Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Zee Entertainment Enterprises Ltd

Weak Q1; recovery eyed in H2

Consumer Discretionary	Sharekhan code: ZEEL
Reco/View: Buy ↔	CMP: **Rs. 238**	Price Target: **Rs. 310** ↓

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)		✓	
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 16.02

Updated Jul 08, 2022

Low Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

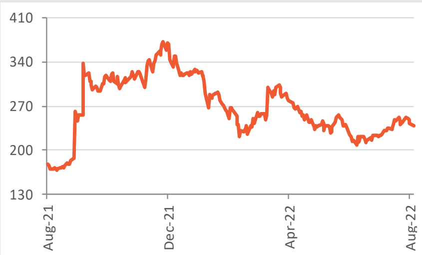
Company details

Market cap:	Rs. 22,846 cr
52-week high/low:	Rs. 379 / 167
NSE volume: (No of shares)	112.9 lakh
BSE code:	505537
NSE code:	ZEEL
Free float: (No of shares)	92.22 cr

Shareholding (%)

Promoters	4.0
FII	39.2
DII	30.5
Others	26.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.9	-3.4	-9.5	33.1
Relative to Sensex	-5.4	-13.5	-12.9	25.9

Sharekhan Research, Bloomberg

Summary

- Q1 was muted with a 6%/20% miss in revenue/operating profit due to weak advertisement revenue growth and decline in subscription revenue. OPM, at 12.8% (down 661 bps y-o-y), missed our estimate by 223 bps due to higher programming & technology and marketing costs.
- Advertisement revenues were hit by FTA withdrawals (Zee Anmol) and lower ad spends by brands; subscription revenues declined given timing effect of some of B2B deals/renewals and a pricing embargo on linear revenue growth. ZEE5 revenue of Rs. 160 crore (up 43% q-o-q) but EBITDA loss widens to Rs. 235 crore.
- We cut our FY23-24 earnings estimate to factor in soft Q1FY23 revenue growth and lower margin assumption (given investment in content & marketing).
- We maintain a Buy on ZEEL with a revised PT of Rs. 310 (reflects cut in earnings estimate) given synergy benefits from the proposed merger, healthy traction in ZEE5, and reasonable valuation of 16.1x FY24E EPS.

ZEE Entertainment Limited (ZEEL) reported weak Q1FY23 results with a 6%/20% miss in consolidated revenue/EBITDA at Rs. 1,846 crore/Rs. 236 crore, up 4% y-o-y and down 32% y-o-y respectively due to weak advertising and subscription revenues and 223 bps miss in OPM at 12.8% (down 661 bps y-o-y; down 817 bps q-o-q). Revenues missed the mark due to muted advertisement revenue growth of 5.4% y-o-y to Rs. 9,763 crore as it got affected by FTA withdrawals (Zee Anmol) and lower ad-spends by brands (especially in FMCG sector due to inflationary environment) due to weak macroeconomic conditions while subscription revenue declined by 5.1% y-o-y to Rs. 7,717 crore as pricing embargo impacted revenue growth and impact of timing of some of B2B deals and renewals. OPM was severely hit by weak revenue growth and higher programming & technology and marketing cost due to higher theatrical releases, investment in ZEE5 and new launches in linear business. Adjusted PAT of Rs. 121 crore (down 46.5% y-o-y; down 53.6% q-o-q) sharply missed our estimate of Rs. 179 crore due to weaker revenue growth and higher-than-expected contraction in margins. We have adjusted reported PAT of Rs. 107 crore (down 50.1% y-o-y) for an exceptional expense of Rs. 15 crore as the company has accounted for the same towards debt service reserve account (DSRA guarantee) in relation to certain financial facilities availed from banks by Siti Networks.

Key positives

- ZEE5's revenues grew by 43% y-o-y to Rs. 160 crore and strong DAUs of 11.3 million (up 4.2 million y-o-y; up 0.8 million q-o-q).
- About 38 shows & movies (incl. 8 originals) released in the quarter.

Key negatives

- Network viewership share dipped by 100 bps q-o-q to 16.1% due to discontinuation of FTA channels.
- Inventory increased by Rs. 372 crore q-o-q primarily due to movie business.

Management Commentary

- Advertising revenues are seeing softness given inflationary environment in FMCG sector. Management expects improvement in ad revenue from Q3FY23 given boost from festival season.
- Annual subscription pack charges for ZEE5 have increased by 40% and would support subscription revenue in the coming quarters.
- ZEE5's global daily active users (DAUs) grew by 8% q-o-q to 11.3 million while Monthly Active Users (MAUs) stood at 103.3 million in Q1FY23 versus 104.8 million in Q4FY22.
- Excluding the impact of Zee Anmol, ZEEL has seen sequential improvement in the viewership share in Q1FY23.
- Received approval of stock exchanges for the scheme of arrangement for merger with Sony. Both ZEEL and Sony are working independently to get necessary regulatory approvals.

Revision in estimates – We have cut our FY23-FY24 earnings estimates to factor in soft Q1FY23 revenue and lower margin assumption.

Our Call

Valuation – Maintain Buy with revised PT of Rs. 310: ZEEL has been progressing well on digital business with launching new shows each quarter. We believe the proposed merger would be a strategic fit from a revenue perspective and would help the combined entity to emerge as a strong player in the entertainment industry for capturing the significant opportunity in the linear business. Further, the merged entity would allocate its growth capital towards premium content, including sports event rights, which would strengthen its position in the OTT space. We expect the company to deliver a 14% CAGR in adjusted net profit over FY2022-FY2024E. The stock currently trades at a reasonable valuation at 22x/16x of FY2023E/FY2024E earnings. Given its strong regional presence and strong traction on its digital platform, we maintain Buy rating on ZEEL with a revised PT of Rs. 310 (reflecting a cut in earnings estimates).

Key Risks

- Slowdown in the economy that would lower demand and subdued realisation for advertisement revenue stream.
- Delay in monetisation benefit from digitisation and a higher content costs could affect earnings.

Valuation (Consolidated) Rs cr

Particulars	FY2021	FY2022	FY2023E	FY2024E
Revenue	7,729.9	8,189.3	8,403.7	9,587.9
OPM (%)	23.2	21.0	19.6	22.1
Adjusted PAT	1,122.9	1,101.6	1,049.6	1,419.1
% y-o-y growth	*123.8*	*-1.9*	*-4.7*	*35.2*
Adjusted EPS (Rs.)	11.7	11.5	10.9	14.8
PE (x)	20.3	20.7	21.8	16.1
P/B (x)	2.3	2.1	2.0	1.8
EV/EBITDA (x)	12.4	12.5	11.8	8.8
RoE (%)	11.1	10.1	9.0	11.1
RoCE (%)	14.7	13.6	12.0	14.9

Source: Company; Sharekhan estimates

Muted Q1; weak revenue growth and steep margin contraction

ZEE Entertainment Limited (ZEEL) reported weak Q1FY23 results with a 6%/20% miss in consolidated revenue/ EBITDA at Rs. 1,846 crore/Rs. 236 crore, up 4% y-o-y and down 32% y-o-y respectively due to weak advertising and subscription revenues and 223 bps miss in OPM at 12.8% (down 661 bps y-o-y; down 817 bps q-o-q). Revenues missed the mark due to muted advertisement revenue growth of 5.4% y-o-y to Rs. 9,763 crore as it got affected by FTA withdrawals (Zee Anmol) and lower ad-spends by brands due to weak macroeconomic conditions while subscription revenue declined by 5.1% y-o-y to Rs. 7,717 crore as pricing embargo impacted revenue growth and impact of timing of some of B2B deals and renewals. OPM was severely hit by weak revenue growth and higher programming & technology and marketing cost due to higher theatrical releases, investment in ZEE5 and new launches in linear business. Adjusted PAT of Rs. 121 crore (down 46.5% y-o-y; down 53.6% q-o-q) sharply missed our estimate of Rs. 179 crore due to weaker revenue growth and higher-than-expected contraction in margins. We have adjusted reported PAT of Rs. 107 crore (down 50.1% y-o-y) for an exceptional expense of Rs. 15 crore as the company has accounted for the same towards debt service reserve account (DSRA guarantee) in relation to certain financial facilities.

Q1FY23 conference call highlights

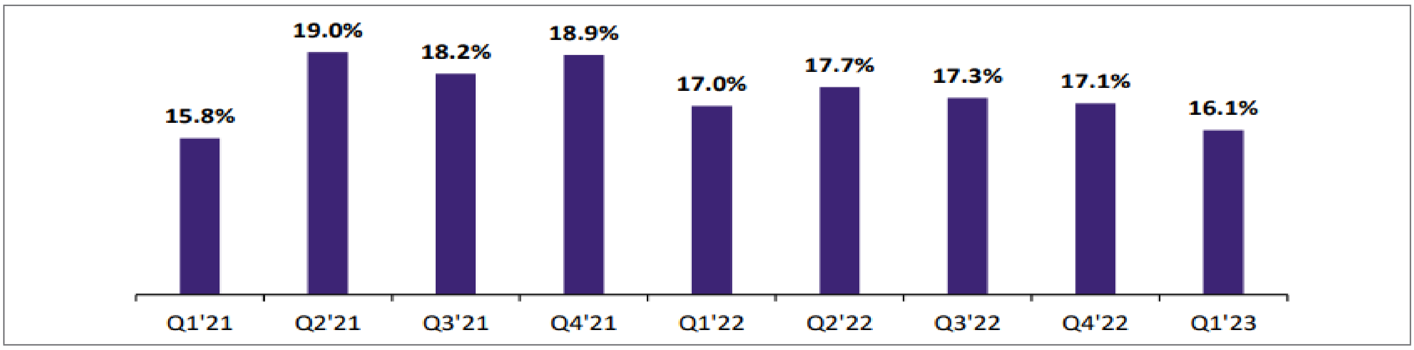
- **ZEE5's operating metrics:** ZEE5 recorded 103 million and 11.3 million global Monthly Active Users and Daily Active Users, respectively, in June. 2022. It released 38 shows & movies (incl. 8 originals) in the quarter. Average watch-time per viewer per month in Q1FY23 stands at 196 minutes. Management expects subscription revenues will bounce back due to 40% increase in annual subscription of ZEE5 to Rs. 699 and consummation of B2B deals.
- **Advertising outlook:** Advertising revenues are softening due to the impact of inflationary environment and macro headwinds especially from the FMCG sector. The company is focusing on recovering its loss in market share, especially in Hindi GEC. The company Advertising revenue should improve in H2FY23 due to the festive season and softening of commodity prices.
- **Viewership Share:** ZEEL said that sequentially there has been improvement in the viewership share excluding Zee Anmol.
- **Awaiting approval for proposed Sony merger:** ZEEL has received approval from both the stock exchanges for the scheme of arrangement for merger with Sony. Teams from both the companies working independently to get other necessary regulatory approvals.
- **Dues from related parties:** Receivables from Dish TV have come down by 21% q-o-q to Rs. 190 crore in Q1FY23. Receivables of Rs. 35.2 crore from Siti are delayed, of which Rs. 15.5 crore has been deposited against court order.
- **Balance sheet Items:** Inventories rose by 5.8% q-o-q to Rs. 676 crore. Trade receivables declined by 5.7% q-o-q to Rs. 164 crore. Cash & Cash equivalents fell by 13% q-o-q to Rs. 113 crore.

Results (Consolidated) Rs cr

Particulars	Q1FY23	Q1FY22	Q4FY22	Y-o-Y %	Q-o-Q %
Advertising Revenues	976.3	926.6	1,119.8	5.4	-12.8
Subscription Revenues	771.7	813.1	854.9	-5.1	-9.7
Other sales and Services	97.7	35.3	348.2	176.7	-71.9
Total Revenues	**1,845.7**	**1,775.0**	**2,322.9**	**4.0**	**-20.5**
Programming and Operating Cost	1002.6	866.4	1257.9	15.7	-20.3
Staff Cost	217.2	228.0	218.9	-4.7	-0.8
Admin. & Selling Expenses	390.1	336.6	359.6	15.9	8.5
EBITDA	**235.8**	**344.0**	**486.6**	**-31.5**	**-51.5**
Depreciation	77.8	59.0	67.7	32.0	15.0
Finance Cost	8.1	1.9	38.1	319.7	-78.7
Other Income	33.8	33.6	38.3	0.6	-11.7
PBT	**183.7**	**306.9**	**439.4**	**-40.2**	**-58.2**
Tax Provision	62.1	94.5	157.2	-34.2	-60.5
PAT	**121.5**	**212.5**	**282.2**	**-42.8**	**-56.9**
Reported Net Income	**106.6**	**213.7**	**181.9**	**-50.1**	**-41.4**
Adjusted Net profit after EO	**121.6**	**227.2**	**261.9**	**-46.5**	**-53.6**
Adjusted EPS (Rs.)	**1.3**	**2.4**	**2.7**	**-46.5**	**-53.6**
Margin (%)			**BPS**		**BPS**
OPM	12.8	19.4	20.9	-661	-817
Adjusted NPM	6.6	12.8	11.3	-621	-469
Tax rate	33.8	30.8	35.8	305	-195

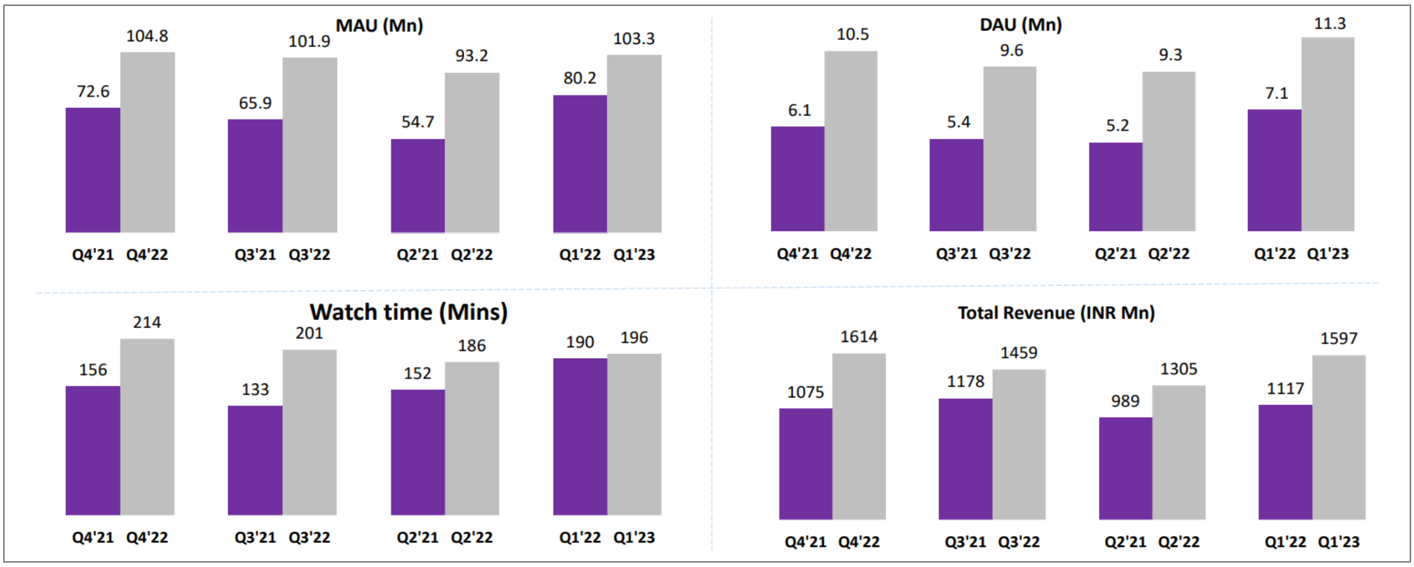
Source: Company; Sharekhan Research

ZEEL's network share trend



Source: Company

Digital business performance trend



Source: Company

Outlook and Valuation

■ Sector View – Expect gradual recovery in M&E industry

As per a KPMG report, the Indian media and entertainment (M&E) industry growth would be significantly impacted owing to nationwide lockdown restrictions owing to the pandemic, slowdown in advertising spends and breaking down of content supply chains. However, the M&E sector is expected to bounce back in 2022 with a 33.1% y-o-y growth to reach Rs. 1.86 trillion. The television segment is expected to revert to an 8.6% y-o-y growth in 2022 on account of a gradual recovery in ad revenue and 4% growth in subscription revenue. We expect television as a medium to continue to stay relevant and the most preferred choice for advertisers, given its reach to the mass audience.

■ Company Outlook – Proposed merger would enhance reach potential

ZEEL is one of India's leading media & entertainment companies, primarily engaged in broadcasting, movies and music production and digital business. The company has a strong presence in the GEC segment, given deep regional penetration and has expanded its presence in movie genre with the launch of new channels. We believe that ZEE5's focus on aggressively building a content catalogue is a step in the right direction given the hyper-competitive nature of the market. The merger is expected to strengthen ZEEL's portfolio with Sony's sport, kids and English movie content. Management stated that priority of focus of the combined entity would be 1) advertisement, 2) subscription, and 3) international business. The combined entity will be in a superior position on maximizing its revenue given its reach potential and investments on digital and sports business.

■ Valuation – Maintain Buy with revised PT of Rs. 310

ZEEL has been progressing well on digital business with launching new shows each quarter. . We believe the merger would be a strategic fit from a revenue perspective and would help the combined entity to emerge as a strong player in the entertainment industry for capturing the significant opportunity in the linear business. Further, the merged entity would allocate its growth capital towards premium content, including sports event rights, which would strengthen its position in the OTT space. We expect the company to deliver a 14% CAGR in adjusted net profit over FY2022-FY2024E. The stock currently trades at a reasonable valuation at 22x/16x of FY2023E/FY2024E earnings. Given its strong regional presence and strong traction on its digital platform, we maintain Buy rating on ZEEL with a revised PT of Rs. 310 (reflecting a cut in earnings estimates).

One-year forward P/E (x) band

Source: Company, Sharekhan Research

About company

ZEEL is one of India's largest vertically-integrated media and entertainment companies, primarily engaged in broadcasting and content development with the widest language footprint, movies and music production, live events, and digital business. The company is amongst the largest producers and aggregators of entertainment content in the world, with an extensive library housing over 250,000 hours of television content. ZEEL houses the world's largest Hindi film library with rights to more than 4,200 movie titles from foremost studios and of iconic film stars. Through its strong presence worldwide, ZEEL is present across 170+ countries and has a reach to over 1.3 billion viewers.

Investment theme

The company has delivered a strong revenue CAGR of 8% over FY2015-FY2021 despite strict lockdown restrictions owing to outbreak of COVID-19 in FY2021.ZEEL's management remains confident of delivering advertising revenue growth, ahead of industry growth rate. Hence, the company is considered as one of the leading players under the structural India consumption theme. The proposed merger with SPNI will create the largest media company in India across languages and genres, with around 25% market share.

Key Risks

Unfavourable regulatory guidelines impacting subscription revenue, a slowdown in the economic environment leading to lower demand, and subdued realisation for advertisement revenue stream. Delay in monetisation benefit from digitisation and increased investments in ZEE5 could affect earnings.

Additional Data

Key management personnel

Punit Goenka	Managing Director and CEO
Amit Goenka	President - Digital Businesses & Platforms
Anurag Bedi	Chief Business Officer – Zee Music
Rohit Kumar Gupta	Chief Financial Officer
Ashish Agarwal	Chief Compliance Officer & Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Invesco Limited	17.92
2	OFI GBL China FD LLC	10.14
3	Invesco Oppenheimer	7.74
4	Blackrock Inc	5.01
5	Life Insurance Corp of India	4.89
6	The Vanguard Group Inc.	4.86
7	Amansa Capital Private Limited	4.38
8	HSBC Holding PLC	2.74
9	Nippon Life India Asset Management	2.64
10	Norges Bank	2.47

Source: Bloomberg (old data)

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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