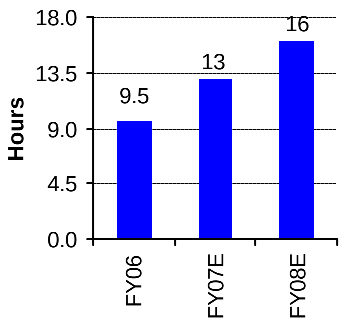
For the company UTV, higher volumes of television content...

Ramp up in television content supply expected in FY07

The company plans to significantly ramp up its quantum of television content over the coming quarters from the nine to 10 hours of content produced per week till the 4Q of FY06.We expect UTV to ramp up its average hours of content per week to around 13 hours by the end of FY07 and subsequently 16 hours by end of FY08.

We opine that UTV has gradually ramped up its content supply post the lull experienced in Q3FY06 on account of the discontinuance of certain existing programs and a delay in the new content coming on air. UTV has also consciously decided to diversify its channel base and is now tapping different channels like Sony, BBC, and National Geographic in addition to the existing Star platform.

Average hours of content supplied



Source: Company, Kotak Securities Private Client Research Estimates

UTV plans to increase the overall hours of content produced on the back of new introductions like Kabhi To Nazar Milao, a daily on Sony from Q1FY07 and Arranged Marriage (Star One) in addition to four other shows expected to come on air during the fiscal across Discovery, Travel & Living and DD. UTV is increasingly diversifying in to non-fiction and regional programming without compromising on its gross average realizations that stand around Rs.700,000 per hour of content produced.

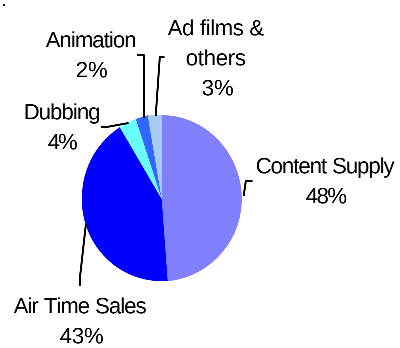
On a sub-segmental basis we expect the TV content revenues to grow to Rs.437mn in FY07 and to a further Rs.538mn in FY08 from the current Rs.341mn in FY06.

Expected program	**Channel, Schedule**
Kabhi To Nazar Milao	Sony, Q1FY07
Arranged Marriage	Star One, Q2FY07
Sohni Mahiwal	DD, FY07
Chamatkar	DD, FY07
Unnamed	Discovery, NA
Unnamed	Travel & Living, NA

Source: Company

...coupled with steady growth in airtime sales are expected to trigger revenue growth and improved profitability:

Revenue break up of TV segment for FY06



Source: Company

The other segment in this line of business-airtime sales is also expected to grow at steady rates going forward and is also expected to show margin improvement as the newly acquired slots start commanding decent advertising rates. The company has added to the number of 'managed' slots over the past fiscal and till Q4FY06 was managing close to 23-24 hours of content per week on an average.

In the process of adding to the hours of 'managed' content , the company normally adopts 'banking' of ad-inventory time that it aims at sweating over time as the newly acquired content slot gains popularity and starts commanding ad rates comparable to other leading programs. We believe the increase in popularity of the program as they reach maturity bodes well for the average realizations / profitability from the air time sales segment.

In our opinion the increase in the slots managed and banking of ad inventory has led to a muted margin performance in the previous quarters, that should improve as the programs gain popularity and the company starts off loading its ad-inventory on better economic terms.

On a sub-segmental basis we expect the air time sales line to report revenues of Rs.470mn in FY07 and Rs.567mn in FY08, an increase from the Rs.300mn reported in FY06.

Within the television segment, the company reports revenues accruing from the dubbing and ad-films business. These sub-segments contributed to around Rs.40mn in FY06. Going forward we expect these lines to grow at steady rates going forward.

We are of the opinion that the businesses of dubbing and post-production provide important synergies to the UTV business model. Though, these are small businesses now, they could be of strategic importance in the future from two angles:

(a) Significant co-production opportunities could possibly come up in these areas, and

(b) These businesses provide synergies to the principal movie and television businesses.

Overall, we expect the television segment to report revenues of Rs.1.11 bn in FY07 (including animation) that are expected to further grow to Rs.1.45 bn in FY08 from the Rs.710 mn reported in FY06.

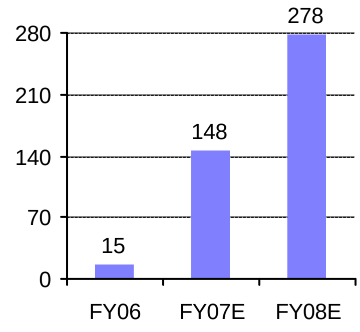
Overall, we expect the margins from the television segment to improve on the back of:

Margin improvement expected across content and air time sales businesses in the television segment

(a) An increase in the number of average hours of content supplied to broadcasters by UTV is expected to positively impact revenues and profitability with EBIT margins expected to increase to 11.5% by end of FY07 from the current 11.2% in FY06.

(b) We expect an increase in revenues from the airtime sales segment on account of back ended addition in 'managed' slots in FY06. We believe that as the newly acquired slots gain popularity UTV will offload its ad inventory at greater realizations. We note that airtime sales for four of the top six programs on Sun TV are managed by UTV. With increasing realizations from these popular programs, the profitability is also expected to go up in the coming quarters. We expect airtime sales EBIT margins to jump from the current 5% to 9-9.5% by end of FY07 on the back of these factors.

Animation segment - Revenue Growth (Rs mn)



Source: Company, Kotak Securities - Private Client Research Estimates

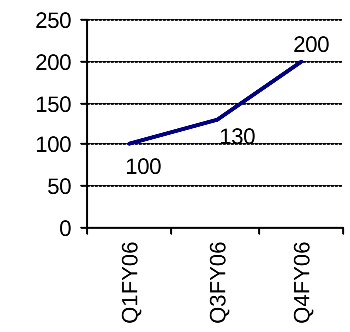
Animation segment revenues expected to start kicking in during FY07, finally…

Over the last fiscal UTV has been investing to upgrade facilities for its animation and post-production businesses. The animation business has taken time to ramp-up, in part due to its facilities getting impacted by the floods in Mumbai during Q1FY06 that is reflected in the lower contribution of Rs.15mn from this business in FY06. UTV has invested a total of Rs.85mn in a 250-seater state of the art animation facility located in Mumbai that has been operational from the current quarter, Q1FY07. In terms of personnel this business at the end of Q4FY06 employed close to 200 people with a complete ramp up expected in this fiscal, FY07.

This business at the end of Q4FY06 had an order book executable over the next 24 months of around $15mn. This order book contains 15 DVD features plus 52 episodes for a TV series and also a 120 part short series.

During Q1FY07 the company has added to its order book by bagging deals that include co-production and outsourcing, these incremental deals have resulted in an enhanced order book of close to $30mn executable over the next 36 months from this segment. Of this close to $20 are pure outsourcing deals that would account for revenues on task-completion and the rest are co-productions which will have a portion of the revenues dependent on the commercial fate of the co-production.

Employee additions in animation



Source: Company, Kotak Securities - Private Client Research Estimates

Given the deal flow in this segment and consequent employee ramp-ups we believe FY07 could see the animation segment starting to deliver in terms of revenues and profitability. We expect revenue growth in this segment to be back –ended towards the second half of fiscal and believe the business will start chipping in from Q1FY07.

The animation segment with its higher gross margins and with most investments in place is expected to contribute to the improving margin profile of UTV in the coming quarters. For FY07, we expect this segment to report revenues of Rs.148mn and grow further to Rs.278mn in FY08, from the current levels of Rs.15mn in FY06.

Animation segment is expected to start contributing to revenues from current fiscal FY07

Television Segment Revenues (Rs mn)

	FY06	FY07E	FY08E
Content Supply	341	438	539
Air Time sales	301	470	567
Dubbing	26	25	24
Animation	15	148	278
Ad films & Others	20	34	46

Source: Company, Kotak Securities - Private Client Research Estimates

Scale up in the movie business to contribute to improvement in financials:

UTV plans to scale up its movie business significantly and this is expected to an important driver for the company's financials going forward. The company has in place a decent pipeline for this business, UTV plans to produce around 4-5 English/Hindi movies and distribute 2 other Hindi movies domestically and/or internationally on a theatrical/DVD/satellite platform over the next fiscal. In terms of movie business FY07 is expected to be a relatively quiet year marked by major releases like Namesake and Don in the second half of the year. Going forward FY08 is expected to be an eventful year with a chunk of releases lined up in the year. Apart from these projects UTV also has rights to the Miramax library (close to 130 English titles) for which the company enjoys rights of display over a variety of platforms like Home Video, theatrical and television.

'Namesake' is an international co-production directed by Mira Nair (scheduled Q3), based on the novel by Pulitzer award winning novelist Jhumpa Lahiri. 'Don', (Q3 expected) is a widely talked about Hindi release being distributed by UTV starring Mr. Shahrukh Khan.

Pipeline of movies - a few of the expected projects

Production	Distribution
Chup Chup Ke - Released in Q1FY07	Rooh - Expected in Q4FY07
Blue Umbrella - Expected in Q2FY07	Don - Expected in Q3FY07
Khosla ka Ghosla - Expected in Q2FY07	
Namesake - Expected in Q3FY07	
K-11	
5-Friends	
Baarish	
Rockstar	
Romanchak	
Goal	
Haar Ki Jeet	

Source: Company

The movie segment has been traditionally a highly unpredictable and volatile business to be in. Integrated companies like UTV do have in place a robust system of processes for movie production. In these processes every project is budgeted from start to finish, which enables quick detection of early warning signals when it comes to schedule or time over runs. The company also gets economies of scale from a large number of shows (large quantity of prints released across centers), which helps reduce content costs.

Post our discussions with the management we feel there are two key areas in film production where we feel confident about UTV:

Structured approach, preference for production and diversification of revenue stream could provide margins of safety in the movie segment

(a) The structured approach which leads to a good blend of creativity, corporatization and financial management,

(b) Diversification of the revenue stream: UTV reduces the dependence on domestic theatrical revenues by recognizing importance of other streams such as international distribution, home video, music rights and satellite rights.

We opine that all these processes help to provide a degree of safety within a characteristically volatile business segment, but content will always remain king and thus it becomes vital for players to have the basic quality of content in place. The below par performance of the movie segment in Q3FY06 (Revenues: Rs.178mn and an EBIT of Rs.-70mn) comes on the back of the failure of UTV's two distributed projects in Hindi.

As a strategic intent, UTV has now decided to focus more on the production side where the content generated is in its hands unlike typical distribution projects where the nature of the Indian movie set up entails the distributor a minimal say in the quality of content in most cases. We see this preference towards production as positive because

(a) the company by being involved from the content creation phase is in greater control of the product and

(b) recent distribution projects have witnessed steep bids being tendered, which generally do not pose a favorable risk-reward ratio.

In FY06 the movies business reported revenues of Rs.1310mn and accounted for 63% of revenues. This healthy figure was on account of the bumper success of one co-production and international distribution project-Rang De Basanti. We are of the opinion that a contribution in similar proportions cannot be expected from this segment given the volatile nature of the movie business. Given the amount of capital employed and management's expectations on quality of content we believe that the big screen (movie) revenues should be around 40-50% of revenues going forward.

The company has invested about Rs.750mn in the movie business currently. We believe this figure is likely to go up to around Rs850mn going forward given the company's pipeline of projects. The evolving multiple revenue streams for its movies: in terms of DVD rights, satellite rights, music and possibly merchandising in the case of successful projects do diversify the company's dependence on purely theatrical earnings to an extent. The growing DVD and home video market are also expected to provide complementary revenue streams for production houses like UTV.

'Expected EBIT margins at a discount to historical margins reported by the movie segment'

We expect movies to contribute Rs.840mn of revenues, a de growth over the previous year accounting for the possible absence of a blockbuster release this year unlike last year (Rang de Basanti). These revenues are expected to grow to Rs.1125mn in FY08 on the back of the large number of releases lined up for FY08. We have assumed in our projections a lower gross margin of 12-12.5% accruing to UTV's consolidated financials from this business as against an average of 15% achieved over the past five quarters, since its initial public offering.

Hungama's improving performance throws in a positive for UTV shareholders:

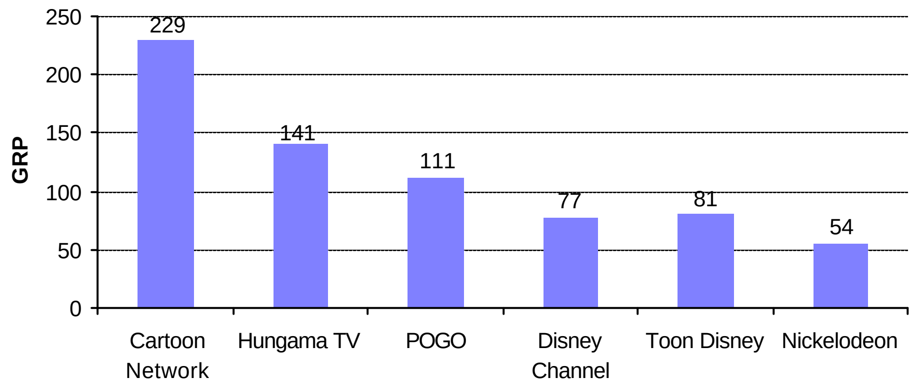
Improving operational performance and popularity is expected to lead to a break even in Q2FY07

Hungama TV is run by a group company UHEL in which UTV holds a 49% stake, the rest being held by promoters and a recent strategic partner in the form of Astro Entertainment Networks, Malaysia. This investor has picked up a 26% stake in Hungama for a consideration of $7mn. UTV has an option of scaling up its stake from the current 49% to 67% if and when required. UTV has invested close to Rs650mn in UHEL till date.

We have not factored in any revenues from Hungama in our projections but are of the opinion that the UTV shareholders have a good amount of value accruing from the JV considering the improving financial performance of the channel. The strategic stake picked up by Astro values the 49% stake of UTV in the JV at approximately Rs.600mn and translates into a value of Rs.30 per share for the existing shareholders of UTV.

According to the latest GRP ratings, Hungama has been making healthy progress in the kids' broadcasting space with its average GRP's increasing by almost 25% in Q4FY06 over the previous quarter, Q3. Hungama appears to have climbed to a healthy No.2 slot for itself in the kids' space, which currently consists of seven players.

Peer comparison for Hungama



Source: GRP rating (ABC), week ended Apr 28, 2006 C&S Household 4-14 yrs

....on course for a breakeven by end of Q2FY07

The channel has been attracting healthy TRP and GRP ratings from the viewer segment that has resulted in healthy growth in advertising revenues for Hungama, which also earns pay revenues by being part of the Star bouquet.

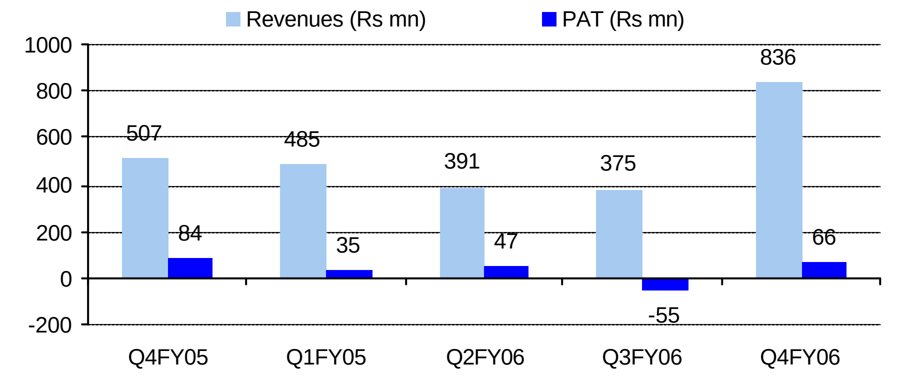
Currently the channel earns close to Rs.5-5.5mn of pay revenues and around Rs.9.5-10mn of ad revenues per month. The cost component as per last available data stands at Rs.20-22mn, indicating a burn of close to Rs.5-6mn per month. Given the increasing ad revenues being generated by the channel on the back of increased popularity and various cost control initiatives implemented by the channel, Hungama is expected to breakeven by the end of Q2FY07.

A possible strategic partner...

UTV has been contemplating the entry of a strategic investor into the company for some period of time now. We believe that any entry of a large strategic investor could bring its experience and domain expertise to the table and probably be positive for the company's future prospects in terms of brand, client reach and scale.

FINANCIALS

Revenue and PAT Trend



Source: Company

Results for Q4FY06

UTV's Q4FY06 results saw a 68% growth in revenues YoY to Rs.836.4mn and a 79% growth in profits to Rs.66.8mn. This growth in the revenue and profit numbers can be attributed to the healthy revenue posted by the movies segment (Rs.626mn, 75% of Q4 revenues) on the back of Rang De Basanti's release (co-production) and the accounting of Bluff Master(distribution) revenues.

Decent Q4 comes after a below par Q3...

The healthy performance in Q4 comes on the back of a below-par Q3FY06 that saw two of UTV's film distribution projects taking a beating at the box-office. We note that the Hindi movie industry structure does not allow for distributor's to have a say in the content creation stage. According to industry sources this is changing with distributor's now getting to preview the project during different stages of production. We thus view the management's preference for self or co-produced projects as a positive in addition to its approach of going in for distribution after vetting the content and bid amounts. We also note that except for the two failed distribution projects in Q3 that led to losses, the company has made profits on the other projects.

For the past five quarters (including Q3FY06), UTV has reported revenues of Rs.1.58bn and an EBIT OF Rs.237mn at EBIT margins of 15%. In our projections we have factored in EBIT margins of a lesser 12-12.5% from the movie segment over the next two fiscals.

In Q4FY06 the TV segment had witnessed margin pressure that could be attributed to:

(a) A significant ramp up in air time sales/ programming slots 'managed' given the company's strategy of 'pre-banking' ad-inventory led to margin erosion in this segment.

(b) A churn in production slate of TV content driven by two programming slots going off-air led to drop in hours of content supplied to broadcasters.

Future Prospects

We believe that the expected jump in different distribution platforms like broadband, DTH and the expected aggressive roll out of new channels could see significant upside for quality content companies. Given the UTV's exposure to different segments in television and films it could stand to gain from any such content explosion.

Going forward on a segmental basis, we expect the television segment (including animation) to report revenues of Rs.1113mn in FY07 and Rs.1453mn in FY08. The movies business is expected to generate revenues of Rs.840mn and Rs.1125mn over the same time period. We expect the smaller allied services segment to report stable growth rates leading to a growth to Rs.97mn in FY07 and Rs.124mn in FY08.

Back ended growth in revenues and profits expected in FY07; seasonality of movie segment and ramp up in content supply towards 2HFY07

Overall, we expect revenues to grow at a CAGR of 16% to Rs.2050mn in FY07 and Rs.2702mn in FY08. We see the margin improvement in the different lines of business to contribute to improved profitability in FY07 and FY08. We see the following levers UTV has for expanding its margins going forward:

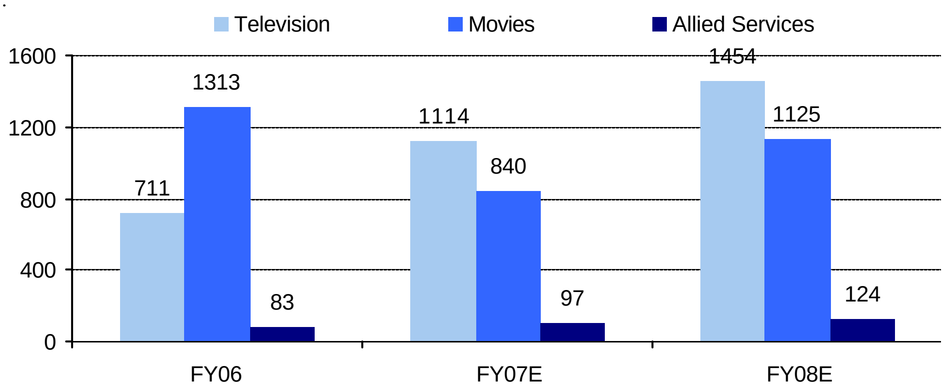
(a) In the TV segment, we expect an improving margin profile on the back of increased hours of content supply and better margins from air time sales due to gradual air-time offload on better terms from recently acquired programming slots.

(b) We believe that the ramp up in the animation segment and order book position lends a decent amount of visibility to revenues from this segment. The revenue growth from this segment (11.5% of total estimated revenues in FY08) at higher EBIT margins is expected to improve the margin profile going ahead.

(c) We estimate the movie segment to report EBIT margins of 12% in FY07. We are sanguine on the margin front for this business on account of the emphasis on production projects and the greater number of revenue streams for movies. We note that our expected margins from this business are at a discount to the average EBIT margins of 15% reported by this segment over the past five quarters (including the below par Q3FY06).

The expected revenue growth coupled with the estimated improving margin profile is expected to result in a CAGR growth of 60% over FY06-08 and net profits of Rs.152mn in FY07 and Rs.237mn in FY08. On the current equity base of Rs.194.9mn, this will translate into an EPS of Rs.7.8 in FY07 and Rs.12.1 in FY08.

Segmental revenue outlook (Rs mn)



Source: Company, Kotak Securities - Private Client Research Estimates

EBIT Margins (%)

	FY06	FY07E	FY08E
Television	8.4	11.2	12.3
Movies	8.2	12.0	12.4
Allied Services	31.4	28.5	28.0

Source: Company, Kotak Securities - Private Client Research Estimates

The other assumptions are as under

In our projections, we have not factored in any revenues from the company's JV-Hungama TV, where UTV has a 49% stake. This channel is expected to break even by the end of Q2FY07.

We have assumed a capex of Rs.130mn across FY07 and FY08, mainly towards expansion and modernization of facilities. This would be lesser than the Rs.150mn incurred in FY06 that was towards the new animation and post production facilities put up in Mumbai.

The 'inventories' line in the balance sheet is expected to increase to Rs.755 mn in FY06 due to increase in 'Films under production' to Rs.410 mn from around Rs.180 mn in FY05. Going ahead, we assumed 'inventories' under 'Films under production' to increase in line with the release pipeline. We estimate inventory position of Rs.840 mn in FY07 and Rs.910 mn in FY08.

The company for FY05 has around Rs.950mn of debt on its books comprising mainly of short term nature that is raised for the movie business. In our projections for FY07 and FY08, we have assumed the debt levels to remain static around the current levels.

Valuations

At the CMP of Rs.157 the stock trades at 13x our estimated FY08E earnings, 10x FY08 cash earnings and 1x our FY08E book value.

We have valued UTV on the basis of the DCF methodology with a WACC of 12.5% and a terminal growth rate of 4%. This has given us a fair value of Rs.221 per share.

Our DCF-based price target of Rs.221 provides an upside of 42% from the current price levels. We recommend a **BUY**.

DCF valuation

Assumptions	
Terminal growth (%)	4.0
Beta (x)	1.03
Risk free rate (%)	7.0
Market risk premium (%)	7.0
Cost of equity (%)	14.2
Cost of debt (%)	7.0
Debt (Rs mn)	950
Equity (Rs mn)	3,062
WACC (%)	12.50

DCF

Rs mn	2006	2007E	2008E	2009E	2010E	2011E	2012E	2013E
PAT	**92**	**152**	**237**	**318**	**382**	**471**	**616**	**728**
Depreciation	47	55	63	69	75	81	87	93
Int (1-tax)	-	56	54	40	34	34	27	27
Capex	150	60	70	55	55	50	50	50
NWC change	379	72	193	201	209	217	226	235
FCFF	**(390)**	**131**	**90**	**171**	**226**	**318**	**454**	**563**
Discounted Value	(390)	131	80	135	159	199	252	3,397

Source: Kotak Securities - Private Client Research

The following grid gives a sensitivity analysis based on various scenarios.

Sensitivity analysis

	WACC (%)		
Terminal growth (%)	12.0	12.5	14.0
3.0	217	203	170
4.0	238	**221**	182
5.0	265	244	197

Source: Kotak Securities - Private Client Research

DCF valuation per share (Rs mn)	
Total FCFF	4,222
Less: Net debt	-92
Shareholders' value	4,314
Value per share (Rs)	**221**

Source: Kotak Securities - Private Client Research

KEY RISKS

Earnings remain sensitive to the volatile movie segment

We note that the movie segment contributed around 63% of revenues (Rs.1312mn) and 55% of the EBIT (Rs.107mn) in FY06.Going forward we expect the movies segment to contribute significantly in terms of revenues and EBIT and expect this segment to contribute around 40-50% of revenues in FY07 and FY08.

We note that due to good process development and project monitoring initiatives UTV's risks are lesser than most other producers but are of the opinion that returns from this business could remain volatile and depend on the commercial fate of the projects.

Further delays in animation segment

A delay in ramp up or lesser than expected progress on the order book from the animation segment could impact our earnings estimated negatively.

Profit and loss statement (Rs mn)

Year end March	FY06	FY07E	FY08E
Revenues	**2,087**	**2,051**	**2,702**
% change yoy	18.0	(1.7)	31.8
EBITDA	**108**	**309**	**422**
% change yoy	(56.2)	186.6	36.7
Depreciation	47	55	63
EBIT	**61**	**254**	**359**
% change yoy	(68.8)	317.1	41.4
Net Interest	-	72	72
Other Income	57	22	30
Earnings Before Tax	117	204	317
% change yoy	(45.0)	73.6	55.5
Tax	11	51	79
as % of EBT	9.1	25.0	25.0
Net Income	**92**	**152**	**237**
% change yoy	(43.4)	64.4	55.7
Shares outstanding (m)	19.5	19.5	19.5
EPS (Rs)	4.7	7.8	12.1
DPS (Rs)	-	0.5	1.0
CEPS (Rs)	7.1	10.6	15.4
BVPS (Rs)	93.8	124.9	167.1

Balance sheet (Rs mn)

Year end March	FY06E	FY07E	FY08E
Shareholder's Equity	195	195	195
Reserves	1,645	2,256	3,083
Net worth	1,840	2,451	3,278
Secured Loans	950	950	950
Total Loans	950	950	950
Minority Interest	27	27	27
Net Deferred tax liability	(8)	(8)	(8)
Total Liability	**2,825**	**3,436**	**4,263**
Net Fixed Assets	399	404	411
Investments	165	165	165
Inventory	755	840	910
Debtors	675	693	874
Cash&Bank balances	877	1,406	2,028
Loans & Advances	452	480	555
Other Current Assets	2	4	5
Current Liabilities	504	534	696
Provisions	6	7	9
Net Current Assets	2,251	2,852	3,667
Miscelleanous Expenses	10	15	20
Total Assets	**2,825**	**3,436**	**4,263**

Cash flow statement (Rs mn)

Year end March	FY06E	FY07E	FY08E
PAT	**92**	**152**	**237**
Depreciation	47	55	63
Change in NWC	(379)	(72)	(193)
Operating cash flow	**(240)**	**135**	**106**
Investments	-	-	-
Capex	(150)	(60)	(70)
Investment cash flow	**(150)**	**(60)**	**(70)**
Loans Raised	766	-	-
Dividend	-	(11)	(22)
Financial cash flow	**766**	**(11)**	**(22)**
Other adjustments	368	465	607
Change in Cash	743	529	622
Opening Cash	134	877	1,406
Closing Cash	877	1,406	2,028

Source: Company, Kotak Securities - Private Client Research

Ratio analysis

Year end March	FY06	FY07E	FY08E
EBITDA margin (%)	5.2	15.1	15.6
EBIT margin (%)	2.9	12.4	13.3
Net profit margin (%)	4.4	7.4	8.8
Adjusted EPS growth (%)	(43.4)	64.4	55.7
Receivables (days)	118.0	119.2	118.0
Fixed Assets Turnover	3.5	2.9	3.5
Interest coverage (x)	-	3.5	5.0
Debt/ equity ratio	0.5	0.4	0.3
ROE (%)	5.8	7.1	8.3
ROCE (%)	5.4	8.9	10.2
EV/ Sales	1.4	1.2	0.7
EV/EBITDA	27.5	7.9	4.3
Price to earnings (x)	33.1	20.1	12.9
Price to book value (x)	1.7	1.3	0.9
Price to cash earnings (x)	22.0	14.8	10.2

Research Team

Name	Sector	Tel No	E-mail id
Dipen Shah	IT, Media, Telecom	+91 22 6634 1376	dipen.shah@kotak.com
Sanjeev Zarbade	Capital Goods, Engineering	+91 22 6634 1258	sanjeev.zarbade@kotak.com
Teena Virmani	Construction, Mid Cap, Power	+91 22 6634 1237	teena.virmani@kotak.com
Awadhesh Garg	Pharmaceuticals	+91 22 6634 1406	awadhesh.garg@kotak.com
Apurva Doshi	Logistics, Textiles, Mid Cap	+91 22 6634 1366	doshi.apurva@kotak.com
Saurabh Gurnurkar	IT, Media, Telecom	+91 22 6634 1273	saurabh.gurnurkar@kotak.com
Vinay Goenka	Auto, Auto Ancillary, Sugar	+91 22 6634 1291	vinay.goenka@kotak.com
Saday Sinha	Economy, Banking	+91 22 6634 1440	saday.sinha@kotak.com
Lokendra Kumar	Oil & Gas	+91 22 6634 1540	lokendra.kumar@kotak.com
Shrikant Chouhan	Technical analyst	+91 22 6634 1439	shrikant.chouhan@kotak.com
Kaustav Ray	Editor	+91 22 6634 1223	kaustav.ray@kotak.com
K. Kathirvelu	Production	+91 22 6634 1557	k.kathirvelu@kotak.com

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