

27 July 2020

## Zee Entertainment

*Risk-reward favourable; maintaining a Buy*

Rating: **Buy**

Target Price: ₹220

Share Price: ₹152

The Zee stock has been an underperformer recently, falling ~40% in the last four months due to cash-flows and balance-sheet concerns. We believe management's focus on cash-flow and cleaning the balance sheet is positive. At the ruling market price, the risk-reward is favourable. We maintain our Buy rating with new target price of ₹220.

Revenues were largely inline, operating profit impacted due to one-offs. The sharp drop in ad revenue pulled down Zee's revenue 3.4% y/y to ₹19.51bn in Q4FY20. Domestic ad revenue slid 15.1% y/y. On the new tariff implemented last year and ramp-up of Zee5's subscriber base, domestic subscription revenue grew 40.7%. At the EBITDA level the company reported a ₹2.84bn loss (vs. ₹5.68bn profit a year ago), due to a one-time item of ₹6bn (includes one-time accelerated amortization of ₹2.6bn and provision of ₹3.4bn on account of Covid-19 led uncertainty). Adjusting for this, EBITDA was ₹3.19bn (down ~44% y/y) with a 16.4% margin (against 28.1% a year back). Factoring in the ~32% ad revenue drop in FY21, we cut our FY21e/FY22e EBITDA 39%/25.7%.

**Ad revenue growth constrained.** Hurt by the weak macro-economic conditions, effect of conversion of two channels from FTA to "pay" and market-share loss in certain regions, the underlying ad-growth slid 15.1% y/y. The Hindi GEC market share eased recently. Leading positions were retained in the Bangla, Marathi and Kannada markets. Competition has intensified in Tamil (Sun TV, Star) and Telugu (Star) even as Zee Keralam gains market share. The company talked of a 28-30% decline in ad revenue in FY21.

**Guiding to FCF of 50% of PAT from FY22 onwards.** The company reported ₹681m free cash-flow in FY20 against a ₹1.47bn negative cash flow in FY19.

**Retaining a Buy.** We value Zee at 10x FY22e EV/EBITDA and retain our Buy rating, with a TP of ₹220. **Risk:** Any slippage in content ratings.

Key financials (YE Mar)	FY18	FY19	FY20	FY21e	FY22e
Sales (₹ m)	66,857	79,339	81,299	65,135	75,479
Net profit (₹ m)	14,778	15,672	5,247	9,130	12,407
EPS (₹)	14.0	16.3	5.5	9.5	12.9
PE (x)	9.9	9.3	27.8	16.0	11.8
EV / EBITDA (x)	6.3	5.1	8.0	8.7	6.5
PBV (x)	1.9	1.6	1.6	1.5	1.4
RoE (%)	20.7	19.0	5.7	9.5	12.0
RoCE (%)	13.5	15.5	7.4	8.6	11.2
Dividend yield (%)	1.9	2.3	0.2	1.2	1.6
Net debt / equity (x)	-0.2	-0.1	-0.0	-0.1	-0.1

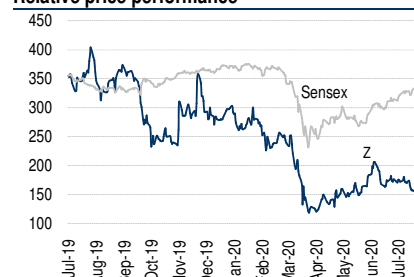
Source: Company, Anand Rathi Research

Key data	Z IN / ZEE.BO
52-week high / low	₹406 / 114
Sensex / Nifty	38129 / 11194
3-m average volume	\$59.5m
Market cap	₹146bn / \$1947.2m
Shares outstanding	961m

Shareholding pattern (%)	Mar'20	Dec'19	Sep'19
Promoters	4.8	4.9	22.4
- of which, Pledged	20.9	18.5	96.0
Free float	95.2	95.1	77.6
- Foreign institutions	67.3	67.4	57.4
- Domestic institutions	3.8	5.0	6.9
- Public	24.1	22.7	13.3

Estimates revision (%)	FY21e	FY22e
Revenues	(27.1)	(22.9)
EBITDA	(39.0)	(25.7)
Net profit	(46.4)	(32.8)

### Relative price performance



Source: Bloomberg

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## Quick Glance – Financials and Valuations

**Fig 1 – Income statement (₹ m)**

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
Net revenues	66,856.8	79,339.3	81,299.2	65,134.6	75,479.0
Growth (%)	4	19	2	-20	16
Ad revenue contri %	62.9	63.5	57.6	49.0	51.9
Direct costs	31,932.0	38,007.4	46,090.1	35,172.7	40,003.9
Gross profit	34,924.8	41,331.9	35,209.1	29,961.9	35,475.1
Gross margins %	52.2	52.1	43.3	46.0	47.0
SG&A	14,164	15,693	18,863	14,981	15,473
<b>EBITDA</b>	<b>20,761</b>	<b>25,639</b>	<b>16,347</b>	<b>14,981</b>	<b>20,002</b>
EBITDA margins (%)	31.1	32.3	20.1	23.0	26.5
- Depreciation	1,821	2,347	2,706	3,110	3,600
Other income	4,335	2,551	240	1,350	1,200
Interest expenses	1,448	1,304	1,449	1,015	1,015
PBT	23,175	24,320	9,588	12,206	16,587
Effective tax rates (%)	36.3	35.7	45.0	25.2	25.2
+ Associates / (Minorities)	12	24	-24	-	-
Net income	14,778	15,672	5,247	9,130	12,407
WANS	960	960	960	960	960
FDEPS (₹ / sh)	14.0	16.3	5.5	9.5	12.9

**Fig 3 – Cash-flow statement (₹ m)**

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
PBT	23,175	24,320	9,588	12,206	16,587
+ Non-cash items	-785	3,481	12,783	1,760	2,400
Oper. prof. before WC	22,390	27,802	22,371	13,966	18,987
- Incr. / (decr.) in WC	-8,551	-17,151	-16,758	-3,021	-1,096
Others incl. taxes	-8,295	-9,299	-3,114	-3,076	-4,180
Operating cash-flow	5,544	1,352	2,499	7,870	13,711
- Capex (tang. + intang.)	3,191	2,823	1,818	3,257	3,774
Free cash-flow	2,353	-1,471	681	4,613	9,937
Acquisitions	-2,015	-	-	-	-
- Div.(incl. buyback & taxes)	3,834	4,734	5,227	3,406	4,154
+ Equity raised	-	-	-	-	-
+ Debt raised	-6,967	-4,876	-5,326	-1,000	-1,000
- Fin investments	2,051	-19,793	-13,734	220	220
- Misc. (CFI + CFF)	-2,498	12,610	8,735	21,728	-2,209
Net cash-flow	-10,016	-3,898	-4,873	2,237	6,772

Source: Company, Anand Rathi Research

**Fig 5 – Price movement**



Source: Bloomberg

**Fig 2 – Balance sheet (₹ m)**

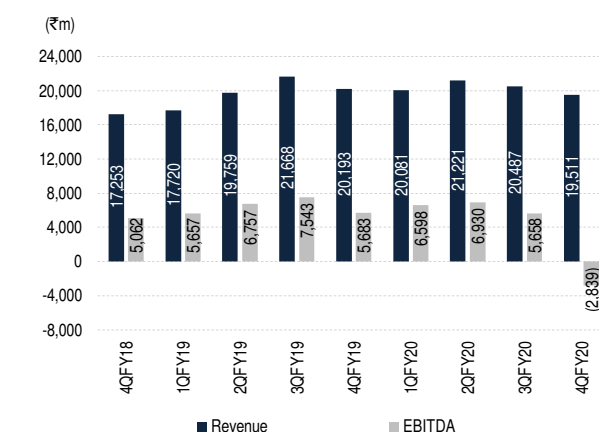
Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
Share capital	961	961	961	961	961
Net worth	75,617	89,239	93,439	99,163	1,07,416
Debt	15,245	11,114	5,950	4,950	3,950
Minority interest	142	143	110	110	110
DTL / (Assets)	-	-	-2,742	-2,742	-2,742
<b>Capital employed</b>	<b>91,004</b>	<b>1,00,496</b>	<b>96,757</b>	<b>1,01,481</b>	<b>1,08,734</b>
Net tangible assets	6,005	5,959	5,898	5,349	4,716
Net intangible assets	1,734	1,383	1,372	1,387	1,404
Goodwill	5,467	5,252	4,070	4,070	4,070
CWIP (tang. & intang.)	920	1,561	832	832	832
Investments (strategic)	3,148	2,740	1,274	1,274	1,274
Investments (financial)	13,695	8,576	2,770	2,770	2,770
Current assets (ex cash)	64,210	91,641	97,435	94,701	97,709
Cash	16,117	12,218	7,345	9,582	16,355
Current liabilities	20,293	28,835	24,238	18,484	20,396
Working capital	43,918	62,806	73,197	76,217	77,313
<b>Capital deployed</b>	<b>91,004</b>	<b>1,00,497</b>	<b>96,758</b>	<b>1,01,481</b>	<b>1,08,735</b>
Contingent liabilities	-	-	-	-	-

**Fig 4 – Ratio analysis**

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
P/E (x)	9.9	9.3	27.8	16.0	11.8
EV / EBITDA (x)	6.3	5.1	8.0	8.7	6.8
EV / Sales (x)	2.0	1.7	1.7	2.1	1.7
P/B (x)	1.9	1.6	1.6	1.5	1.4
RoE (%)	20.7	19.0	5.7	9.5	12.0
RoCE (%) - after tax	13.5	15.5	7.4	8.6	11.2
RoIC (%) - after tax	21.8	20.9	8.7	9.6	13.1
DPS (₹ / sh)	2.9	3.5	0.3	1.8	2.5
Dividend yield (%)	1.9	2.3	0.2	1.2	1.6
Dividend payout (%) - incl. DDT	20.7	20.7	19.0	19.0	19.0
Net debt / equity (x)	-0.2	-0.1	-0.0	-0.1	-0.1
Receivables (days)	84	84	94	130	100
Inventory (days)	131	175	267	290	267
Payables (days)	91	101	94	75	75
CFO : PAT%	37.5	8.6	47.4	86.2	110.5

Source: Company, Anand Rathi Research

**Fig 6 – Quarterly financial performance**



Source: Company

## Result Highlights

### Q4 FY20 Results at a Glance

Fig 7 – Segment-wise results

(₹ m)	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	QoQ %	YoY%
Revenues	20,193	20,081	21,221	20,487	19,511	-4.8%	-3.4%
Growth Y/Y %	17.0%	13.3%	7.4%	-5.5%	-3.4%	207 bps	-2042 bps
Advertisements	12,175	11,867	12,247	12,308	10,389	-15.6%	-14.7%
Domestic	11,575	11,322	11,690	11,570	9,829	-15.0%	-15.1%
International	600	545	557	738	560	-24.1%	-6.7%
Subscriptions	5,653	7,088	7,235	7,137	7,414	3.9%	31.2%
Domestic	4,696	6,240	6,459	6,317	6,607	4.6%	40.7%
International	957	848	776	820	807	-1.6%	-15.7%
Others	2,365	1,126	1,739	1,042	1,708	63.9%	-27.8%
Programming & Operating cost	(8,833)	(7,800)	(8,963)	(8,476)	(13,046)	53.9%	47.7%
As % of revenues	-44%	-39%	-42%	-41%	-67%	-2549 bps	-2312 bps
Staff cost	(2,015)	(2,003)	(2,123)	(2,075)	(1,604)	-22.7%	-20.4%
As % of revenues	-17%	-17%	-17%	-17%	-15%	142 bps	111 bps
Selling & Other costs	(3,662)	(3,680)	(3,206)	(4,277)	(7,699)	80.0%	110.3%
As % of revenues	-18%	-18%	-15%	-21%	-39%	-1858 bps	-2133 bps
EBITDA	5,683	6,598	6,930	5,658	(2,839)	NA	NA
EBITDA margins %	28%	33%	33%	28%	-15%	NA	NA
Depreciation	(568)	(690)	(583)	(656)	(778)	18.6%	36.9%
EBIT	5,115	5,908	6,346	5,002	(3,616)	NA	NA
EBIT margins %	25%	29%	30%	24%	-19%	NA	NA
Other income	661	1,718	594	309	(2,380)	NA	NA
Interest expense	(1,142)	(205)	(180)	(200)	(864)	331.0%	-24.3%
PBT	4,417	7,420	5,054	5,111	(7,997)	NA	NA
PBT margins %	23%	37%	32%	25%	-35%	NA	NA
Taxes	(1,494)	(2,146)	(921)	(1,622)	372	NA	NA
ETR	-32%	-29%	-14%	-32%	-5%	NA	NA
PAT	2,925	5,297	4,121	3,486	(7,658)	NA	NA
PAT margins %	15.6%	26.3%	27.5%	17.0%	-33.3%	NA	NA

Source: Company, Anand Rath Research

Fig 8 – Quarterly result

Year-end: Mar (₹m)	Q4 FY20	% Q/Q	% Y/Y	FY20	FY19	% Y/Y
Sales	19,511	(4.8)	(3.4)	81,299	79,339	2.5
EBITDA	(2,839)	NA	NA	16,347	25,640	(36.2)
EBITDA margins (%)	(15)	NA	NA	20	32	-1221 bps
EBIT	(3,616)	NA	NA	13,640	23,293	(41.4)
EBIT margins (%)	(19)	NA	NA	17	29	-1258 bps
PBT	(7,997)	NA	NA	9,588	24,321	(60.6)
Tax	372	NA	NA	(4,317)	(8,673)	(50.2)
Tax rate (%)	(5)	NA	NA	(45)	(36)	-937 bps
Net income	(7,658)	NA	NA	5,247	15,673	(66.5)

Source: Company, Anand Rath Research

## Conference call highlights

### Company-specific

- Performance in Hindi, Tamil and Telugu has been below expectations. The company needs to rebuild content here to remain competitive.
- All markets, except Tamil, have started shooting.
- Advertising revenue in Q1 FY21 will be nearly two-thirds of last year; recovery expected from H2 FY21. Ad revenue to decline ~28-30% in FY21.
- Subscriptions revenue to be stable; even DPO has some problems in collecting revenues. Expecting to see modest to reasonable growth in subscription revenues in FY21.
- Cash and Treasury investments are ₹10.2bn (incl. ~₹2.2bn overseas Treasury investments).
- Don't expect any further impact of subscription revenues from related parties.
- In Zee5 the company remains committed to original-content strategy and film strategy. The number of Zee5 subscribers continues to increase' 60% growth seen. Invested 7% of EBITDA in Zee5 since launch. The company will be sharing Zee5 financial data from Q1 FY21. Ahead, the biggest investment will be on Zee5.
- Future inventory growth will be in line with passing through P&L, not accelerated growth.
- Expect to generate FCF in FY22 (~50% of PAT).
- Alt Balaji tie-up was for three year, extendable. The contract now is in the second year.
- Non-content cost is 40-45% of expenditure; flexibility is on marketing and advertising which can be 15-20%, the rest is fixed.
- FY21 margins will not be anywhere close to the earlier 30%. If everything comes to normal expecting ~30%+ margins in FY22.

## Factsheet

**Fig 9 – Factsheet**

Year-end: Mar	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20
<b>Revenue split (%)</b>					
Advertisements	60	59	58	60	53
Subscriptions	28	35	34	35	38
Others	12	6	8	5	9
<b>Revenue split (₹m)</b>					
Advertisements	12,175	11,867	12,247	12,308	10,389
Subscriptions	5,653	7,088	7,235	7,137	7,414
Others	2,365	1,126	1,739	1,042	1,708
<b>Y/Y growth (%)</b>					
Advertisements	16	4	1	-16	-15
Subscriptions	3	37	19	15	31
Others	83	5	11	22	-28
<b>Advertisement revenue split (%)</b>					
Domestic revenues	95	95	95	94	95
International revenues	5	5	5	6	5
<b>Subscription revenue split (%)</b>					
Domestic revenues	83	88	89	89	89
International revenues	17	12	11	11	11

Source: Company

## Valuations

Zee is uniquely positioned in the media sector due to its leading position in Hindi GEC and the various sub-segments – specifically, regional content. It is also afforded a scarcity premium as the other two competitors are unavailable for investors in the secondary market.

We now value Zee at 10x FY22e EV/EBITDA (earlier at 12x FY22e EBITDA) and arrive at a target price of ₹220 (earlier ₹350).

**Fig 10 – Change in estimates**

(₹ m)	FY21e			FY22e		
	New	Old	Chg %	New	Old	Chg %
Revenues	65,135	89,306	(27.1)	75,479	97,939	(22.9)
EBITDA	14,981	24,559	(39.0)	20,002	26,933	(25.7)
EBITDA margins %	23.0%	27.5%	-450 bps	26.5%	27.5%	-100 bps
EBIT	11,871	21,937	(45.9)	16,402	25,711	(36.2)
EBIT margins %	18.2%	24.6%	-634 bps	21.7%	26.3%	-452 bps
PBT	12,206	22,772	(46.4)	16,587	24,697	(32.8)
Net profit	9,130	17,034	(46.4)	12,407	18,473	(32.8)

Source: Anand Rathi Research

### Risk

- Any loss in content rating in the flagship/leadership genres.

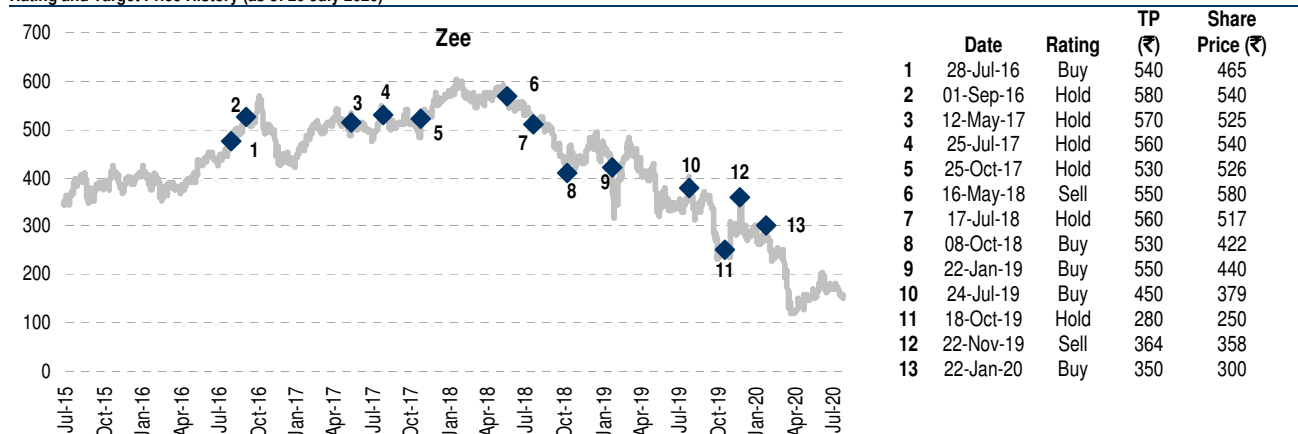
## Appendix

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