

Potential breakdown on the cards

Media & Entertainment ▶ Company Update ▶ January 8, 2024

TARGET PRICE (Rs): 315

According to media reports, Sony India is close to calling off the merger with Zee Entertainment. Sony is likely to issue a termination notice by 20-Jan-24; now, the decision on who would be at the helm of the merged company is the contentious issue, according to these reports. After receiving all necessary regulatory approvals, this breakdown can be a setback to both Sony and Zee, having both reported subpar growth over the last year. We believe the merger not going through will be a lose-lose for both parties, particularly in the face of competition with a much larger entity of Reliance-Disney (if the merger goes through). Both parties will potentially have to recalibrate their strategies from ground zero, which would be a tall order. We believe clarity should emerge in the next couple of weeks regarding a final decision concerning the merger, and if it does not go through, we see significant downside from current levels. Hence, we advise caution in the stock.

Zee Entertainment: Financial Snapshot (Consolidated)

Y/E March (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Revenue	81,893	80,879	87,536	90,312	97,737
EBITDA	17,221	11,011	11,827	18,763	21,179
Adj. PAT	11,016	5,811	6,011	11,308	13,237
Adj. EPS (Rs)	10.0	0.5	5.0	11.8	13.8
EBITDA margin (%)	21.0	13.6	13.5	20.8	21.7
EBITDA growth (%)	(3.8)	(36.1)	7.4	58.6	12.9
Adj. EPS growth (%)	20.6	(95.0)	898.1	137.1	0.0
RoE (%)	10.6	5.5	5.6	9.9	10.8
RoIC (%)	12.0	6.1	6.1	10.3	11.4
P/E (x)	24.2	46.0	44.4	23.6	20.2
EV/EBITDA (x)	14.8	23.9	22.6	14.1	12.3
P/B (x)	2.5	2.6	2.4	2.3	2.1
FCFF yield (%)	(0.5)	(0.8)	(2.0)	2.5	2.4

Source: Company, Emkay Research

Lose-lose if no merger happens

The potentially merged Sony-Zee entity would have been a formidable competitor to the Reliance-Disney association, given that it has fared better than the latter on most parameters. However, the standalone entities can be vulnerable to competition from the significantly larger entity (if the Reliance-Disney merger gets consummated). Zee's advertising revenue growth has been sluggish (-8% in FY23, -3.5% in H1FY24), despite FMCG companies ramping up their spending. This can be attributed to i) the shrinking share of television advertising vis-à-vis digital and ii) sports advertising gaining at the cost of GECs. The standalone entities also risk the foregoing synergies; we had estimated 4% revenue synergies (of the total revenue) accruing from better bargaining power with content producers, distributors, and advertisers along with some cost rationalization.

Investments to also be potentially hit

To plug the gap on the sports side, Zee signed an agreement with Disney Star in Aug-22 to purchase television broadcasting rights of the ICC Men's Cricket and U-19 events for four years (2024-27). As per our calculations, Zee would have to pay Rs110-120bn over the tenure of this deal. However, with the merger possibly not going through, we believe this deal will be in jeopardy as such a large payment will not be justified on a standalone basis. Zee5 has also seen its losses widen due to upfront fixed costs and has been unable to reverse its losses yet. With a focus on profitability, growth can potentially suffer. SonyLiv on its part has managed to scale its SVOD base better (33.3mn as per latest estimates in May-23). However, it has been unable to achieve leadership on the linear TV side. In our view, the failure of the merger could force both companies to have a complete relook at their strategies, potentially squandering a time of more than two years. The stock has traded at a valuation of ~17x its one-year fwd. EV/EBITDA over the last 10 years (our valuation adjusts for OTT losses); it has de-rated over the last couple of years but can see significant further de-rating if the merger does not consummate.

Target Price – 12M	Sep-24
Change in TP (%)	-
Current Reco.	BUY
Previous Reco.	BUY
Upside/(Downside) (%)	13.1
CMP (08-Jan-24) (Rs)	278.2

Stock Data	Ticker
52-week High (Rs)	300
52-week Low (Rs)	170
Shares outstanding (mn)	960.5
Market-cap (Rs bn)	267
Market-cap (USD mn)	3,214
Net-debt, FY24E (Rs mn)	-20
ADTV-3M (mn shares)	16
ADTV-3M (Rs mn)	4,260.9
ADTV-3M (USD mn)	51.3
Free float (%)	96.0
Nifty-50	21,513
INR/USD	83.1
Shareholding, Sep-23	
Promoters (%)	4.0
FPIs/MFs (%)	35.0/42.2

Price Performance

(%)	1M	3M	12M
Absolute	(0.3)	6.7	17.0
Rel. to Nifty	(2.8)	(2.5)	(2.9)

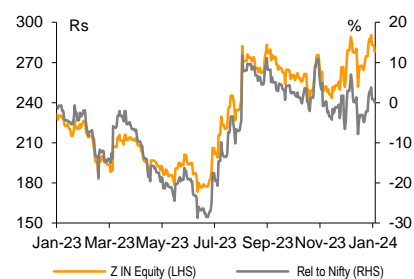
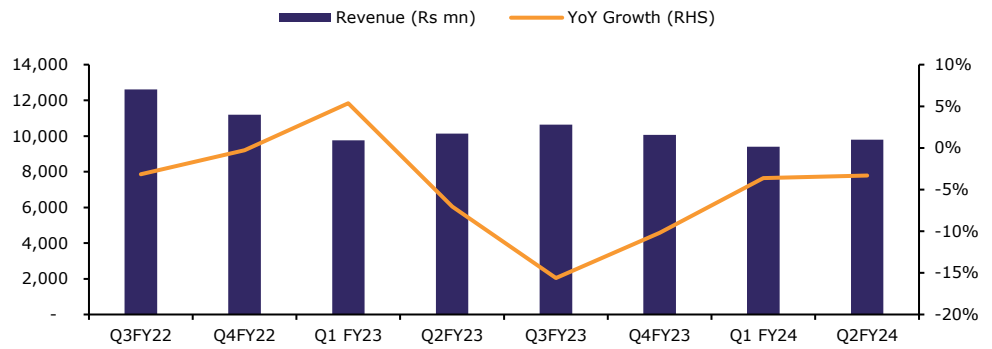
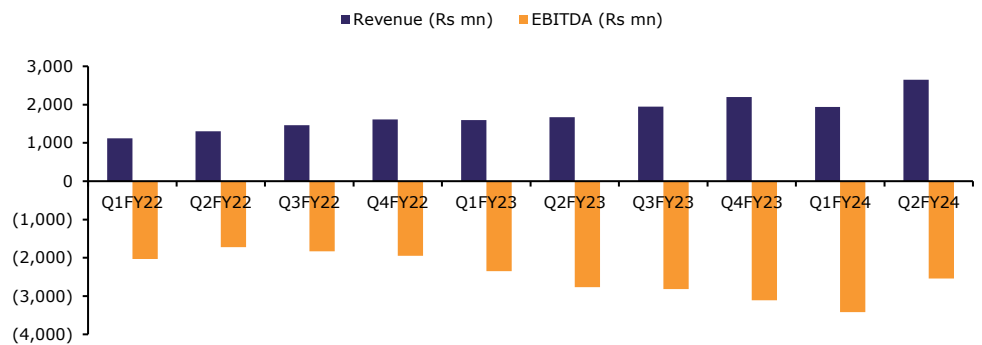
1-Year share price trend (Rs)**Pulkit Chawla**pulkit.chawla@emkayglobal.com
+91 22 6624 2458

Exhibit 1: Zee's advertising growth has been sluggish over the last couple of years



Source: Company, Emkay Research

Exhibit 2: Zee5 – EBITDA losses have increased despite revenue growth



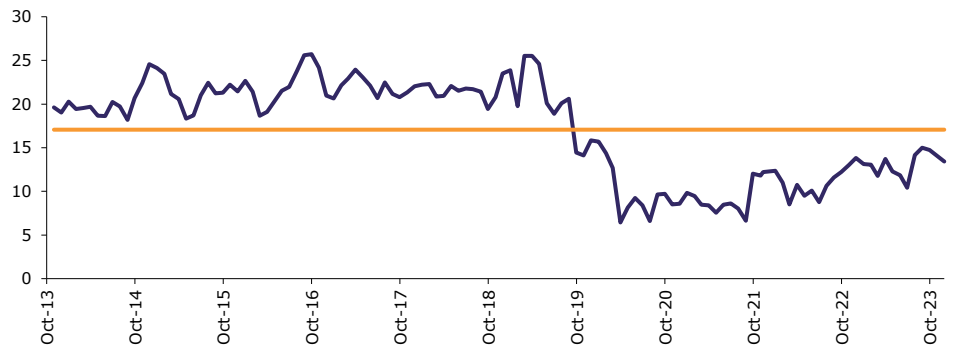
Source: Company, Emkay Research

Exhibit 3: Zee5 – MAUs and DAUs have shown moderation in growth

Zee5 (reported)	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23
MAUs (mn)	40	55	66	43	80	93	102	105	103	112	120	114
DAUs (mn)	4	5	5	6	7	9	10	11	11	11	12	11

Source: Company, Emkay Research

Exhibit 4: One-year forward EV/EBITDA valuation



Source: Company, Emkay Research

Zee Entertainment: Consolidated Financials and Valuations

Profit and Loss					
Y/E March (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Revenue	81,893	80,879	87,536	90,312	97,737
Revenue growth (%)	5.9	(1.2)	8.2	3.2	8.2
EBITDA	17,221	11,011	11,827	18,763	21,179
EBITDA growth (%)	(3.8)	(36.1)	7.4	58.6	12.9
Depreciation & Amortization	2,459	3,128	3,685	3,841	4,060
EBIT	14,762	7,884	8,142	14,922	17,119
EBIT growth (%)	(3.2)	(46.6)	3.3	83.3	14.7
Other operating income	0	0	0	0	0
Other income	1,213	797	600	840	960
Financial expense	451	702	828	640	680
PBT	15,524	7,979	7,914	15,122	17,399
Extraordinary items	(1,370)	(5,333)	(1,241)	0	0
Taxes	4,597	2,167	1,901	3,806	4,154
Minority interest	88	0	0	0	0
Income from JV/Associates	1	(1)	(2)	(8)	(8)
Reported PAT	9,646	478	4,770	11,308	13,237
PAT growth (%)	20.6	(95.0)	898.1	137.1	17.1
Adjusted PAT	11,016	5,811	6,011	11,308	13,237
Diluted EPS (Rs)	10.0	0.5	5.0	11.8	13.8
Diluted EPS growth (%)	20.6	(95.0)	898.1	137.1	0.0
DPS (Rs)	2.5	0.0	1.5	3.5	4.1
Dividend payout (%)	24.9	0.0	30.0	30.0	30.0
EBITDA margin (%)	21.0	13.6	13.5	20.8	21.7
EBIT margin (%)	18.0	9.7	9.3	16.5	17.5
Effective tax rate (%)	29.6	27.2	24.0	25.2	23.9
NOPLAT (pre-IndAS)	10,390	5,743	6,186	11,166	13,032
Shares outstanding (mn)	960.3	960.3	960.3	960.3	960.3

Source: Company, Emkay Research

Cash Flows					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
PBT	15,524	7,979	7,914	15,122	17,399
Others (non-cash items)	0	0	0	0	0
Taxes paid	(4,597)	(2,167)	(1,901)	(3,806)	(4,154)
Change in NWC	(9,849)	(3,436)	(11,120)	(6,003)	(8,433)
Operating cash flow	1,669	1,741	(2,666)	9,146	8,864
Capital expenditure	(2,915)	(3,793)	(2,800)	(2,500)	(2,500)
Acquisition of business	0	0	0	0	0
Interest & dividend income	270	270	270	270	270
Investing cash flow	5,630	(2,675)	(2,200)	(1,660)	(1,540)
Equity raised/(repaid)	0	0	0	0	0
Debt raised/(repaid)	(3,468)	2,057	55	0	0
Payment of lease liabilities	353	2,033	55	0	0
Interest paid	(451)	(702)	(828)	(640)	(680)
Dividend paid (incl tax)	(2,401)	0	(1,431)	(3,392)	(3,971)
Others	11,751	5,526	9,007	0	0
Financing cash flow	5,431	6,881	6,803	(4,032)	(4,651)
Net chg in Cash	12,731	5,948	1,937	3,454	2,673
OCF	1,669	1,741	(2,666)	9,146	8,864
Adj. OCF (w/o NWC chg.)	(8,180)	(1,695)	(13,786)	3,143	432
FCFF	(1,246)	(2,052)	(5,466)	6,646	6,364
FCFE	(1,427)	(2,484)	(6,024)	6,276	5,954
OCF/EBITDA (%)	9.7	15.8	(22.5)	48.7	41.9
FCFE/PAT (%)	(14.8)	(519.8)	(126.3)	55.5	45.0
FCFF/NOPLAT (%)	(12.0)	(35.7)	(88.3)	59.5	48.8

Source: Company, Emkay Research

Balance Sheet					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Share capital	961	961	961	961	961
Reserves & Surplus	1,07,665	1,04,222	1,09,375	1,17,291	1,26,556
Net worth	1,08,626	1,05,183	1,10,336	1,18,251	1,27,517
Minority interests	0	0	0	0	0
Deferred tax liability (net)	(3,080)	(4,229)	(4,229)	(4,229)	(4,229)
Total debt	763	2,820	2,875	2,875	2,875
Total liabilities & equity	1,06,309	1,03,773	1,08,982	1,16,897	1,26,163
Net tangible fixed assets	6,073	7,455	7,770	7,764	5,968
Net intangible assets	5,343	4,645	3,376	2,031	582
Net ROU assets	835	1,497	1,566	1,576	3,262
Capital WIP	872	191	191	191	191
Goodwill	0	0	0	0	0
Investments [JV/Associates]	0	0	0	0	0
Cash & equivalents	13,382	6,278	2,895	6,149	8,542
Current assets (ex-cash)	1,02,781	1,09,230	1,21,132	1,26,521	1,40,113
Current Liab. & Prov.	23,005	27,167	27,949	27,335	32,495
NWC (ex-cash)	79,776	82,062	93,183	99,186	1,07,618
Total assets	1,06,309	1,03,773	1,08,982	1,16,897	1,26,163
Net debt	(12,619)	(3,457)	(20)	(3,274)	(5,667)
Capital employed	1,06,281	1,02,128	1,08,982	1,16,897	1,26,163
Invested capital	92,027	95,660	1,05,895	1,10,557	1,17,430
BVPS (Rs)	113.1	107.8	114.9	123.1	132.8
Net Debt/Equity (x)	(0.1)	0.0	0.0	0.0	0.0
Net Debt/EBITDA (x)	(0.7)	(0.3)	0.0	(0.2)	(0.3)
Interest coverage (x)	0.0	0.1	0.1	0.0	0.0
RoCE (%)	15.4	8.3	8.3	14.0	14.9

Source: Company, Emkay Research

Valuations and Key Ratios					
Y/E Mar	FY22	FY23	FY24E	FY25E	FY26E
P/E (x)	24.2	46.0	44.4	23.6	20.2
P/CE(x)	19.8	29.9	27.5	17.6	15.4
P/B (x)	2.5	2.6	2.4	2.3	2.1
EV/Sales (x)	3.1	3.3	3.1	2.9	2.7
EV/EBITDA (x)	14.8	23.9	22.6	14.1	12.3
EV/EBIT(x)	17.2	33.4	32.8	17.7	15.3
EV/IC (x)	2.8	2.8	2.5	2.4	2.2
FCFF yield (%)	(0.5)	(0.8)	(2.0)	2.5	2.4
FCFE yield (%)	(0.5)	(0.9)	(2.3)	2.3	2.2
Dividend yield (%)	0.9	0.0	0.5	1.3	1.5
DuPont-RoE split					
Net profit margin (%)	13.5	7.2	6.9	12.5	13.5
Total asset turnover (x)	0.8	0.8	0.8	0.8	0.8
Assets/Equity (x)	1.0	1.0	1.0	1.0	1.0
RoE (%)	10.6	5.5	5.6	9.9	10.8
DuPont-RoIC					
NOPLAT margin (%)	12.7	7.1	7.1	12.4	13.3
IC turnover (x)	0.9	0.9	0.9	0.8	0.9
RoIC (%)	12.0	6.1	6.1	10.3	11.4
Operating metrics					
Core NWC days	355.6	370.3	388.5	400.9	401.9
Total NWC days	355.6	370.3	388.5	400.9	401.9
Fixed asset turnover	3.1	2.8	2.7	2.6	2.6
Opex-to-revenue (%)	29.6	31.1	32.3	31.2	30.8

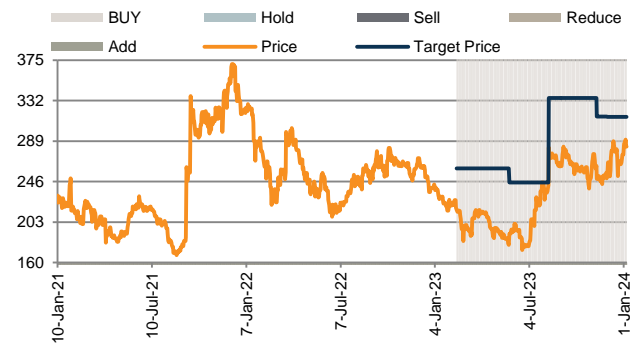
Source: Company, Emkay Research

RECOMMENDATION HISTORY - DETAILS

Date	Closing Price (INR)	TP (INR)	Rating	Analyst
30-Nov-23	253	315	Buy	Pulkit Chawla
10-Nov-23	249	315	Buy	Pulkit Chawla
02-Nov-23	269	335	Buy	Pulkit Chawla
10-Aug-23	282	335	Buy	Pulkit Chawla
10-Aug-23	282	265	Buy	Pulkit Chawla
26-May-23	191	245	Buy	Pulkit Chawla
14-Feb-23	216	260	Buy	Pulkit Chawla

Source: Company, Emkay Research

RECOMMENDATION HISTORY - TREND



Source: Bloomberg, Company, Emkay Research

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BUY	>15% upside
ADD	5-15% upside
REDUCE	5% upside to 15% downside
SELL	<15% downside

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7th Floor, The Ruby, Senapati Bapat Marg, Dadar - West, Mumbai - 400028. India
Tel: +91 22 66121212 Fax: +91 22 66121299 Web: www.emkayglobal.com

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