Research
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January 4, 2013

Eros International (EROINT)

₹ 207

High growth potential; de-risked model!!!

Eros International, a leading producer/distributor with the largest film library is best positioned to capitalise on changing dynamics of the film entertainment industry. While increasing penetration of multiplex screens & higher average ticket prices will lead to robust growth in theatrical revenue, advent of premium TV, pay per view, online media & rise in cost of satellite rights on the back of imminent digitisation will help monetise the long tail more effectively. Bundled deals with satellite channels and guaranteed 39% cost recovery from its parent make the company's business model relatively de-risked. A consistent track record in delivering three to four movies in the top 10 grosser at box office each year & strong movie slate lends stability & visibility to future earnings. Eros is expected to post revenue & PAT CAGR of 19.4% and 19.1%, respectively, over FY12-15E. Eros is cheaply valued compared to other media businesses. Given the structural shift in film entertainment space, a re-rating is on the cards. We initiate coverage with BUY and TP of ₹ 267.

Explosive growth in cinema screens to drive theatrical revenue…

While just one movie crossed ₹ 100 crore box office collection in 2008 and 2009, 11 movies have breached this barrier in 2012, largely fuelled by explosive growth in multiplex screens and rising ATP. Multiplex screens that contribute ~50% of box office collection are expected to grow from 1225 in 2011 to 2200 in 2016. Largest grossing film in 1995 released with 500 prints, in 2009 with 1000 prints while in 2012 largest grosser had about 3500 prints. Theatre screens would continue to grow at a scorching pace given that India remains severely under penetrated.

De-risked business model

For large budget movies, Eros generally recovers whole production cost even before theatrical release in the form of sale of music rights, satellite rights and 39% guaranteed cost recovery from its parent for international distribution. With the advent of premium TV, pay per view and increasing price of satellite rights, its dependence on theatrical revenue would further decline from ~40% currently. This not only makes Eros far less risky than its peers but also ensures healthy return ratios.

Robust earnings growth to re-rate stock

The company is trading at a significant discount to other media companies in spite of having robust return ratios. We believe the structural shift in the film industry would lead to a re-rating of the stock. We have valued the stock at 12x FY14E to arrive at a target price of ₹ 267.

Exhibit 1: Valuation Metrics

(Year-end March)	FY11	FY12	FY13E	FY14E	FY15E
Net Sales (₹ crore)	707.0	943.9	1,128.0	1,327.6	1,604.9
EBITDA (₹ crore)	156.1	212.4	258.1	312.5	376.8
Net Profit (₹ crore)	117.2	147.8	177.0	204.0	249.5
EPS (₹)	12.8	16.1	19.3	22.2	27.2
P/E (x)	16.2	12.8	10.7	9.3	7.6
Price / Book (x)	2.8	2.3	1.9	1.6	1.3
EV/EBITDA (x)	12.5	9.6	8.1	6.5	5.0
RoCE (%)	17.4	16.2	17.0	17.9	18.7
RoE (%)	17.5	17.7	17.5	16.8	17.0

Source: Company, ICICIdirect.com Research

Rating Matrix

Rating	:	**Buy**
Target	:	₹ 267
Target Period	:	12-15 months
Potential Upside	:	29%

YoY Growth (%)

(YoY Growth)	FY12	FY13E	FY14E	FY15E
Net Sales	33.5	19.5	17.7	20.9
EBITDA	36.0	21.5	21.1	20.6
Net Profit	26.1	19.7	15.3	22.3
EPS	26.1	19.7	15.3	22.3

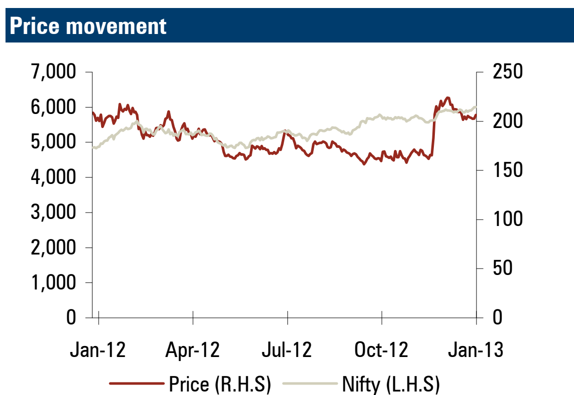
Valuation Summary

	FY12	FY13E	FY14E	FY15E
P/E	12.8	10.7	9.3	7.6
Target P/E	16.6	13.8	12.0	9.8
EV / EBITDA	9.6	8.1	6.5	5.0
P/BV	2.3	1.9	1.6	1.3
RoNW	17.7	17.5	16.8	17.0
RoCE	16.2	17.0	17.9	18.7

Stock Data

Market Capitalization	₹ 1898.7 Crore
Total Debt (FY12)	₹ 436.2 Crore
Cash and Investments (FY12)	₹ 300.4 Crore
EV	₹ 2034.6 Crore
52 week H/L	224 / 156
Equity capital	₹ 91.8 Crore
Face value	₹ 10
MF Holding (%)	2.3
FII Holding (%)	6.3

Price movement



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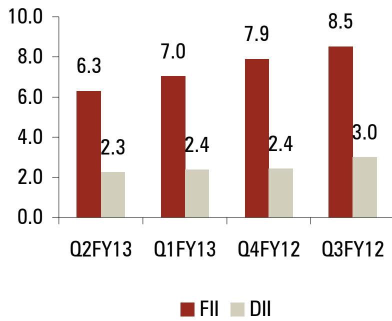
Shareholding pattern (Q2FY13)

Shareholder	Holding (%)
Promoters	77.8
Institutions	8.55
Public	13.65

FII & DII holding trend (%)



Company background

Eros International Media Ltd is a leading company in the Indian film entertainment industry that acquires, co produces and distributes Indian language films in multiple formats. The company was incorporated in 1994 and listed in 2010.

Eros co-produces 60% of the movies while the rest are either acquired or produced. The company has had long industry associations, a consistent track record of releasing three to four movies of the top 10 movies in the box office and a wide distribution network. Eros has been able to develop strong relationships with key figures in the Indian film industry, which help it secure key films and build a strong portfolio of movies. Some of the big starrer movies to which Eros has the rights include Ra One, Housefull, Housefull 2, Ready, Rockstar, Golmaal 3, Om Shanti Om, Hey Babyy, Love Aaj Kal, De Dana Dan, etc.

The company distributes movies to Indian multiplexes and single screens through its internal distribution offices in Mumbai, Delhi, Punjab, Chennai and Mysore and also through sub-distributors. Outside India, the company leverages on its parent's (Eros International Plc and Eros Worldwide) presence. The parent has offices in Dubai, Singapore, the US, the UK, Australia and Fiji.

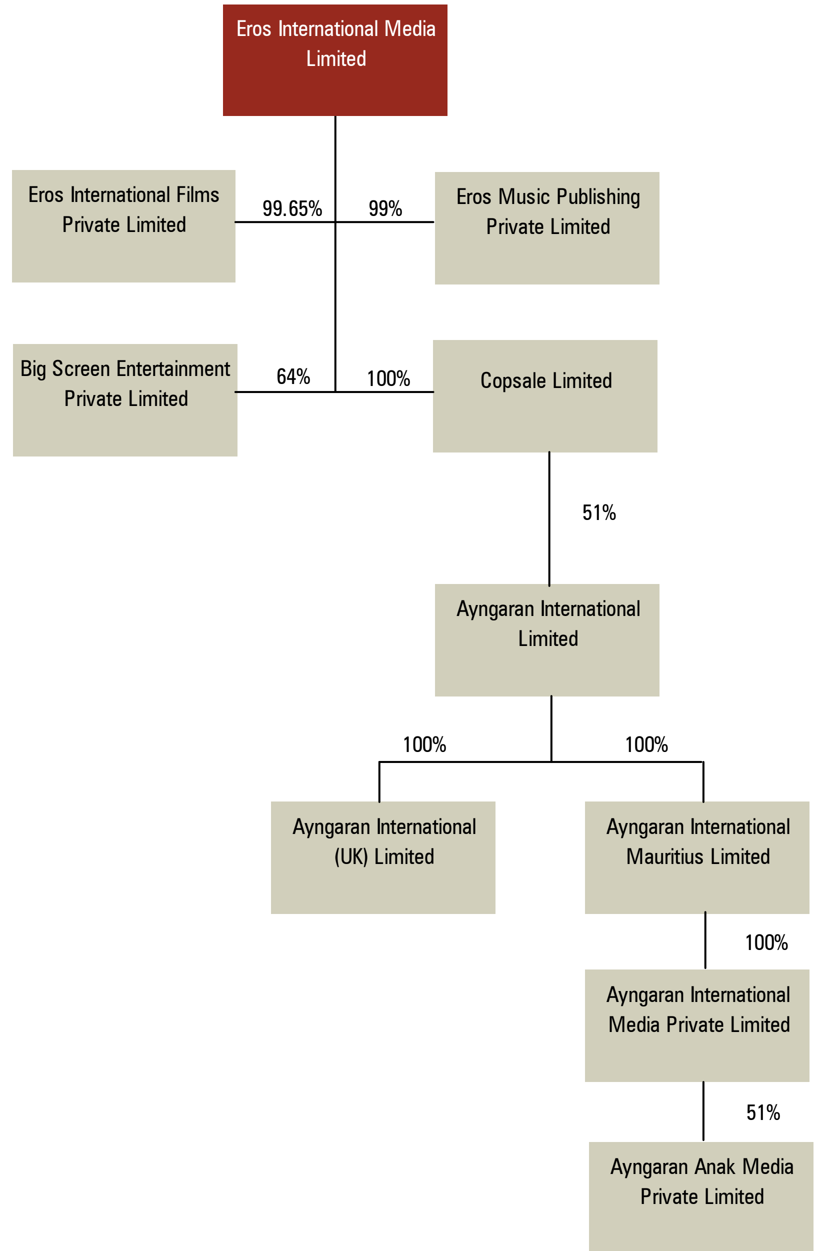
Eros has a movie library of 1100+ movies, which it licenses to Indian broadcasters. The company has had deals with all top four Hindi GEC broadcasters viz. Star Network, Sony, Zee and Colors. The satellite licenses are monetised around the world through the parent.

Eros also has access to a global network for the digital distribution of content including movies, music, videos, clips and other video content. It distributes content through IPTV, VoD and online internet channels. The Eros channel on YouTube has exceeded one billion views. The company has recently launched Eros Now, an on-demand entertainment portal accessible via internet enabled devices.

The company directly acquires Hindi and regional language films other than Tamil movies. Also, a few Tamil movies have been acquired by Eros directly as well. The company made a major foray into the Tamil film industry by acquiring a 51% stake in Tamil film distribution house Ayngaran.

Eros Music Publishing signs up artistes and composers with a view to collecting and administering music publishing revenues generated worldwide from the use of the work of such artists.

Exhibit 2: Eros - group structure



Source: Company, ICICIdirect.com Research

Investment Rationale

Changing dynamics of film industry

The Indian media industry grew by a handsome 11.7% in 2011 even as the economy had started showing signs of a slowdown. In spite of the previous slowdown in 2009, the industry grew at a CAGR of 9.1% in 2007-11. The feature of the media industry, of late, has been increasing penetration of digital system – in the form of DTH and digital cable in TV, shift from analog screens to digital screens, increasing use of technology like animation, VFX, etc. in films and digital advertising. Going forward, the industry is expected to grow at a CAGR of 14.9% from ₹ 728 billion in CY11 to ₹ 1457 billion in CY16.

Exhibit 3: Media industry

₹ billion	2007	2008	2009	2010	2011	CAGR (07-11)%	2012E	2013E	2014E	2015E	2016E	CAGR (11-16)%
TV	211.0	241.0	257.0	297.0	329.0	11.7	380.0	435.0	514.0	618.0	735.0	17.4
Print	160.0	172.0	175.2	192.9	208.8	6.9	226.0	246.8	270.0	294.9	323.4	9.1
Film	92.7	104.4	89.3	83.3	92.9	0.1	100.0	109.7	121.1	134.5	150.3	10.1
Radio	7.4	8.4	8.3	10.0	11.5	11.7	13.0	16.0	20.0	24.0	29.5	20.7
Music	7.4	7.4	7.8	8.6	9.0	5.0	10.0	11.3	13.1	15.4	18.2	15.1
OOH	14.0	16.1	13.7	16.5	17.8	6.2	19.5	21.5	23.6	26.0	29.0	10.3
Animation	14.0	17.5	20.1	23.6	31.0	22.0	36.3	43.0	51.1	61.0	69.0	17.4
Gaming	4.0	7.0	8.0	10.0	13.0	34.3	18.0	23.0	29.0	37.0	46.0	28.8
Digital Advertising	4.0	6.0	8.0	10.0	15.4	40.1	19.9	25.8	33.5	43.7	57.0	29.9
Total	514	580	587	652	728	9.1	823	932	1076	1254	1457	14.9

Source: FICCI-KPMG report 2012, ICICIdirect.com Research

Film industry commences turnaround

The film industry has been under pressure from many one-offs, which have stalled its growth in the last few years. The multiplex strike and fighting for a higher revenue contribution from producers impacted the industry's fortunes for two months in 2009 when none of the movies were released. Also, the strike meant late cash flows for producers, jeopardising projects that were under production, thus affecting a part of 2010 as well. Year 2010 was characterised by a severe lack of good content. Though many big starrer movies were released during 2010, only a few witnessed any success at the box office. In 2011, the cricket world cup, in which India emerged victorious, had an adverse effect on the film industry.

Exhibit 4: Film Industry

₹ billion	2007	2008	2009	2010	2011	CAGR (07-11)%	2012E	2013E	2014E	2015E	2016E	CAGR (11-16)%
Domestic Theatrical	71.5	80.2	68.5	62.0	68.8	-1.0	73.5	80.2	88.0	97.2	108.0	9.4
Overseas Theatrical	8.7	9.8	6.8	6.6	6.9	-5.6	7.5	8.3	9.2	10.2	11.5	10.8
Home Video	3.3	3.8	4.3	2.3	2.0	-11.8	1.7	1.4	1.2	1.0	0.9	-14.8
C&S Rgihts	6.2	7.1	6.3	8.3	10.5	14.1	12.0	13.7	15.6	17.8	20.3	14.1
Ancillary streams	2.9	3.5	3.5	4.1	4.7	12.8	5.4	6.2	7.2	8.3	9.6	15.4
Total	92.7	104.4	89.3	83.3	92.9	0.1	100	109.7	121.1	134.5	150.3	10.1

Source: FICCI-KPMG 2012, ICICIdirect.com Research

However, the latter part of 2011 witnessed a turnaround in the film industry especially in the third quarter of CY11 with movies like Singham and *Delhi Belly* followed by *Ra.One* and *Don 2* in the last quarter. The turnaround was led by a strong quality of content and the trend continued in 2012 as well. While only five movies grossed more than ₹ 100 crore at the box office in 2011, 11 have crossed that milestone in 2012.

While only one movie crossed the ₹ 100 crore box office collection mark in 2008 and 2009, eleven movies have crossed the benchmark in 2012

Exhibit 5: Movies grossing over ₹ 100 crore at box office

Year	Movies grossing over ₹ 100 crore
2008	Ghajini
2009	Three Idiots
2010	Dabangg Golmall 3
2011	Ready Singham Bodygaurd Ra One Don 2
2012	Agneepath Housefull 2 Rowdy Rathore Bol Bachchan Ek Tha Tiger Barfi Jab Tak Hai Jaan Talaash Dabangg 2 Khiladi 786 Son of Sardaar

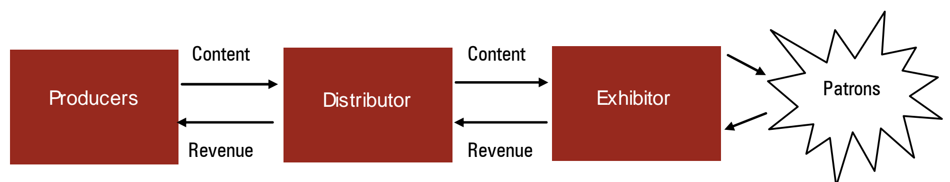
Source: Company, ICICIdirect.com Research

The film industry grew at a CAGR of a mere 0.1% in CY07-11 to ₹ 92.9 billion, mainly due to the multiplex strike and the cricket world cup affecting revenues from 2009 to early 2011. However, the trend seen in the latter part of 2011 of strong content has continued in 2012 and is expected to drive growth subsequently.

Value chain in industry

The value chain in the industry includes the producer who produces the content, distributor who distributes the content from producers to exhibitors and exhibitors including single screen and multiplexes who provide the last mile connectivity and display content to patrons. While the content moves from producer-distributor-exhibitor, the revenue collected from patrons moves in the reverse direction.

Exhibit 6: Value chain



Source: Company, ICICIdirect.com Research

The box office collections received from exhibitors is shared in different ways with distributors. Multiplexes share 50% of net box office collections with the distributor in the first week, 42.5% in the second, 37.5% in the third and 30% from the fourth week onwards. However, the single multiplex and single screen theatres, due to a lower bargaining power, end up sharing ~60% of the net collections with the distributor.

Many models have been adopted in the past for revenue share between producers and distributors. Some of the most widely used ones include:

Exhibit 7: Revenue share between distributor and producer

Minimum Guarantee plus royalty model	Commision Model	Outright sale model
- distributor pays a fixed amount to acquire rights - if revenue exceedes minimum guarantee, distributors' costs and commisions, its shared in a pre determined ratio - distributor bears the risk - usually used for big budget movies from established production houses	- distributor retains a commision from the revenues and remits the remaining to the producer - risks shared by the distributor and producer - usually used for a small budget movie	- distributor purchases a film's entire exhibition rights for a specified amount - entire risk borne by the distributor

Source: Company, ICICIdirect.com Research

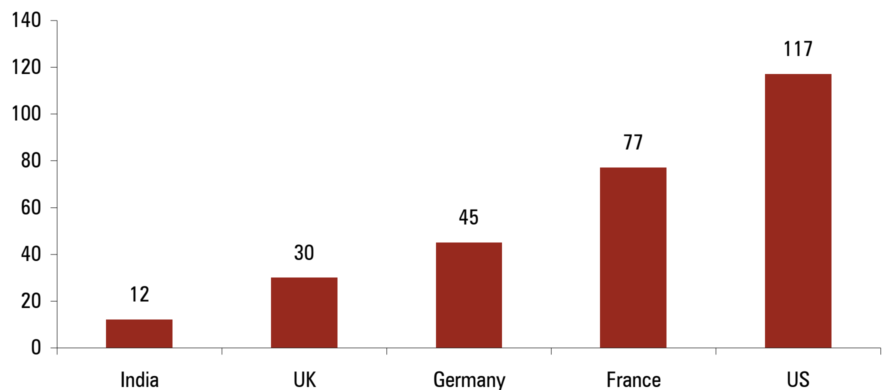
Emerging trends in film industry

Growth in multiplexes

India is highly under-penetrated in terms of the number of movie screens available in terms of population. The number of screens per million populations stood at 12 in India as compared to 117 in the US. This provides huge potential for growth reflected by the growth in multiplex screens over the years. Multiplexes generally provide a better ambience than a single screen theatre and also a choice to consumers with four to six screens in one location. Hence, multiplexes command a premium on ticket prices over the single screen cinemas even at higher occupancy levels. It is well represented by the fact that in spite of total multiplex screens being ~15% of the total number of screens in India, in CY11, multiplexes accounted for more than 50% of theatrical revenues.

India is highly underpenetrated in terms of number of screens per population as compared to countries like US, UK etc

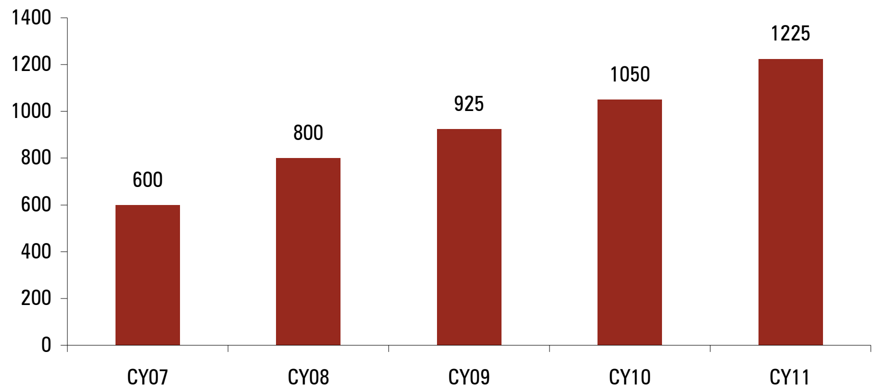
Exhibit 8: Screens per million population



Source: Company, ICICIdirect.com Research

The number of multiplex screens has more than doubled from CY07-11 to 1225 and is expected to grow to 2200 screens by 2016

Exhibit 9: Impressive growth in multiplex screens in India



Source: Crisil estimates, ICICIdirect.com Research

Also, the movies released, of late, have had a wider exposure in the first weekend as compared to those in previous years. While a big budget movie would typically release in 1,200 screens in 2010, the number went up to 2,500-3,000 in CY11. In CY12, some movies were also released across 3,500 screens. The largest grossing film in 1995, Hum Aapke Hai Kaun released with 500 prints. In 2009, 3 Idiots released with 1,000 prints while in 2012 largest grosser Ek Tha Tiger had about 3,500 prints. This signifies the explosive growth in theatre screens in the last couple of years. Theatre screens would continue to grow at a scorching pace given that India remains severely under penetrated.

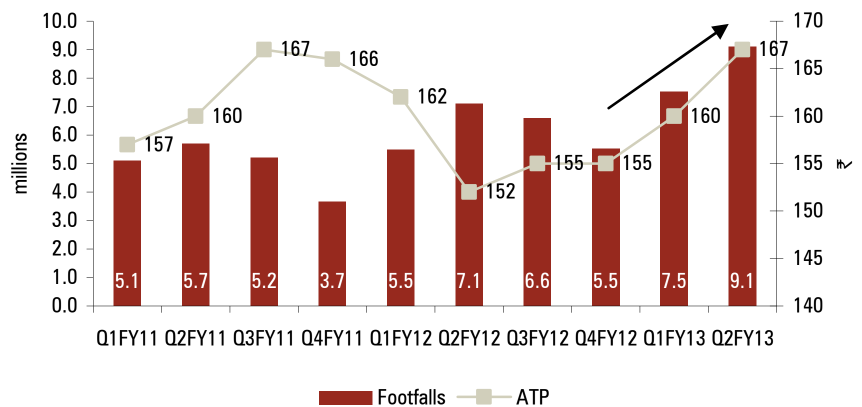
Exhibit 10: Average number of screens for theatrical release

	Big Budget		Medium Budget	
Market	2010	2011	2010	2011
Domestic	1200	2500-3000	600	1000+
International	250	400-500	100-120	100-120

Source: FICCI-KPMG report 2012, ICICIdirect.com Research

PVR Ltd, a leading multiplex chain in the country, has witnessed a continuous increase in its footfalls even at a higher ATP especially in 2012 indicating a jump in the box office collections of the entire industry.

Exhibit 11: PVR - increasing footfalls at higher ATP



Source: Company, ICICIdirect.com Research

PVR Ltd, a leading multiplex chain in the country, has witnessed a continuous increase in its footfalls even at a higher ATP especially in 2012 indicating a jump in the box office collections of the entire industry. The management of Eros has indicated that the change in the industry was brought about by corporatisation in the business leading to better marketing of movies and aggressive expansion plans of multiplexes.

Multiplexes have a strong presence in urban areas. They are currently looking at expansion in Tier II/ Tier III towns and the southern regions, which are currently dominated by single screens. Also, the emergence of 3D films has served well for multiplexes as they can charge a premium for a better viewing experience to the user to capitalise on the rising disposable income seen in Tier II/Tier III towns. According to Crisil estimates, the number of multiplex screens is expected to double in 2011-16 to reach ~2,200 screens. Even at that level, the multiplex penetration in India would be way less than that of some of the developed countries.

A producer/distributor stands to gain from the growth in multiplexes even though the revenue share received from multiplexes chains is lesser than that of single screen entities, as multiplexes command a higher ATP along with higher footfalls leading to a surge in box office collections.

Satellite rights for movies reaching new highs…to grow further thanks to digitisation!!!

Movie acquisition costs have been growing at 30-35%/annum over the last three years. The rise in movie acquisition costs can be attributed to the shortened theatrical window and increasing competition among broadcasters.

The Hindi GEC channel space is characterised by intense competition among the top four broadcasters – viz. Zee TV, Star Plus, Sony and Colors. In a quest to raise the GRPs of channels, broadcasters have turned to acquiring movies, even at a very high cost.

Zee TV was a consistent No. 4 in terms of GRP in the Hindi GEC space owing to its strategy of not investing in high cost content. However, at the fag end of 2011, Zee TV changed its strategy and started acquiring high cost big starrer movies starting with Don 2 and Agneepath. As a result, it has witnessed a strong surge in its market share and, hence, ad growth in FY13. Even Colors had given up its strategy of acquiring high cost movies in mid-2012. However, unable to maintain market share in the Hindi GEC space, Colors has returned to the picture, signing a deal with Eros for seven to eight movies recently for ₹ 95 crore.

Distributors have also built different models to arrive at movie acquisition costs. According to media sources, Ek Tha Tiger was sold at ₹ 50 crore and ₹ 5 crore each for every ₹ 50 crore grossed by the movie at the box office. It turned out to be a blockbuster grossing just below ₹ 200 crore and its C&S rights were sold for ₹ 65 crore eventually.

Exhibit 12: Rising satellite right costs for broadcasters

2009		2010		2011		2012		Yet to release	
Movie	Cost	Movie	Cost	Movie	Cost	Movie	Cost	Movie	Cost
Ghajini	20-25	3 Idiots	30-35	Ra One	35-40	Ek Tha Tiger	65	Dabangg 2	50+
Singh is King	15-20	Housefull	15-20	Bodygaurd	25-30	Don 2	35-40	Talaash	40+
Welcome	10-15	Dabang	10-15	Rajneeti	20-25	Agneepath	30-45	Krrish 3	35-40

Source: FICCI KPMG report 2012, ICICIdirect.com Research

The movie acquisition costs would be further pushed upwards owing to digitisation of the cable & satellite industry. As digitisation plugs the revenue leakage caused by LCOs, MSOs stand to gain. Also, digitisation would provide an opportunity to DTH operators to speed up their subscriber addition. Through DTH or MSO, broadcasters would witness a significant jump in their subscription revenue once under-reporting is done away with.

The jump in the subscription revenue would fuel further competition in the already competitive Hindi GEC channels for good content. The top 4 operators would feel the need to acquire movies apart from other high cost content. We expect movie acquisition costs to remain high subsequently as well.

Though on a lower base, C&S rights for regional cinema have also been doing well buoyed by competition among broadcasters. National broadcasters have been gaining an increasing presence in regional markets. Star and Zee already have regional channels of their own. Zee has also launched a new Bangla movie channel signifying the demand. TV18 (Colors) recently bought the Eenadu group of channels to get a foothold in the regional territory.

Revenues from selling movie rights are expected to grow at a CAGR of 14.2% in 2011-16 to ₹ 20.3 billion.

Overseas theatrical revenue to provide support

The film industry, especially big budget movies by established production houses, has been benefiting from rising exposure to overseas markets. Hindi films have continued to do well in the US, UK and Canada. They have been opening up in previously untapped markets in Latin America, Western Europe and Pakistan. In 2011, Indian films also started gaining acceptance in Taiwan, South Korea and China.

Movies like *Ra One* and *Bodyguard* opened simultaneously in 50 countries. *Three Idiots* had a 29-week theatrical run in Taiwan collecting ~₹ 3 crore. The success prompted distributors to release the movie with subtitles in 230 screens in South Korea and across 900 screens in China with dubbing in Mandarin. However, low and medium budget movies continue to have limited exposure to overseas markets.

The revenue contribution from overseas markets is expected to grow at a CAGR of 10.5% to ₹ 11.5 billion.

Home video no more appealing; ancillary streams offer huge potential…

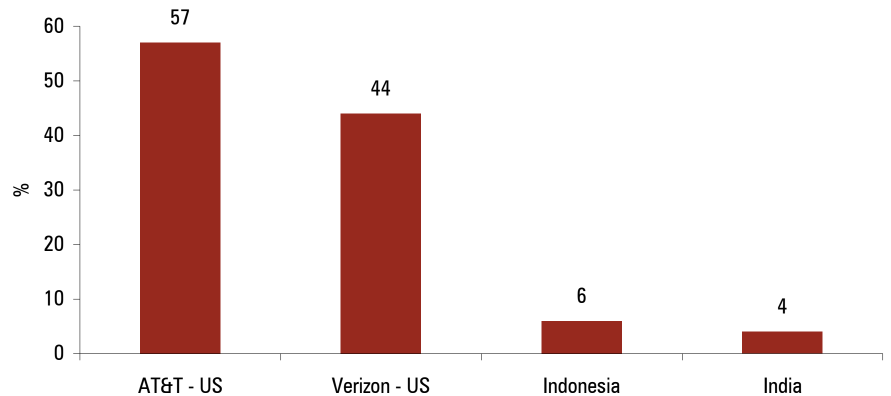
The home video segment has lost its appeal to a distributor due to unchecked piracy. However, piracy can be checked by implementing stringent laws on piracy and by increasing digitisation of screens. Movies shown over a digital screen cannot be easily recorded over a camera. A unique code, which is available only to the exhibitor to unlock the digital signals sent by a distributor, makes it virtually impossible for the signal to be pirated. Currently, 80% of the total screens in India are digital as compared to 15% a few years ago. Digitisation of screens also reduces the distribution cost of a movie to one-fifth.

However, even if piracy is contained, the competition of ancillary revenue streams including pay per view (PPV) on the DTH platform and potentially on digital cable as well and online streaming by operators like Netflix, Amazon and Hulu, would exert downward pressure on the appeal of home video. Such service providers are spending heavily on content licensing to expand their library to attract more subscribers.

India currently has a low smart phone penetration and low data usage as compared to some of the developed or developing countries. However, it has a significant potential to grow owing to various initiatives by operators, handset OEMs and VAS providers such as decreasing device prices, availability of affordable data plans and development of mobile internet ecosystem around consumers in India.

India currently has a low smart phone penetration and low data usage as compared to some of the developed or developing countries. However, it has a significant potential to grow owing to various initiatives by operators, handset OEMs and VAS providers such as decreasing device prices, availability of affordable data plans and development of mobile internet ecosystem around consumers in India.

Exhibit 13: Share of smart phone in total SIM base



Source: Company, ICICIdirect.com Research

Growing internet penetration and higher data usage per subscriber would be a growth driver for ancillary revenue streams of a distributor. The music rights of a movie, though less compared to other forms of revenue, provide a huge potential for growth with increasing internet penetration in the form of ring back tones, paid downloads, etc. According to Ficci, Eros sold its music rights of Ra One for ₹ 15 crore to T Series. Also, growing internet penetration would encourage subscription based online streaming as well.

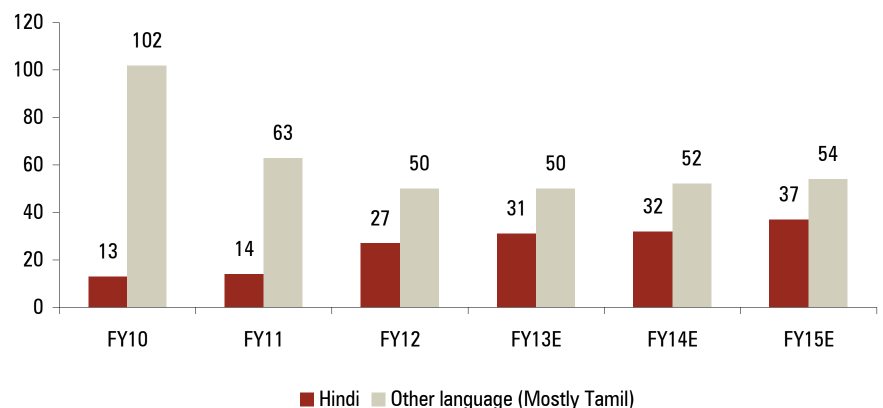
Another key revenue stream that the distributor can exploit remains licensing and merchandising though this stream would offer potential only to a few 'A' category movies. Ra.One, again, would be a classic example for this stream as the movie explored merchandising options through gaming (playstation), digital comics, costumes, novels, action figures, toys, stationary, accessories etc. Eros earned ~₹ 15 crore from the merchandising of Ra.One.

While the home video segment is expected to decline at 14.8% CAGR from CY11-16 to ₹ 0.9 billion, the ancillary revenue stream is expected to witness growth of 15.4% to ₹ 9.6 billion.

Eros – consistent provider of good content

Eros has a strong movie library of 1100+ movies and continues to strengthen the library by adding 75-80 movies every year, which includes ~25 Hindi movies. As per our estimates, ~78% of theatrical revenues are contributed by Hindi movies. Along with the movie library, Eros also has an unparalleled distribution network. Also, long industry associations with key industry players help it acquire/co-produce good quality content. Some of the renowned names in the industry with which Eros has had recent tie-ups include Red Chillies (Shah Rukh Khan), Excel Entertainment (Farhan Akhtar), Illuminati films (Saif Ali Khan), Rajinikanth, etc.

Exhibit 14: Eros - movies released



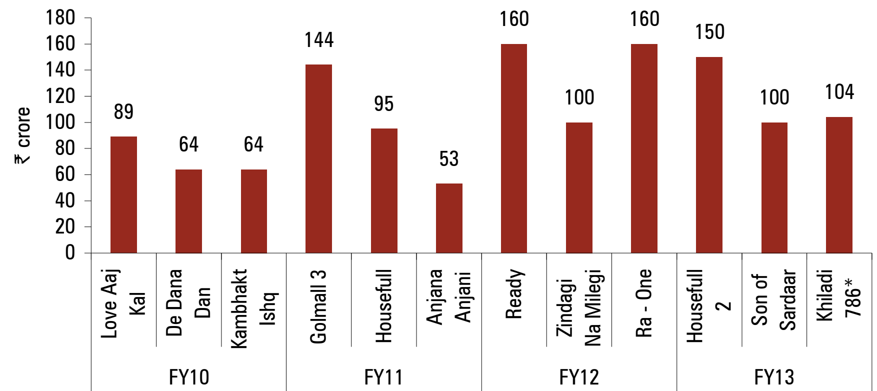
Source: Company, ICICIdirect.com Research

The company has a separate Greenlight board, which consists of Eros executives that run the business in India and abroad. The board executes a thorough review of the film projects based on creative criteria as well as financial criteria. Creative criteria include producer and director skill along with the track record, movie script, star cast, actors & fit for role, genre of movies and likely resonance with audiences and tentative release date and fit with overall slate. Also, financial criteria like prior track record of the actor/director with that genre of movie including return on previous films, expected return on investment, budget of film and fixed price/budget cap are also looked at.

The performance of the Greenlight board has been satisfactory with Eros consistently having three to four films in the top 10 movies at the box office every year since CY09. Even in CY12, the company has had three movies, which have collected over ₹ 100 crore at the box office viz. *Housefull 2*, *Son of Sardaar* and *Khiladi 786 in the Hindi space while Thuppaki in the Tamil space has crossed that milestone*.

The company has been consistently delivering three to four films in the top 10 movies at the box office every year since CY09. Even in CY12, the company has had three movies, which have collected over ₹ 100 crore at the box office viz. *Housefull 2*, *Son of Sardaar* and *Khiladi 786*. *In the Tamil space Thuppaki has crossed that milestone*

Exhibit 15: Eros movies in top 10 grossing movies at box office



** - latest*

Source: Industry, ICICIdirect.com Research

Exhibit 16: Movies released in FY13

Movie	Starcast	Release
Housefull 2	Akshay Kumar, John Abraham	Q1FY13
Vicky Donor	Ayushman Khurana, Jhanvi Gautam	Q1FY13
Ferrari Ki Sawari	Sharman Joshi	Q1FY13
Teri Meri Kahani	Shahid Kapoor, Priyanka Chopra	Q1FY13
Tezz	Ajay Devgan, Anil Kapoor	Q1FY13
Cocktail	Saif Ali Khan, Deepika Padukone	Q2FY13
Shirin Farhad ki to Nikal Padi	Farah Khan, Boman Irani	Q2FY13
English Vinglish	Sridevi, Priya Anand	Q3FY13
Bhoot Returns	Manisha Koirala, JD Chakravarthy	Q3FY13
Chakravyuh	Arjun Rampal, Abhay Deol	Q3FY13
Son of Sardaar	Ajay Devgan, Sanjay Dutt	Q3FY13
Khiladi 786	Akshay Kumar, Asin	Q3FY13
Maatran (Tamil)	Suriya, Kajal Aggarwal	Q3FY13
Thuppaki (Tamil)	Vijay	Q3FY13

Source: Company, ICICIdirect.com Research

The company also has a good movie pipeline till FY14, which provides a certain visibility for earnings till then.

Exhibit 17: Good visibility of forthcoming movies

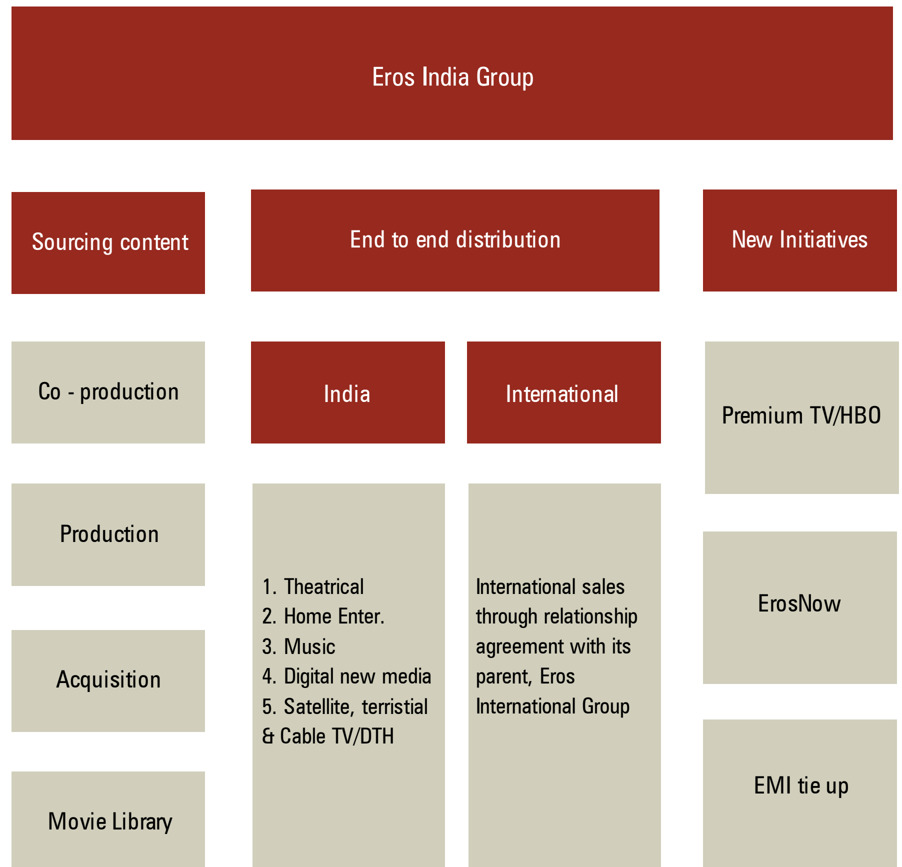
Movie	Star cast	Expected release
Kochadaiyaan (Tamil, Hindi, Telugu)	Rajnikanth, Deepika Padukone	FY13
Dishkiyaaoon	Sanjay Dutt, Harman Baweja	FY13
3G	Neil Nitin Mukesh, Sonal Chauhan	FY13
Go Goa Gone	Saif Ali Khan, Kunal Khemu	FY13
Table no. 21	Paresh Rawal, Rajeev Khandelwal	FY13
Ram Leela	Ranvir Singh, Deepika Padukone	FY14
Tanu Weds Manu Season 2	R Madhavan, Kangana Ranaut	FY14
Namak	Shahid Kapoor	FY14
Illuminati films - untitled	Saif Ali Khan	FY14
Sarkar 3	Amitabh Bachchan, Abhishek Bachchan	FY14
Rana (Tamil, Hindi, Telugu)	Rajnikanth, Deepika Padukone	FY14

Source: Company, ICICIdirect.com Research

De risked business model…

Eros has a de-risked business model wherein the dependence on theatrical revenue is far lesser than that of other distribution firms. This is due to relationship agreement with its parents, Eros International Plc. taking care of its overseas distribution, increasing TV syndication charges, a strong portfolio of movies from yesteryears that could be bundled with new releases to get a higher price, a co-production model and other newer streams of monetising the content.

Exhibit 18: Business model



Source: Company, ICICIdirect.com Research

The company generally co-produces 60% of its movie slate. Apart from co-producing, the company also acquires movies from third party and also produces a few movies on its own.

Co-production

Co-production is the most widely followed model by the company for acquiring content followed by acquisition from third-party producers. The key difference between a co-produced film and a produced film is that the production line responsibility lies with the co-producer the company works with. Typically, once the star cast, budget and expected cash outflow is decided, the co-producer takes the lead in production and execution. The company does all the financing required for making the movie and also pays a production fees to the co-producer for his services.

In return, Eros gets to keep worldwide distribution rights for a certain period and minimum 50% share in the intellectual property rights of the film. Also, the company only shares the revenue with the co-producer after they have recovered the entire cost of the movie including the distribution and marketing cost along with an additional commission for

their investment. The co-production model is generally used by the company due to its advantage of scalability.

According to the company presentation, the company typically gets a first position recoupment of 20% fixed profit on all gross revenues, followed by the recovery of print and advertising (P&A) costs along with the entire investment on the movie. The remaining profit, if any, is shared with the co-producer in a pre-agreed ratio. The management has indicated that the pre-agreed ratio normally tends to be 50:50, 60:40 or 70:30 with Eros getting the higher share.

Acquisition and production

The company also acquires movies from third-party producers wherein typically the film is evaluated at a very early stage when the concept and budget becomes available or during the course of its production at a negotiated price. In an acquisition model, generally 35-50% of the total acquisition cost is payable when the film is delivered by the producer to the company. At this time, the company would have already begun its pre-sales process for the film.

The distribution rights are usually for 15-20 years. According to the company presentation, Eros gets a first position recoupment of 20% fixed profit on all gross revenues, followed by all P&A costs and the entire minimum guarantee price (in a minimum guarantee plus royalty model). The remaining profit is shared with the producer in a pre-agreed ratio.

Eros also produces its own films, though in a very small number. The company typically invests in a creative team for the development stage. Once the project has been agreed, Eros seeks to get an execution team on board on a project by project basis rather than maintaining such a team on a permanent basis.

The co-production model is generally used by the company due to its advantage of scalability.

Exhibit 19: Comparison of movie acquisition models

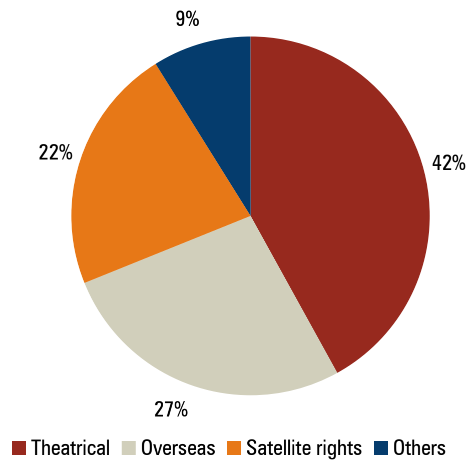
	Execution Role	Creative control	Cost	Scalability
Acquisition	Low	Low	Market Value	High
Co-production	Moderate	Moderate	Cost plus arrangement	Moderate-high
Production	High	High	At cost	Low

Source: Company, ICICIdirect.com Research

Monetisation of rights – reducing dependence on theatrical revenue

The company enjoys a less than 50% dependence on theatrical revenues primarily due to the relationship agreement with its parent assuring 39% of the entire movie cost and increasing revenue from sale of television rights of movies. In FY12, theatrical revenue contributed 42% of the overall pie. The overseas distribution revenue by virtue of its relationship agreement with its parent and sale of TV rights contributed 27% and 22% of the total revenue, respectively, while other revenue including music, home entertainment and new media chipped in at 9% of total revenue.

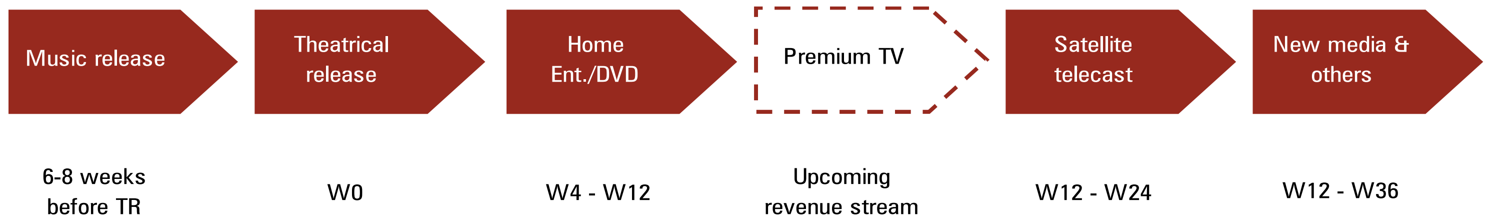
Exhibit 20: FY12 revenue split



Source: Company, ICICIdirect.com Research

As a distributor, Eros has access to different streams to monetise its content at different points of time with respect to its release date. These non-theatrical streams have been gaining significance recently owing to increasing internet users in India, digitisation of the cable & satellite industry and increasing competition among Hindi GEC broadcasters.

Exhibit 21: Distribution platforms



Source: Company, ICICIdirect.com Research

Relationship agreement with parent ensures 39% recovery of costs

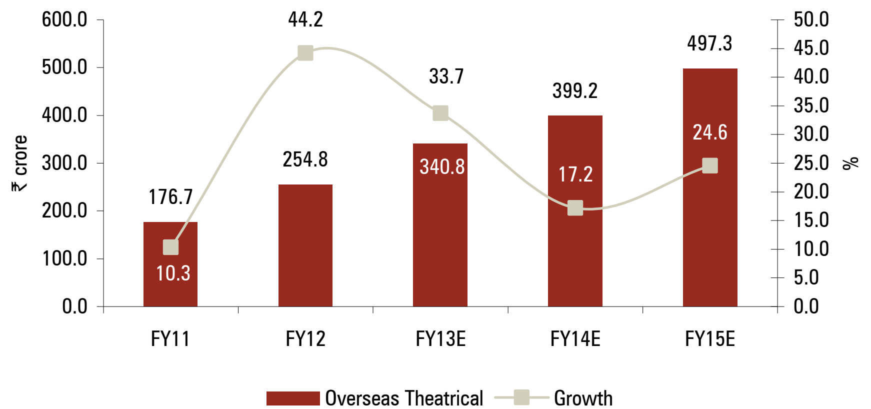
The company has entered into a relationship agreement with Eros Plc. and Eros Worldwide effective from October 2009. According to the agreement, Eros Worldwide would acquire, absolutely and unconditionally, exclusive distribution rights for Indian films except Tamil films for which the company holds the distribution rights outside the territory of India, Nepal and Bhutan.

The company would bear 30% of the entire production cost of such a film with an additional mark-up of 30% thereon payable by Eros Worldwide to the company. This translates into 39% guaranteed recovery of costs. The company has further overflow arrangements with the parent.

We expect the overseas revenue to grow at a CAGR of 25.0% in FY12-15 as the company continues to invest in higher number of movies to form 31.0% of the total revenue in FY15.

We expect the overseas revenue to grow at a CAGR of 25.0% in FY12-15 as the company continues to invest in higher number of movies

Exhibit 22: Overseas income from parent



Source: Company, ICICIdirect.com Research

Strong library to add value to newly released movies for satellite rights

The company boasts of a strong movie library of 1100 plus movies of yesteryears. Along with that, the company keeps adding 70-80 movies annually. The strong movie library helps Eros to monetise the rights of its new movies better. Eros has the highest number of movies in its catalogue and leads the second highest in the industry by far. This portfolio approach of movies has been a strategy of the company while a long relationship with industry participants has enabled it to build such a portfolio. The revenue from TV syndication rights for the company grew by 17% in FY12.

The company recently signed a deal with Colors channel in India worth ₹ 95 crore wherein some of the company's new and existing movies would be shown exclusively on Colors channel. The management indicated that deal is for seven or eight movies with new movies being *Khiladi 786*, *Shirin Farhad Ki to Nikal Padi* and *Cocktail*. Other major deals include exclusive license of 35 previously released films to Sahara One and 16 other films to Sony, Colors and 9X where telecasts were shared between the three channels in a particular order for a limited period of time.

Also, the competition among GEC broadcasters bodes well for Eros as it implies rising sales from TV rights for the company. Also, with digitisation, the revenue leakage due to under reporting in the analog cable system would be plugged and broadcasters are expected to witness a 3-4x jump in their subscription revenue. All Hindi GECs are expected to improve their quality of offerings to garner a higher share of the subscription pie. With cricket and movies being the most popular among the India viewers, movie rights are further expected to be in demand.

We expect the TV syndication revenue to grow at a CAGR of 21.0% in FY12-15 to form 22.9% of the revenue in FY15.

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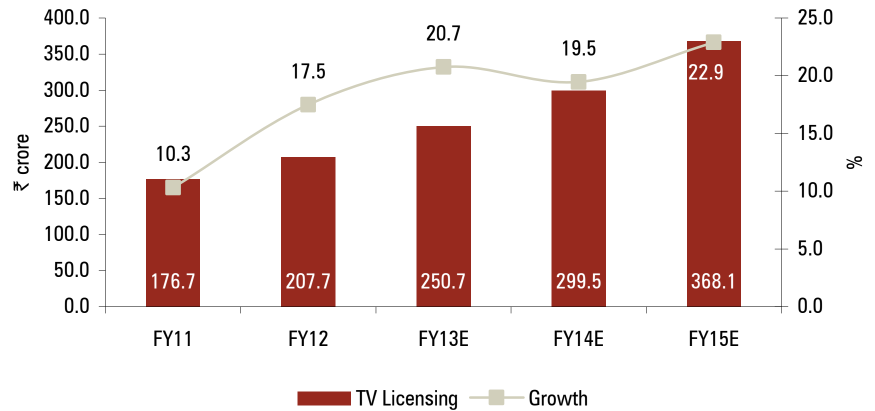
Exhibit 23: Sale of satellite rights



Source: Company, ICICIdirect.com Research

Ancillary revenue streams to grow over long term

Due to lower internet penetration and widespread analog cable system in India, movies have been unable to garner significant revenue from ancillary revenue streams. However, the ancillary revenue stream formed ~9% of the total revenue in FY12.

However, over the long term, ancillary revenue stream is expected to grow, driven by increasing internet penetration and digitisation. Eros has launched a subscription based portal Erosnow.com for online viewing of movies. All DTH operators have pay per view available on their platform. Digital cable is also expected to follow the pay per view model. We expect the ancillary revenue of the company to grow at a CAGR of 15.0%.

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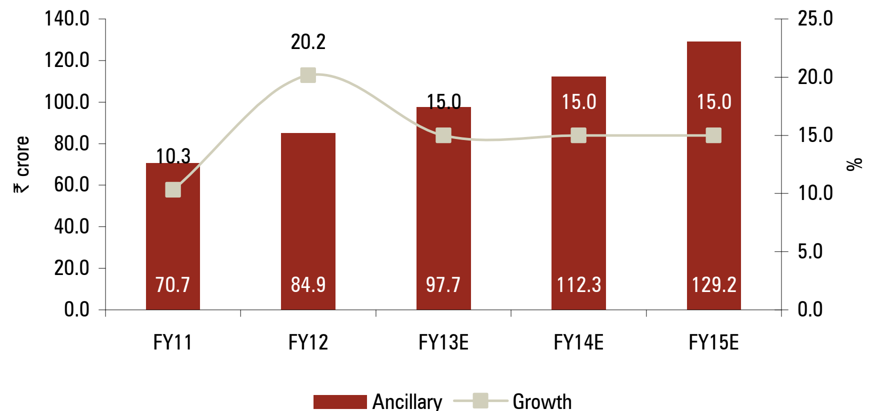
Exhibit 24: Ancillary revenue trend



Source: Company, ICICIdirect.com Research

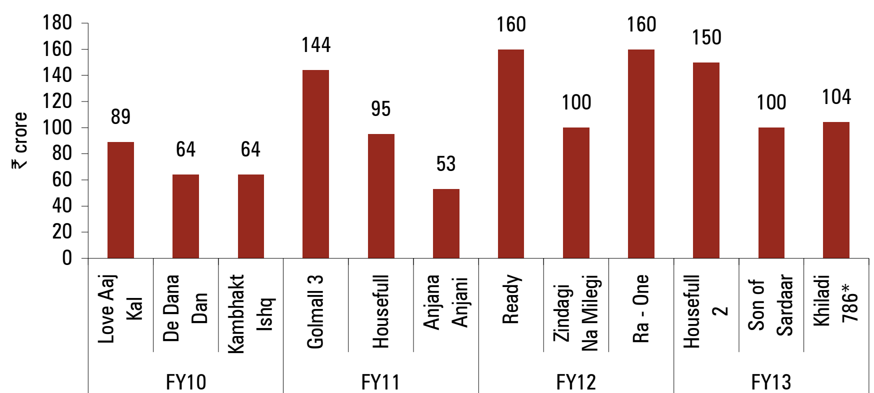
Eros has consistently been able to deliver three to four movies annually in the top 10 movies at the box office. Eros currently has a 40% share of the box office collections. The average collections of top 3 movies for Eros have almost doubled from FY10 to FY12.

Theatrical revenue on the rise…

Eros has consistently been able to deliver three to four movies annually in the top 10 movies at the box office. Eros currently has a 40% share of the box office collections. The average collections of top 3 movies for Eros have almost doubled from FY10 to FY12.

Eros has a wide distribution network with its own distribution offices, which gives the company greater control, flexibility and transparency over the distribution process and allows greater marketing control. Also, the company ensures sufficient availability of prints to release a movie across a large number of screens.

Exhibit 25: Eros - top 3 movies



** - latest*

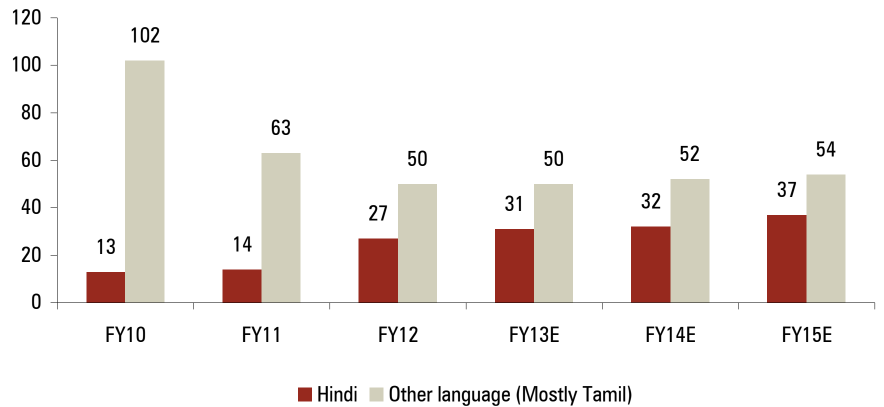
Source: Company, ICICIdirect.com Research

Going forward, we expect the growth in theatrical revenue to be driven by an increase in the volume of movies, which is possible due to the co-production model that enables scalability. Also, a better mix, with a higher contribution of big budget movies, would provide further impetus to growth. We expect the number of movies released to increase from 77 in FY12 to 91 in FY13 with growth being led by high yielding Hindi movies from 27 to 37.

Also, growth would also be seen on a per movie basis thanks to the growth in multiplexes, which have been witnessing growth in their occupancy even at higher ATP. A wider release would also lead to better exploitation of theatrical rights. *Om Shanti Om*, a blockbuster of Eros, released in ~1000 screens in 2008 while big budget movies in 2012 have been releasing across 3,500 screens. We expect theatrical revenues to grow at a CAGR of 15.5% from FY12-15.

We expect the number of movies released to increase from 77 in FY12 to 91 in FY13 with growth being led by high yielding Hindi movies from 27 to 37.

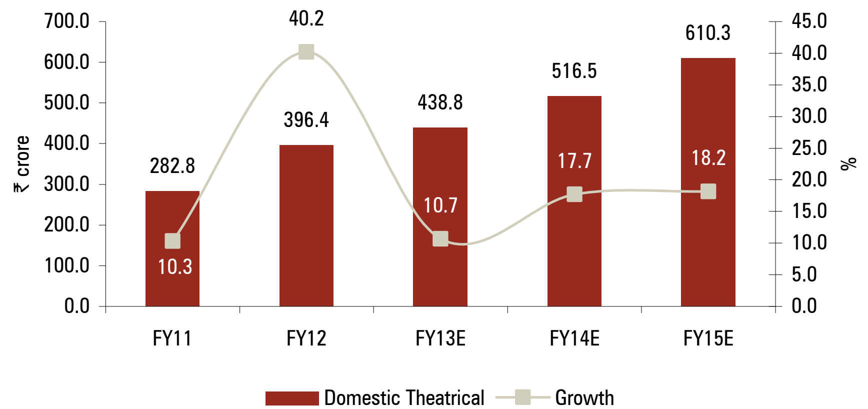
Exhibit 26: Eros - movies released



Source: Company, ICICIdirect.com Research

We expect theatrical revenues to grow at a CAGR of 15.5% from FY12-15.

Exhibit 27: Domestic theatrical



Source: Company, ICICIdirect.com Research

'A' category movie – de risked and driving growth…

'A' (big budget ~₹ 50 crore) category movies have emerged to be the least risky category of movies. Such movies get a hefty price for satellite rights and ancillary revenue streams including music while those in 'B' (~₹ 35 crore), 'C' (~₹ 15 crore) and 'D' (~₹ 5 crore) category have seen relatively lesser growth in the past few years. The pre-release sales of 'A' category movie go a long way in recovering costs of the movie making it the least dependent on theatrical revenue. Above that, theatrical revenues have also seen a substantial rise for such movies. The number of movies to hit the ₹ 100 crore box office mark has risen from one or two movies a year to five in 2011 and 11 in 2012. *Ek Tha Tiger*, released in 2012, went on to gross ~ ₹ 185 crore at the box office. Even movies like *Ra One*, *Ready* and *Housefull 2,* which were released in 2011 and 2012 have crossed the ₹ 150 crore mark.

Among the rare failures of 'A' category movies, *Agent Vinod* and *Desiboyz* managed to collect ₹ 53 crore and ₹ 70 crore, respectively, at the box office. Even after a poor performance at the box office, the movies were still able to recover their costs due to non theatrical revenues, especially sale of satellite rights.

Exhibit 28: Typical co production model dynamics for a 'A' movie

Particulars	₹ crore	Remarks
Total Cost of production	50.0	Pre agreed budget, star cast, script with co producer including co producer fees
Print & Advertisement costs	5.0	Depending on budget of the movie
Total movie cost	55.0	Production cost varies depending on star cast and genre of movies
Sale of television rights	25.0	varies from ₹ 1.5 crore - ₹ 50 crore, depending on movie budget and star cast
Music & ancillary revenue	10.0	Includes revenue from sale of music rights, new media and merchandising of movie content
Overseas revenue (@39% of cost)	19.5	As per relationship agreement of the company with its parent
Revenue prior to release	54.5	Almost the entire cost of 'A' movie is generally recovered prior to release itself
Gross box office collections	100.0	
Entertainment tax (@25%)	25.0	Varies from state to state; on an average 25%
Exhibitor net collection	75.0	
Exhibitor share (@50%)	37.5	Multiplexes share ~40%, Single screens share ~60%; On an average 50%
Producer share (@50%)	37.5	
Total producer revenue	92.0	Includes theatrical, satellite, overseas and music and ancillary revenue
20% EROS commision	18.4	first position recoupment which varies from 15-20%
Eros - P&A costs recovery	5.0	
Eros - production cost recovery	50.0	
Distributable profits	18.6	Profits after commisions and recovery of all costs to be shared with co producer
Eros share (@60%)	11.2	Ranges from 50-70% depending on agreement with co producer
Co producer share (@40%)	7.4	
Total revenue for Eros	84.6	

Source: Company, ICICIdirect.com Research

'A' movies with a budget of ~ ₹ 50 crore has almost entire cost of the movie recovered prior to the release itself making it the least risky model. 'D' movies come next in terms of risk as the losses in absolute amount in case of a flop is minimum and has huge upside potential in case of a hit

Exhibit 29: Dependence on box office collections

	Case I	Case II	Case III	Case IV
A' Movie				
Overall cost of movie		55		
Revenue from satellite, music overseas		54.5		
	Case I	Case II	Case III	Case IV
Gross box office collections	50.0	75.0	100.0	150.0
Producer share of box office collections	18.8	28.1	37.5	56.3
Eros Share of overall revenues	71.8	78.2	84.6	97.3
B' Movie				
Overall cost of movie		35		
Revenue from satellite, music overseas		26.7		
	Case I	Case II	Case III	Case IV
Gross box office collections	25.0	40.0	60.0	80.0
Producer share of box office collections	9.4	15.0	22.5	30.0
Eros Share of overall revenues	36.1	41.7	47.5	52.6
C' Movie				
Overall cost of movie		15		
Revenue from satellite, music overseas		8.7		
	Case I	Case II	Case III	Case IV
Gross box office collections	10.0	20.0	40.0	60.0
Producer share of box office collections	3.8	7.5	15.0	22.5
Eros Share of overall revenues	12.4	16.2	22.1	27.2
D' Movie				
Overall cost of movie		5		
Revenue from satellite, music overseas		2.9		
	Case I	Case II	Case III	Case IV
Gross box office collections	2.5	5.0	15.0	30.0
Producer share of box office collections	0.9	1.9	5.6	11.3
Eros Share of overall revenues	3.8	4.7	7.8	11.6

Source: Company, ICICIdirect.com Research

Foray into premium TV with HBO – game changer???

Eros has formed a strategic tie-up with HBO to launch two ad-free premium television channels in India. HBO is a leading premium cable television network owned by Time Warner. Its programming reaches 29 million subscribers in the US. It also has broadcasts in 151 countries worldwide with ~25% penetration worldwide.

While the concept of premium television is commonplace in the US, in India it would be a novel concept. Channels would follow a subscription based model and it would be an ad-free channel, which enjoys first television window after theatrical release and DVD. Other features of the channels include both Bollywood and Hollywood content in a single channel, which is available both in SD as well as HD.

HBO plans to launch two such channels – HBO Hits and HBO Defined. The Hollywood content would be provided mainly by Paramount and Warner Brothers while the Bollywood content would be taken care of by Eros.

Math adds up well for Eros in HBO deal

Eros has no equity investment in the tie-up. The only contractual obligation that Eros would have in the deal is to provide 10-12 premiers a year for a first window post theatrical release along with ~100 library titles every year. The movies delivered by Eros could be in Hindi or any regional languages. Moreover, Eros is free to license such films to other broadcasters after a four to six weeks exclusive window on the HBO premium channels.

The channels would have ~30% of the content in Hindi and other regional languages in India while the balance 70% would be English movies. The three content providers viz. Eros, Paramount and Warner Brothers would have an equal share of the revenue share received from MSO/DTH before the operational and overhead costs of the channel. All costs including technical and marketing costs would be borne by HBO. The profits after deducting the marketing and overhead costs would be shared equally between HBO and Eros. This deal provides a huge upside to the company depending on the acceptability of the channels and number of subscribers subscribing to channels.

However, the only downside that the company would have to face is a reduction in its TV syndication revenue. Broadcasters get the highest viewership in the first telecast of a movie. Eros can only sell satellite rights for such movies to other channels 4-6 weeks after the movies have been telecast on HBO. Thus, broadcasters would tend to lose viewership on the first telecast and would try to negotiate the rights from Eros at a lesser price. The company is prepared to negotiate with broadcasters on the price for the higher window of telecast.

The loss of TV syndication revenue would be minimal when the subscriber base of the HBO channels is small as broadcasters only tend to lose a small part of their viewership. However, as the subscriber base of HBO Hits and HBO Defined grows, broadcasters would negotiate strongly for the pricing of satellite rights, which at that time would me more than compensated by the profit that Eros receives from HBO. Moreover, If Eros chooses to, it can sell the satellite rights of a movie to a broadcaster directly, without giving it to HBO, as its contractual obligation is only to supply 10-12 new movies a year. We believe the maths add up well for the company.

However, it remains to be seen if Indian consumers would subscribe to such a model. We anticipate, the channels would be priced at a combined

rate, which would be north of ₹ 100/month. Also, premium channels would not be allowed to be bundled with other channels.

Assuming an ARPU of ₹ 100, 50% revenue share between the DTH/cable operator, 16% cost of content each of Eros, Warner Brothers and Paramount and a marketing and overhead expense of ₹ 20 crore to be borne by HBO, Eros would earn an EBIT of ₹ 2.6 crore with a subscriber base of 0.5 million, ₹ 15.2 crore with 1 million, ₹ 40.4 crore with 2 million and ₹ 242.0 crore with 10 million.

The downside of the deal would be a loss of revenue of ₹ 35.7 crore in FY15 @10% of sale of satellite rights, ₹ 28.5 crore @8% and ₹ 7.1 crore @2%. The loss of revenue will be minimal when the subscriber base of the channels is smaller. When the subscriber base grows, the loss of revenue will be more than compensated by the profit contribution of the channels to Eros.

The channels are expected to be launched in Q4FY13. We have currently not included the financials of these channels into our estimates.

Exhibit 30: Eros' share from HBO deal

Subscribers	million	0.5	1	2	5	10
Consumer ARPU	₹	100	100	100	100	100
Channel share	%	50%	50%	50%	50%	50%
Channel revenue	₹ crore	30.0	60.0	120.0	300.0	600.0
Content Cost						
Eros share (16%)	₹ crore	4.8	9.6	19.2	48.0	96.0
Paramount share (16%)	₹ crore	4.8	9.6	19.2	48.0	96.0
Warner Brothers share (16%)	₹ crore	4.8	9.6	19.2	48.0	96.0
Total	₹ crore	14.4	28.8	57.6	144.0	288.0
Profit before other expenses	₹ crore	15.6	31.2	62.4	156.0	312.0
Other expenses	₹ crore	20.0	20.0	20.0	20.0	20.0
Profit	₹ crore	-4.4	11.2	42.4	136.0	292.0
Eros share	₹ crore	-2.2	5.6	21.2	68.0	146.0
HBO Share	₹ crore	-2.2	5.6	21.2	68.0	146.0
Contribution to Eros EBIT	₹ crore	2.6	15.2	40.4	116.0	242.0

Source: Company, ICICIdirect.com Research

Exhibit 31: Eros' share sensitivity to ARPU

Subscribers (million)	0.25	0.5	1	2	5	10
ARPU (₹)						
80	-5.0	0.1	10.2	30.3	90.8	191.6
90	-4.3	1.3	12.7	35.4	103.4	216.8
100	-3.7	2.6	15.2	40.4	116.0	242.0
110	-3.1	3.9	17.7	45.4	128.6	267.2
120	-2.4	5.1	20.2	50.5	141.2	292.4

Source: Company, ICICIdirect.com Research

Exhibit 32: Downside to deal

		FY13E	FY14E	FY15E
Sale of satellite rights	₹ crore	250.7	299.5	368.1
Loss of revenue				
@ 2%	₹ crore	5.0	6.0	7.4
@ 4%	₹ crore	10.0	12.0	14.7
@ 6%	₹ crore	15.0	18.0	22.1
@ 8%	₹ crore	20.1	24.0	29.4
@ 10%	₹ crore	25.1	30.0	36.8

Source: Company, ICICIdirect.com Research

Financials

Handsome revenue growth

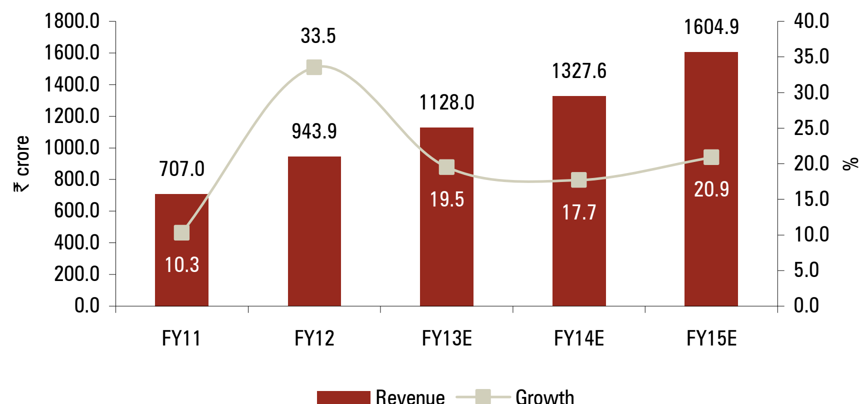
We expect the company to benefit from the changing structural trend in the film industry with the emergence of multiplexes and growth in the number of movies produced as Indian patrons get hungrier for content. While the growth in number of movies released would drive domestic theatrical and overseas revenue, a strong portfolio of movies would help in better monetisation of movie rights through TV syndication. Ancillary revenues, which are very nascent at this stage, are also expected to grow handsomely.

We expect domestic theatrical, overseas revenue, TV syndication revenue and ancillary revenues to grow at a CAGR of 15.5%, 25.0%, 21.0% and 15.0%, respectively, in FY12-15. Overall revenues are expected to grow at a CAGR of 19.4% in FY12-15 to ₹ 1604.9 crore.

Overall revenues are expected to grow at a CAGR of 19.4% in FY12-15 to ₹ 1604.9 crore.

The recent deal with HBO to launch two ad-free channels can provide further upside to the tune of ₹ 40.4 crore (at a base case of 2 million subscribers and ARPU of ₹ 100). We have currently not included the financials of these channels in our estimates.

Exhibit 33: Handsome revenue growth



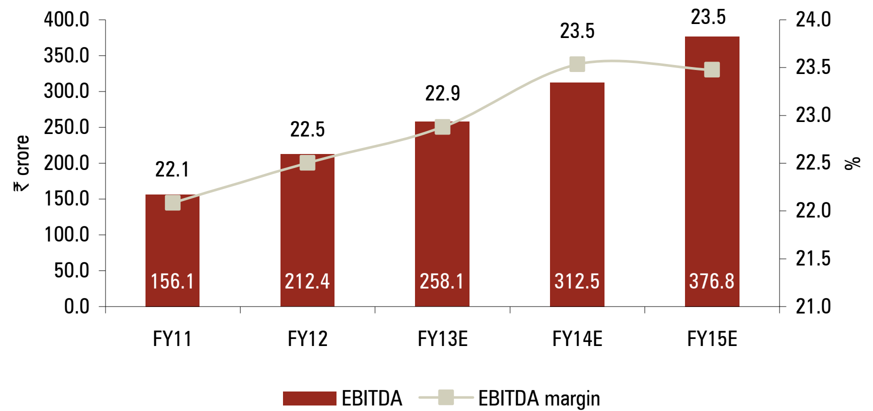
Source: Company, ICICIdirect.com Research

EBITDA margin to improve

EBITDA margins are expected to improve as movie rights are exploited over newer streams coupled with robust growth in the traditional ones including theatrical and sale of satellite rights. Along with this, a robust growth in revenue would drive the EBITDA to grow at 21.1% CAGR in FY12-15 to reach ₹ 376.8 crore.

EBITDA margins are expected to improve as movie rights are exploited over newer streams coupled with robust growth in the traditional ones including theatrical and sale of satellite rights. Along with this, a robust growth in revenue would drive the EBITDA to grow at 21.1% CAGR in FY12-15 to reach ₹ 376.8 crore.

Exhibit 34: EBITDA margins to remain stable



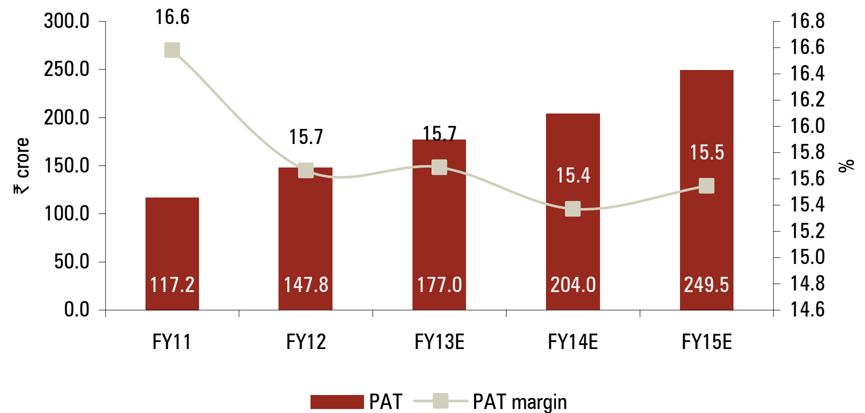
Source: Company, ICICIdirect.com Research

PAT to grow at CAGR of 19.1%

PAT is expected to grow at a CAGR of 19.1% in FY12-15 to ₹ 249.5 crore driven by strong revenue growth and improving EBITDA margins. However, higher depreciation could be a drag on PAT margins.

PAT is expected to grow at a CAGR of 19.1% in FY12-15 to ₹ 249.5 crore driven by strong revenue growth and improving EBITDA margins. However, higher depreciation could be a drag on PAT margins.

Exhibit 35: PAT to grow at 14.7%



Source: Company, ICICIdirect.com Research

Capex intensity to remain stable

The handsome growth in revenue would be driven by increasing capex in terms of number of movies acquired/co produced and increase in the costly ‘A’ category movies. As a result, we expect the capex intensity to remain stable at 0.6 in FY12-15.

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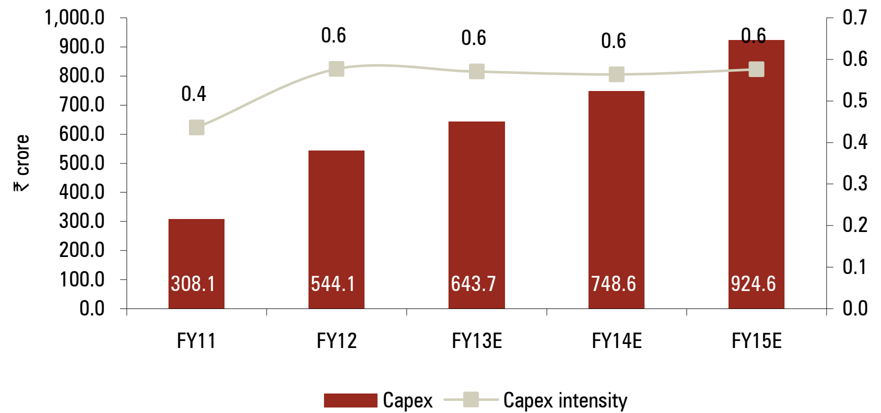
Exhibit 36: Capex intensity to remain stable



Source: Company, ICICIdirect.com Research

Return ratios to improve

Return ratios are expected to improve as the company finds newer ways to exploit its rights over difference streams. The RoCE and RoIC are expected to improve from 16.2% and 19.1% in FY12 to 18.7% and 22.7% in FY15, respectively.

Eros would start generating free cash flow from FY13 onwards. If the company chooses to repay debt or pay dividend post then, the RoE would also improve. However, in the absence of those, the RoE stands to fall marginally from 17.7% in FY12 to 17.0% in FY15.

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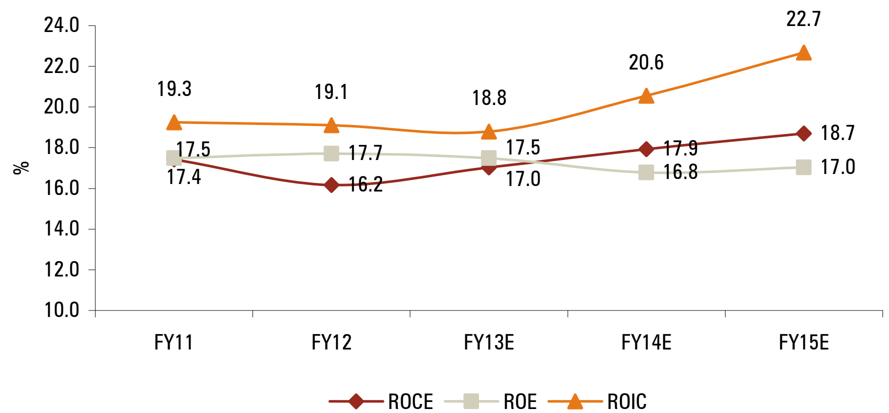
Exhibit 37: Return ratios to improve



Source: Company, ICICIdirect.com Research

Risks & concerns

Dependence on theatrical revenues

The company, though to a lesser extent than its peers, is dependent on theatrical revenues, which is dependent on the taste of patrons and can change in unpredictable ways. If Eros is unable to deliver three or four movies in the top 10 at the box office, then its return ratios could be affected. Severe competition from other production houses in terms of good movies can also affect the box office collections of the company.

Relationship with various industry participants

The company is dependent on its relationships with key production houses for the acquisition/co-production of movies. Any stress in such relationships could affect the number of movies the company plans to release in the future.

Negotiations with multiplexes and single screens

The company has agreements with multiplex chains and single screens in place for distribution of movies. If negotiations on revenue share fail, especially with large multiplexes, the revenues of the company may get affected or the release of a movie can be delayed.

PVR, which recently acquired Cinemax, has gone on to become the No. 1 multiplex chain in the industry, way ahead of the second operator. It is possible that as multiplex operators become larger, they may try to negotiate a better deal from production houses. Such a move could affect theatrical revenues and margins of the company.

Relationship agreement with its parent

The relationship agreement between the company and its parent, which assures 39% cost recovery of movies, is set to expire in October 2014. Though we expect the agreement to be renewed, the terms of the agreement change may be disadvantageous to Eros. This may dent the overseas revenue of the company.

Escalation in content price

The content cost has not escalated in FY12. However, with newer streams of revenues coming up for exploitation, content costs may also go up in terms of higher payment to key actors/directors, higher producer fees for co-production, etc. We have factored in a 10% increase in content prices each year since FY12. Should the content cost rise more, the margins of the company could be dented.

Rising TV syndication costs may be unsustainable

Revenues from sale of satellite rights have gone up by leaps and bounds in recent years. However, broadcasters are yet to go through the entire lifecycle of movie rights in this era of costly satellite rights. Should the broadcaster be unable to recover its costs in a movie, it may be hesitant to bid heavily for forthcoming movies, which would dent our revenue estimates from sale of satellite rights.

Valuation

While increasing penetration of theatre screens and higher average ticket prices will lead to handsome growth in theatrical revenue, better monetisation of content through premium TV, pay per view and satellite rights on the back of imminent digitisation will positively change the dynamics of the film entertainment industry.

With Eros having lower dependence on theatrical revenue and guaranteed 39% cost of production recovery from parent company, its business model is de-risked in comparison to other movie production houses in India. Also, the largest movie library gives it the ability to monetise the long tail effectively through bundled deals with satellite channels. Moreover, Eros' consistent track record in delivering three to four movies in the top 10 grosser at box office each year lends stability and visibility to future earnings.

The company is expected to post revenue CAGR of 19.4% over FY12-15E while the EPS would post a CAGR of 19.1% over the same period. The balance sheet for the company remains robust with strong internal accruals to meet future capex requirements.

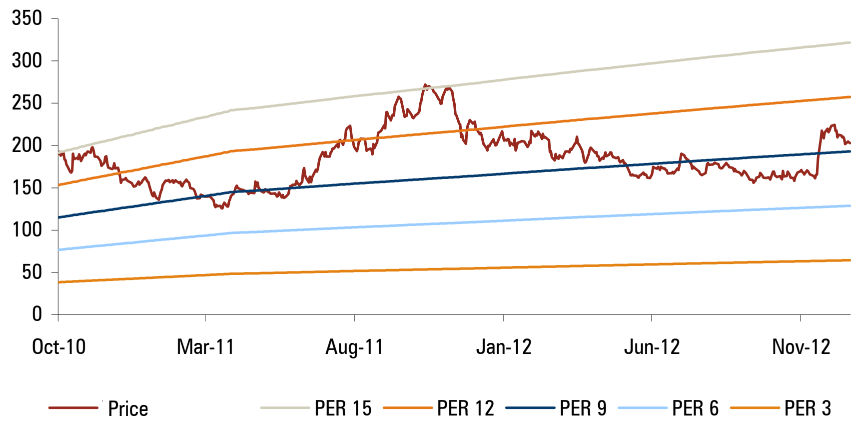
The company is currently trading at a significant discount to other media companies in spite of having robust return ratios. We believe with the structural change in the theatrical business, advent of premium TV and pay per view, imminent digitisation and monetisation through new media will continue to fuel the earnings growth, which would lead to a re-rating of the stock. The stock, since its listing in October 2010, has been trading at an average one year forward rolling PE of 10.7x. We have valued the stock at 12x FY14E EPS to arrive at a target price of ₹ 267.

Exhibit 38: Media companies - Multiples & ratios

	PE (x)			EV/EBITDA(x)			RoCE (%)			RoE (%)		
	FY12	FY13	FY14	FY12	FY13	FY14	FY12	FY13	FY14	FY12	FY13	FY14
Broadcasters												
Zee Entertainment	37.2	32.4	26.6	29.2	24.5	19.6	20.5	21.1	22.4	17.1	17.1	17.9
Sun TV	24.5	25.6	20.5	11.8	11.2	9.3	35.7	32.0	34.4	26.6	23.2	25.2
Multiplexes												
PVR	29.0	16.7	13.1	12.2	6.6	5.1	9.0	11.3	12.6	9.1	12.8	14.1
Cinemax		13.3	15.3		7.1	7.2		24.1	19.8		24.6	17.6
Cable distribution												
Hathway	NA	NA	NM	24.8	21.1	14.5	1.8	2.4	6.2	NM	NM	0.8
Dish TV	NA	NA	NM	18.1	14.2	10.7	NM	NM	0.4	NM	NM	-1.3
Print Media												
Jagran Prakashan	18.4	12.8	13.1	11.1	10.1	8.5	23.1	21.9	24.0	23.7	29.8	26.0
DB Corp	19.1	19.3	15.0	10.9	10.5	8.1	26.6	24.2	27.6	21.7	18.5	19.7
HT Media	14.6	13.8	11.0	9.1	8.6	6.3	10.1	9.4	11.3	11.4	10.9	12.1
Film Entertainment												
Eros	12.7	10.6	9.2	9.5	8.1	6.4	16.2	17.0	17.9	17.7	17.5	16.8

Source: Company, ICICIdirect.com Research

Exhibit 39: One year forward rolling P/E



Source: Company, ICICIdirect.com Research

Financial summary

Profit and loss statement

(₹ Crore)

(Year-end March)	FY12	FY13E	FY14E	FY15E
Total operating Income	943.9	1,128.0	1,327.6	1,604.9
Growth (%)	33.5	19.5	17.7	20.9
Operating Expenses	662.5	787.6	911.6	1,112.5
Employee Expenses	22.6	25.9	30.5	35.3
Administrative Expenses	46.4	56.4	73.0	80.2
Total Operating Expenditure	731.5	869.9	1,015.1	1,228.1
EBITDA	212.4	258.1	312.5	376.8
Growth (%)	36.0	21.5	21.1	20.6
Depreciation	6.0	11.0	15.9	20.8
Interest	13.4	13.6	13.5	13.5
Other Income	19.3	20.0	20.0	20.0
PBT	212.3	253.5	303.0	362.5
Total Tax	63.1	80.0	99.0	113.0
Minority Interest	1.3	(3.4)	-	-
PAT	147.8	177.0	204.0	249.5
Growth (%)	26.1	19.7	15.3	22.3
EPS (₹)	16.1	19.3	22.2	27.2

Source: Company, ICICIdirect.com Research

Cash flow statement

(₹ Crore)

(Year-end March)	FY12	FY13E	FY14E	FY15E
Profit after Tax	147.8	177.0	204.0	249.5
Add: Depreciation	249.5	358.7	428.0	498.7
(Inc)/dec in Current Assets	321.5	-69.7	-75.5	-104.9
Inc/(dec) in CL and Provisions	-137.5	55.6	60.3	83.7
Others	13.4	13.6	13.5	13.5
CF from operating activities	594.7	535.1	630.3	740.5
(Inc)/dec in Fixed Asset	-583.1	-231.5	-127.8	-126.9
Others	-102.4	-351.8	-412.8	-478.6
CF from investing activities	-685.6	-583.4	-540.7	-605.5
Issue/(Buy back) of Equity	0.3	0.0	0.0	0.0
Inc/(dec) in loan funds	237.6	0.0	0.0	0.0
Others	2.5	-13.6	-13.5	-13.5
CF from financing activities	240.5	-13.6	-13.5	-13.5
Net Cash flow	149.6	-61.8	76.1	121.4
Opening Cash	150.8	300.4	238.5	314.7
Closing Cash	300.4	238.5	314.7	436.1

Source: Company, ICICIdirect.com Research

Balance sheet

(₹ Crore)

(Year-end March)	FY12	FY13E	FY14E	FY15E
Liabilities				
Equity Capital	91.7	91.7	91.7	91.7
ESOP's	1.9	1.9	1.9	1.9
Reserve and Surplus	741.0	917.9	1,122.0	1,371.5
Total Shareholders funds	834.6	1,011.6	1,215.6	1,465.1
Total Debt	436.2	436.2	436.2	436.2
Other Non Current Liabilities	118.4	114.9	114.9	114.9
Total Liabilities	1,389.2	1,562.7	1,766.8	2,016.3
Assets				
Gross Block	1,903.9	2,547.6	3,296.2	4,220.8
Less: Acc Depreciation	1,375.1	1,798.2	2,434.9	3,253.3
Net Block	528.8	749.3	861.3	967.4
Capital WIP	428.0	428.0	428.0	428.0
Total Fixed Assets	956.8	1,177.3	1,289.3	1,395.4
Investments	51.5	51.5	51.5	51.5
Inventory	7.0	8.4	9.9	12.0
Debtors	245.0	292.8	344.6	416.5
Loans and Advances	40.0	47.9	56.3	68.1
Other Current Assets	65.1	77.8	91.6	110.7
Cash	300.4	238.5	314.7	436.1
Total Current Assets	657.5	665.3	817.0	1,043.3
Creditors	280.7	335.4	394.8	477.2
Provisions	4.3	5.1	6.0	7.3
Total Current Liabilities	285.0	340.5	400.8	484.5
Net Current Assets	372.5	324.8	416.2	558.8
Other Non Current Assets	6.9	6.9	6.9	6.9
Deffered tax assets	1.5	2.2	2.9	3.6
Application of Funds	1,389.2	1,562.7	1,766.8	2,016.3

Source: Company, ICICIdirect.com Research

Key ratios

(Year-end March)	FY12	FY13E	FY14E	FY15E
Per share data (₹)				
EPS	16.1	19.3	22.2	27.2
Cash EPS	16.8	20.5	24.0	29.4
BV	90.9	110.2	132.5	159.6
DPS	0.0	0.0	0.0	0.0
Cash Per Share	32.7	26.0	34.3	47.5
Operating Ratios (%)				
EBITDA Margin	22.5	22.9	23.5	23.5
PBT / Total Operating income	22.5	22.5	22.8	22.6
PAT Margin	15.7	15.7	15.4	15.5
Inventory days	2.7	2.7	2.7	2.7
Debtor days	94.7	94.7	94.7	94.7
Creditor days	108.5	108.5	108.5	108.5
Return Ratios (%)				
RoE	17.7	17.5	16.8	17.0
RoCE	16.2	17.0	17.9	18.7
RoIC	19.1	18.8	20.6	22.7
Valuation Ratios (x)				
P/E	12.8	10.7	9.3	7.6
EV / EBITDA	9.6	8.1	6.5	5.0
EV / Net Sales	2.2	1.9	1.5	1.2
Market Cap / Sales	2.0	1.7	1.4	1.2
Price to Book Value	2.3	1.9	1.6	1.3
Solvency Ratios				
Debt/EBITDA	2.1	1.7	1.4	1.2
Debt / Equity	0.5	0.4	0.4	0.3
Current Ratio	2.3	2.0	2.0	2.2
Quick Ratio	2.3	1.9	2.0	2.1

Source: Company, ICICIdirect.com Research

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