

13 October 2018

Zee Entertainment

Cautiously optimistic; maintaining a Buy

Rating: **Buy**

Target Price: Rs220

Share Price: Rs186

In the last 12-15 months, on concerns—promoter group (pledged shares), related-party loans/corporate guarantees given on behalf of group companies and balance sheet (rising inventory/receivables), Zee's multiples have been depressed. Though we believe that some issues such as related-party concerns persist, we reiterate that revenue and EBITDA have bottomed out in Q1 FY21 and should improve from now. Also, recent board-member changes, better disclosures (quarterly balance sheets, Zee5 figures, etc.) and lower receivables/inventory (as indicated by management) should ease such concerns. We are cautiously optimistic and maintain our Buy, with an unchanged target of Rs220 (valuing Zee at 10x FY22e EBITDA).

Key FY20 annual report highlights. **1)** Investment in movie satellite rights rose, increasing inventory by Rs14.83bn to Rs53.48bn (inventory days lengthened by 86 days to 261); **2)** Trade receivables rose Rs289m in FY20 to Rs20.85bn (receivables days lengthened by 10 to 94); **3)** The company had trade receivables of Rs8.15bn from two strategic customers (Dish TV and Siti Networks), including amounts long overdue; **4)** After the stake sale, the promoters' stake has shrunk to 4.77% (~16.4% pledged) from 38.2% in FY19; **5)** The company did not disclose subscription income from Dish TV as a related party (Rs4.84bn in FY19). Our estimates suggest this should be Rs5bn+ in FY20 (~20% of domestic subscription income), **6)** An accelerated content amortisation charge of Rs2.6bn. Also provision of Rs3.4bn, including Rs1.2bn from a related-party distributor due to Covid-19.

Q2 FY21 results preview. We expect revenue to drop 18.8% y/y to Rs17.23bn due to a 30% y/y fall in domestic advertising revenues and flat y/y growth in domestic subscription revenues (high base). We expect the EBITDA margin to contract 1,070bps y/y to 22% (though q/q up 520bps).

Retaining a Buy. We now value Zee at 10x FY22e EBITDA and retain our Buy rating, and target price of Rs220. **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)	11.3	10.7	31.8	18.3	13.5
EV / EBITDA (x)	7.3	5.9	9.3	10.1	7.6
PBV (x)	2.2	1.9	1.8	1.7	1.6
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

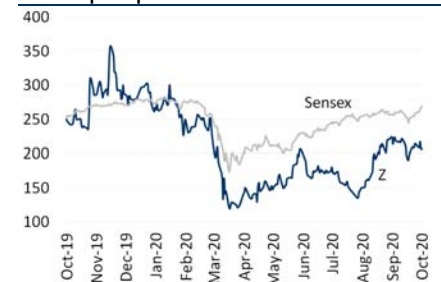
Source: Company, Anand Rathi Research

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Key data	Z IN / ZEE.BO
52-week high / low	Rs364 / 114
Sensex / Nifty	40183 / 11835
3-m average volume	\$106.6m
Market cap	Rs198bn / \$2700.2m
Shares outstanding	961m

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

Relative price performance



Source: Bloomberg

Shobit Singhal
Research Analyst

Quick Glance – Financials and Valuations

Fig 1 – Income statement (Rs 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 %	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
EBITDA	20,761	25,639	16,347	14,981	20,002
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 rate (%)	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 (Rs / sh)	14.0	16.3	5.5	9.5	12.9

Fig 3 – Cash-flow statement (Rs 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 (Rs m)

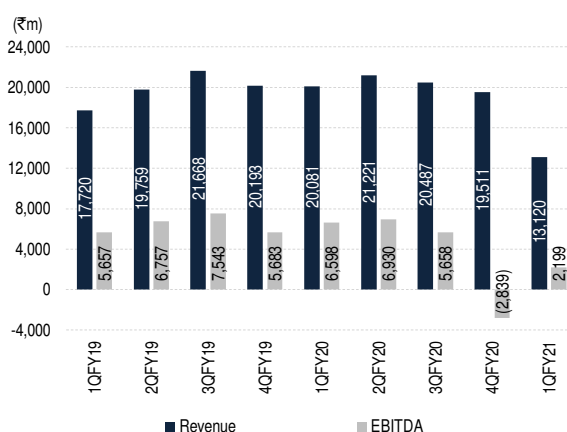
Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
Share capital	961	961	961	961	961
Net worth	75,617	89,239	93,439	99,163	1,07,416
Total debt	15,245	11,114	5,950	4,950	3,950
Minority interest	142	143	110	110	110
DTL / (Assets)	-	-	-2,742	-2,742	-2,742
Capital employed	91,004	1,00,496	96,757	1,01,481	1,08,734
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
Capital deployed	91,004	1,00,497	96,758	1,01,481	1,08,735
Contingent liabilities	6,969	5,514	3,551	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY18	FY19	FY20	FY21e	FY22e
P/E (x)	11.3	10.7	31.8	18.3	13.5
EV / EBITDA (x)	7.3	5.9	9.3	10.1	7.6
EV / sales (x)	2.0	1.7	1.7	2.1	1.7
P/B (x)	2.2	1.9	1.8	1.7	1.6
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

Annual report summary (five years)

Fig 7 – Annual report summary of the last five years

	FY16	FY17	FY18	FY19	FY20
Revenues (Rs m)	58,125	64,342	66,857	79,339	81,299
<i>Growth %</i>	19.0	10.7	3.9	18.7	2.5
Advertising	33,652	36,735	42,048	50,367	46,812
<i>Revenue contribution %</i>	57.9	57.1	62.9	63.5	57.6
<i>Y/Y growth %</i>	26.5	9.2	14.5	19.8	-7.1
Subscriptions	20,579	22,629	20,287	23,106	28,873
<i>Revenue contribution %</i>	35.4	35.2	30.3	29.1	35.5
<i>Y/Y growth %</i>	14.7	10.0	-10.3	13.9	25.0
Others	3,894	4,978	4,522	5,867	5,614
<i>Revenue contribution %</i>	6.7	7.7	6.8	7.4	6.9
<i>Y/Y growth %</i>	-9.4	27.8	-9.2	29.7	-4.3
PAT (incl. exceptional items)	8,236	22,202	14,778	15,672	5,247
PAT (excl. exceptional items)	8,567	9,967	13,432	15,890	8,090
<i>PAT margins %</i>	14.7	15.5	20.1	20.0	10.0
EBITDA	15,136	19,269	20,761	25,639	16,347
<i>EBITDA margins %</i>	26.0	29.9	31.1	32.3	20.1
Intangibles / Goodwill	491	458	1734	1383	1372
Capital employed	66,048	86,771	91,896	101,846	100,904
<i>Intangibles as % of total capital employed</i>	0.7	0.5	1.9	1.4	1.4
Dividend payout ratio %	25.2	21.7	20.7	20.7	19.0
BVPS (₹)	50.0	69.7	78.7	92.9	97.3
Stock options allotted	Not granted any	9,800	18,900	12,880	16,735
<i>As % of existing share capital</i>	NA	0.0	0.0	0.0	0.0
Audit committee members	4	4	4	4	4
Board members	8	8	8	8	8
Independent directors on the audit committee	3	3	3	3	3
CEO / Promotor on the audit committee	Yes - Ashok Kurien, co-founder	Yes - Ashok Kurien, co-founder	Yes - Ashok Kurien, co-founder	Yes - Ashok Kurien, co-founder	Yes - Ashok Kurien, co-founder
Remuneration committee members	3	3	3	3	4
Board members	8	8	8	8	8
Independent directors, remuneration committee	2	2	2	2	3

Source: Company, Anand Rathi Research

Fig 7 – Annual report summary of the last five years (contd.)

	FY16	FY17	FY18	FY19	FY20
CEO / promoters in the remuneration committee	Yes - Subodh Kumar, co-founder	Yes - Subodh Kumar, co-founder	Yes - Subodh Kumar, co-founder	Yes - Subodh Kumar, co-founder	Yes - Ashok Kurien, co-founder
Independent directors on the Board	4	4	4	4	4
Auditor	MGB & Co LLP	MGB & Co LLP	Deloitte	Deloitte	Deloitte
ETR % (excl. exceptional items)	-39.1	-40.6	-38.5	-35.3	-34.7
ETR % (incl. exceptional items)	-40.1	-23.5	-36.3	-35.7	-45.0
Top-five directors / KMP compensation					
Ratio to the median					
Subhash Chandra	3.1	3.1	3.1	3	4.77
Subodh Kumar	49.1	3.1	3.1	3	2.04
Punit Goenka	99.1	97.1	99.1	83.0	90.2
Ashok Kurien	3.1	3.1	3.1	3	5.54
% increase					
Subhash Chandra	Nil	10.0	25.0	9.0	59.0
Subodh Kumar	8.0	10.0	25.0	9.0	NA
Punit Goenka	15.0	5.0	9.0	9.0	8.7
Ashok Kurien	Nil	10.0	25.0	9.0	84.7
Median increase in compensation of employees %	9	8	12	9.20	18.47
Permanent employees on the rolls	2,121	2,034	1,931	1,776	3,083
CFO : Net income %	85.3	74.3	41.3	8.5	30.9
CFO : EBITDA %	48.3	38.4	26.7	5.3	15.3
FCF : Net income %	49.3	46.5	17.5	-9.3	8.4
FCF : EBITDA %	27.9	24.1	11.3	-5.7	4.2
EPS growth %	2.9	16.4	34.8	16.7	-66.5
BVPS growth %	36.1	39.2	13.0	18.0	4.7
Inventory holding (days)	79	94	131	175	261
Receivables (days)	85	70	84	84	94
Payables (days)	40	68	91	101	94
Capex	-3083	-2768	-3191	-2823	-1818
As % of revenue	-5.3	-4.3	-4.8	-3.6	-2.2
As % of EBITDA	-20.4	-14.4	-15.4	-11.0	-11.1
D&A	-777	-1152.3	-1821	-2347.2	-2706.3
Total GFA (incl. intangibles)	8020	9534	13545	15573	16854.14
D&A as % of GFA incl. intangibles	-10.8	-13.1	-15.8	-16.1	-16.7
Working capital, excl. cash and current debt	25,740	34,821	43,918		
Goodwill on consolidation	8,843	2,676	5,467	5,252	4,070
Goodwill addition / deduction explanation	Goodwill rose by Rs956m, chiefly on acquiring the entire 4.5 lakh shares of Sarthak Entertainment Pvt Ltd (Odiya language channel)	Goodwill reduced by Rs6167m chiefly on de-recognition of goodwill relating to the sports business	Goodwill rose by Rs2791m, chiefly on acquiring the balance 49% stake in India Webportal Pvt Ltd	Goodwill reduced by Rs218m chiefly on impairment of the online media business	Goodwill reduced by Rs1182m chiefly on impairment of the online media business

Source: Company, Anand Rathi Research

Fig 7 – Annual report summary of last five years (contd.)

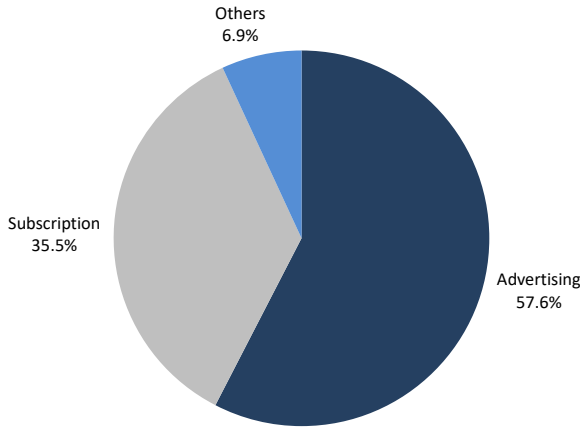
	FY16	FY17	FY18	FY19	FY20
Capital employed	66,048	86,771	91,896	101,846	100,904
Goodwill as % of capital employed	13.4	3.1	5.9	5.2	4.0
Cash and investments	19,246	38,001	29,813	20,794	10,115
As % of capital employed (incl. all investments)	29.1	43.8	32.4	20.4	10.0
Debt	17,149	19,088	15,245	11,114	5,950
Net cash balance	2,097	18,913	14,568	9,680	4,165
Contingent liabilities	29,604	11,594	6,969	5,514	3,551
As % of PAT (excl. exceptional items)	345.6	116.3	51.9	34.7	43.9
Related party transactions (consolidated)	31,551	15,421	12,465	13,701	12,499
Guarantees given	22,174	5,057	1,037	1,137	1,973
Claims against the company not acknowledged as debt	948	611	650	440	317
Key related party transactions					
Subscription income					
Dish TV, India	1,839	2,313	2,442	4,839	
Siti Networks	676	707	746	1012	1233
Others	58	209	293	376	722
Corporate guarantees given					
Taj TV	21,374	4,018	Nil		
Broadcast Audience Research Council	170	170	170	170	34
Siti Networks	630	869	867	967	1,166
Purchase of Services					
Broadcast Audience Research Council		273	287	383	368
Digital Subscriber Management & Consultancy Services Pvt. Ltd.	503	528	563	582	581
Essel Business Excellence Services		197	302	743	622
Siti Networks	356	261	270	249	380
Essel Corporate Resources Pvt. Ltd.	240	200	366		
Fly by Wire International Pvt. Ltd.		267	88		
Others	1280	602	654	1077	1114
FCF	4,225	4,638	2,353	-1,471	681
Cash paid to shareholders	-4,051	-4,065	-3,834	-4,734	-5,227

Source: Company, Anand Rathi Research

Annual report analysis, FY20

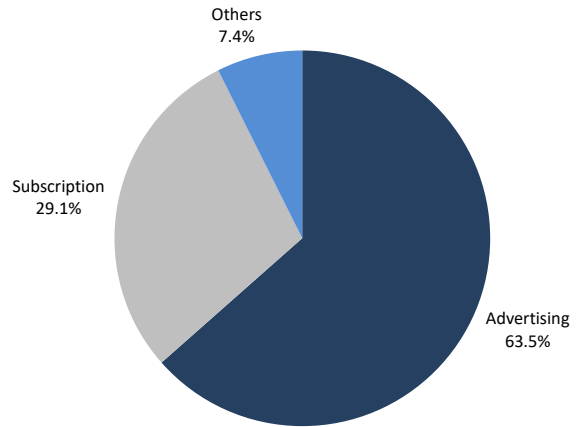
With 37 channels in five categories domestically (Hindi GEC, Hindi movies, regional general entertainment, regional movies, niche categories) and internationally with 35 Indian-language channels, eight non-Indian-language channels and digital platforms, Zee offers a broad range of content for a widely diverse Indian audience at home and abroad.

Fig 8 – Revenue breakdown, FY20 ₹81,299m



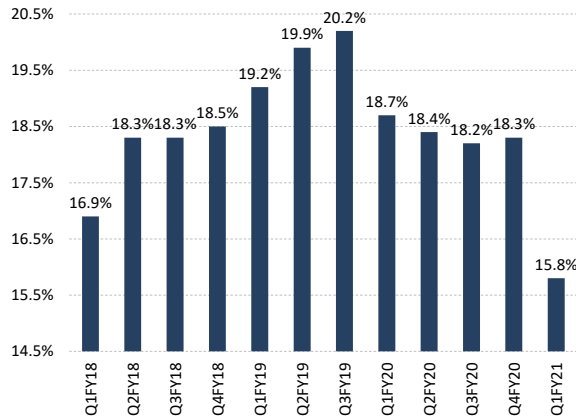
Source: Company, Anand Rathi Research

Fig 9 – Revenue breakdown, FY19 ₹79,339m



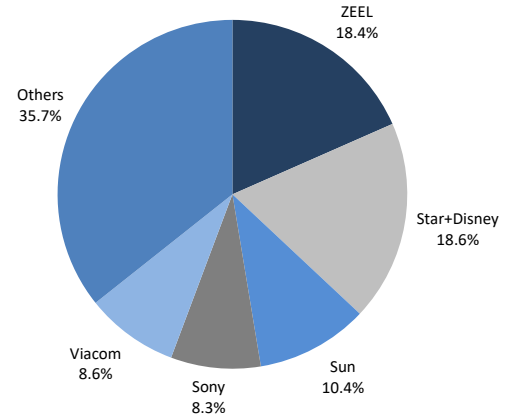
Source: Company, Anand Rathi Research

Fig 10 – Zee viewership market share (quarterly trends)



Source: Company, Anand Rathi Research

Fig 11 – Network share of broadcasters in FY20



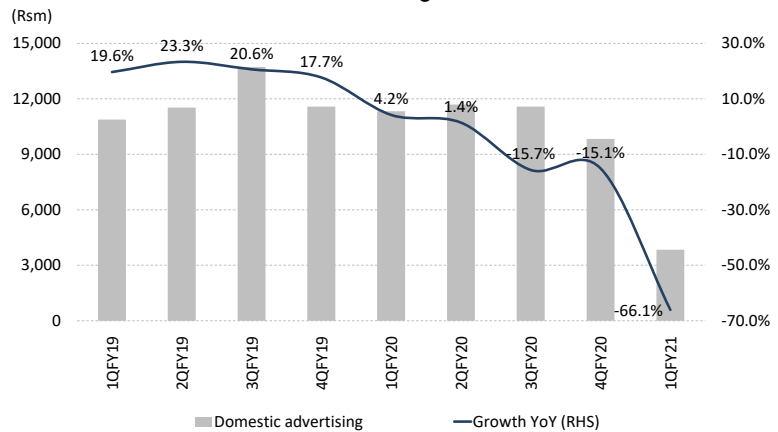
Source: Company

Notes: Network share excludes news and sports channels

Domestic ad revenue (~95% of total ad revenue) fell 7% in FY20. Zee’s domestic advertising revenues for the year slipped 7% largely due to the macro-economic slowdown, fall in FTA revenue and loss of viewership in certain markets. Private consumption growth in the country was tepid in FY20, which compelled marketers to reduce spending on advertising.

Besides, in Mar’19, Zee had pulled out from DD FreeDish two of its popular FTA channels (Zee Anmol and Zee Anmol Cinema) and changed them to “pay”. Due to this, viewership of these two channels dropped markedly and the overall share of Zee Entertainment dropped to 18.4% in FY20, from 19.7% in FY19. Excluding the share of these two channels, however, its network share grew 170bps in FY20, driven by the strong performance of Hindi movie channels and several regional channels.

Fig 12 – Growth trend - domestic advertising

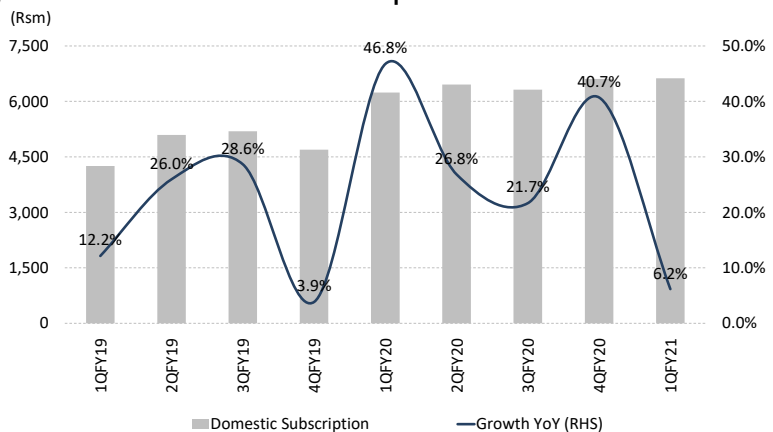


Source: Company, Anand Rathi Research

FY20 domestic subscription revenue (80.7% of total subscription revenue) grew 33%. In FY20, domestic subscription revenues grew 33% due to better monetisation of TV viewership on the implementation of NTO and on an increase in the number of Zee 5’s subscribers. Over the past decade, the proportion of the Zee Television network viewership has almost doubled from 11% to ~19%. Subscription revenue, however, did not grow commensurately due to past pricing.

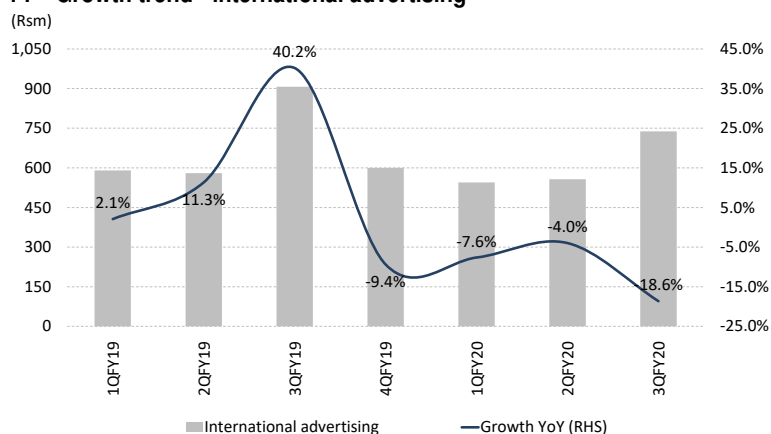
The implementation of NTO gave consumers the flexibility to choose and pay for content they wanted, and allowed broadcasters to decide on pricing of their content. NTO has given the company an opportunity to monetise these strong viewership gains, especially in southern markets. This resulted in industry-leading growth in subscription revenues for ZEEL during the year. Besides, Zee 5 subscription revenue grew on the 80+ original shows/movies released during the year and partnerships with others across the digital eco-system.

Fig 13 – Growth trend - domestic subscriptions



Source: Company, Anand Rathi Research

Regulatory challenges in certain markets hit international market (9% of overall revenue). International revenues declined 10% y/y as the company has been suffering losses in West Asia (the Mid-East) and the UK, and expects to shut from FY21 its subscription business, which would be available only through Zee 5 in these markets.

Fig 14 – Growth trend - international advertising

Source: Company, Anand Rathi Research

Other business verticals (~6.9% of revenue). Zee's other businesses slipped ~4.3% y/y in FY20. In the past few years Zee has invested in and scaled up its new businesses: digital, movies, music labels and live entertainment. These are at various stages of development and have different investment needs.

Zee 5 MAU (monthly active user) base had modest y/y growth. That was accomplished, however, with less marketing expenditure on user acquisition, highlighting growth in its organic user base. Also, Zee 5 reported a global DAU (daily active user) base of 6m with a watch time of 136 minutes per viewer during the month. Zee 5 established itself as the biggest producer of original digital content in India with 80+ shows/movies released during the year.

Zee Studios is strengthening its pipeline of in-house projects while venturing into producing content for digital platforms. During the year, its revenue plunged 58.6% y/y to Rs1,241m. Zee Studios co-produced/distributed 14 movies during the year, in Hindi, Marathi, Tamil and Punjabi. The movie business revenue declined as movies released in FY20 could not match the success of movies released the previous year.

During the year, the company announced plans to scale up the other digital business, SugarBox (Margo Technologies). However, Covid-19 stretched investment timelines. Clarity will emerge toward end-FY21.

Fig 15 – Movie business review

13 movies released in FY19	14 movies released in FY20
Hindi	Hindi
Permanu, Dhadak, Beyond the Clouds, Paltan, Manikarnika, Kesari, Love Sonia	Good Newwz, Tashkent Files, Article 15, Pehlwaan, Pal Pal Dil ke Paas, Hotel Mumbai, Hacked, Bhoot
Marathi	Marathi
Anandi Gopal, Naal, Nude, Pushpak Viman, Aa Bb Kk	Rampat, Khari Biscuit, Dhurala
Punjabi	Punjabi
Kala Shah Kala	Surkhi Bindi
	Tamil
	Nerkonda Paarvai
	Haryanvi
	Chhoriyan Chhoron se Kam Nahi Hoti

Source: Company, Anand Rathi Research

A large part of the company’s investments in new businesses would go toward its digital strategy. Meanwhile, investment in its domestic broadcast business will be limited on the launch of four regional channels during the year. Zee Studios business largely works on a rolling working-capital basis. Hence, we don’t see the need for further significant investments. Zee Music, after relentlessly acquiring titles in the last five years, has passed its investment phase.

Fig 16 – Music business review - key highlights

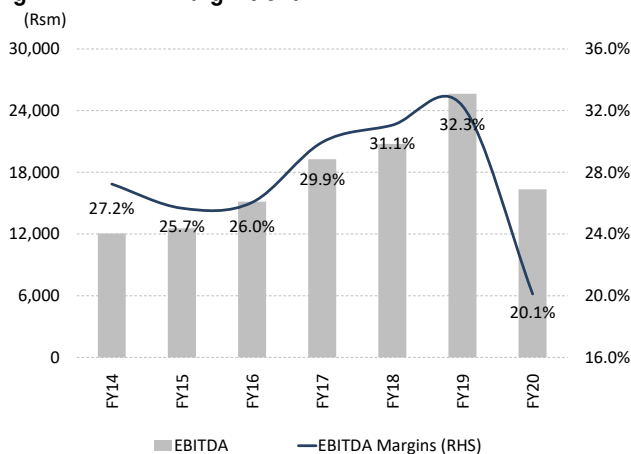
- ✚ With more than 55m subscribers (~30% y/y growth), ZMC is the second-most subscribed Indian music channel on YouTube, generating ~2.5bn video views a month
- ✚ In FY20, ZMC acquired rights to more than 193 movies’ music (67 in Hindi, 126 in regional languages) and more than 850 non-film singles
- ✚ Since its 2014 launch, it has established itself as one of the top music labels in India, publishing more than 1,000 songs a year. ZMC has acquired almost 50% of new Bollywood music released in the last few years and simultaneously expanded its presence in regional markets
- ✚ The label’s catalogue now consists of over 7,000 songs in Hindi and regional languages. ZMC has been scaling up production of non-film music, offered under the brand ‘Zee Music Originals’. Several of these go on to become superhits

Source: Company, Anand Rathi Research

FY20 EBITDA margin fell to 20.1%, from 32.3% in FY19. The EBITDA margin contracted to 20.1% in FY20, from 32.3% in FY19. Higher content investments in digital and in its broadcast businesses (programming cost rose 25.9% y/y) during the year, pushed up Zee Entertainment’s costs. The operating-cost-to-revenue also went up due to subdued revenue growth.

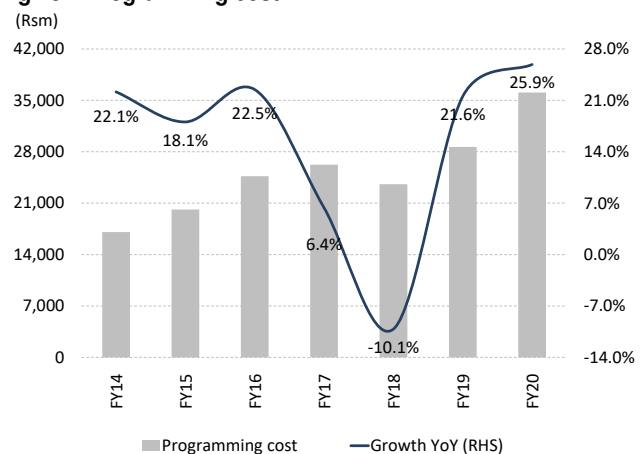
During the year, the company has taken into the profit and loss account (under operating costs) an accelerated content amortisation charge of Rs2.6bn. Also, Rs3.4bn, including Rs1.2bn from a related-party distributor, has been provided for the balances related to advertisements, subscriptions and other receivables where recovery has turned doubtful due to the Covid’19-triggered uncertainties. Excluding one-offs, the EBITDA and EBITDA margin for the year were Rs22.4bn and 27.5%.

Fig 17 – EBITDA-margin trend

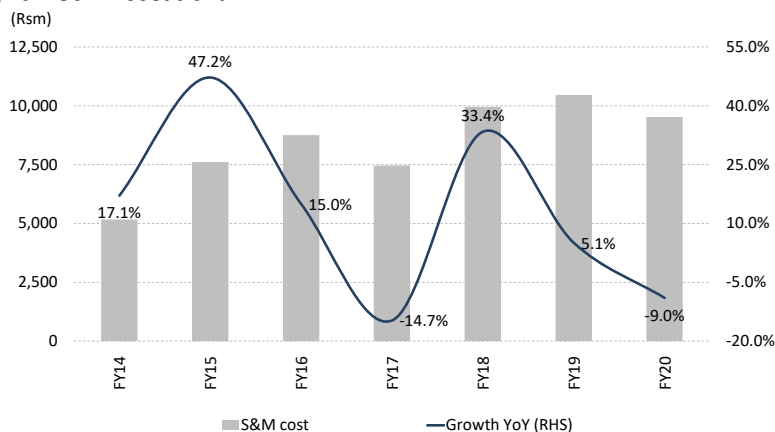


Source: Company, Anand Rathi Research

Fig 18 – Programming cost



Source: Company, Anand Rathi Research

Fig 19 – S&M - cost trend

Source: Company, Anand Rathi Research

During the year, of the CSR budget (Rs880.9m, incl. unutilized CSR of Rs394.8m carried forward from the previous year), the company contributed Rs0.72m towards various CSR projects. On 31st Mar'20, Rs880.18m was unutilized due to non-availability of suitable CSR projects. Subsequently, (from 1st Apr'20 to 30th Jun'20, the company contributed Rs139.9m for various programmes to combat the global Covid'19-caused pandemic.

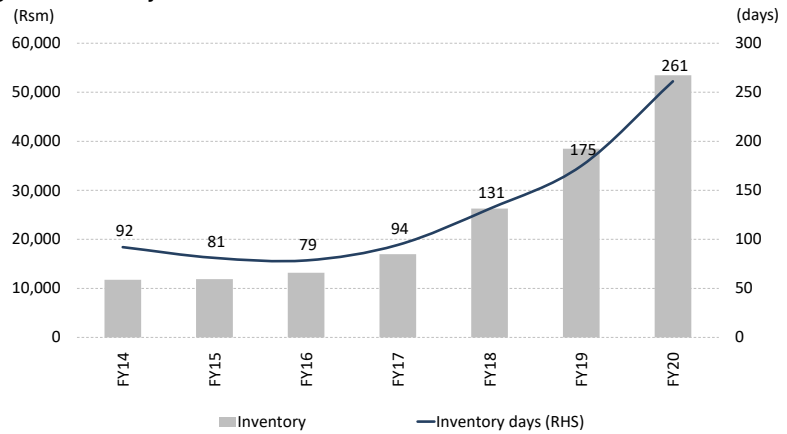
Updates on balance sheet, cash flow

Cash & cash equivalents; debt at end-FY20. On 31st Mar'20, the company had cash & equivalents of Rs7.35bn (down 39.9% y/y) and Rs2.77bn in Treasury investments (down 67.7% y/y). During the year, the company decided to sell its overseas investment and appointed a consultant to identify a buyer. While these investments had been deployed in high-yield assets, the impact of the pandemic markedly contracted the value of the underlying assets. Consolidated long-term debt shrank to Rs5.95bn, from Rs11.11bn on 31st Mar'19. Overall debt declined on part redemption of preference shares.

Excl. income tax paid, FY20 cash flow from operations down 47.3% y/y. Higher working capital required pulled down cash flow from operations (excl. income tax paid) by Rs5.6bn. Including that, net cash-flow from operations rose 85% y/y to Rs2.5bn as lower tax outflow from the reduced corporate tax rate led to better cash generation than the previous year.

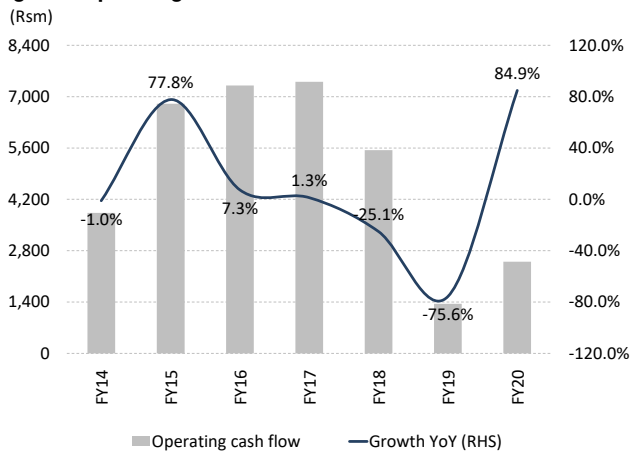
Investment in movie satellite rights rose, increasing inventory by Rs14.83bn. Continued content investment and a sharper focus on satellite movie rights led to a 38.9% rise in inventory, to Rs53.48bn. Consequently, inventory days lengthened to 261, from 175 in FY19. Of the inventory, 62% is expected to be recovered after 12 months (vs. 66% a year ago), highlighting Zee's solid ramp-up in its future content slate. We expect peak investments in inventory are behind and working-capital intensity will start lessening from FY21. Further, capex was lower, at Rs1.82bn vs. Rs2.8bn in FY19.

Fig 20 – Inventory trend



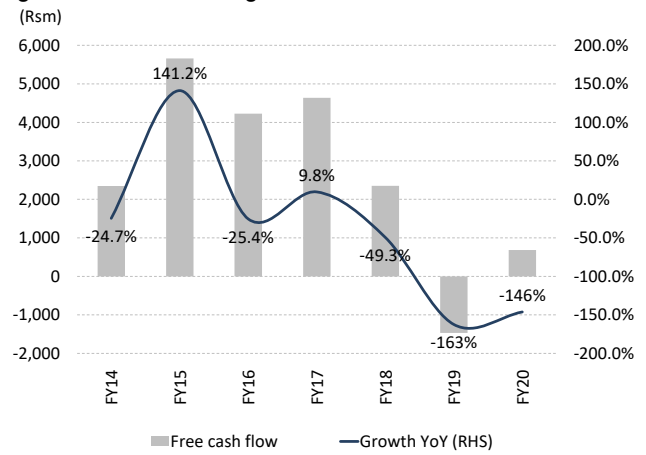
Source: Company, Anand Rathi Research

Fig 21 – Operating cash-flow trend



Source: Company, Anand Rathi Research

Fig 22 – Free cash-flow generation trend



Source: Company, Anand Rathi Research

Delay in recovering receivables from related parties, which continue high. Zee Entertainment’s trade receivables rose by Rs289m in FY20 to Rs20.85bn (receivables days lengthened by 10 to 94). On 31st Mar’20, the company had trade receivables of Rs8.15bn from two strategic customers (Dish TV and Siti Networks), including amounts long overdue.

It recorded an expected credit loss of Rs1.18bn due to the potential impact of Covid-19 and Rs0.38bn toward the time value of money on account of delayed collections. It said it has received payment plans from them and the receivables position was expected to come down. Given the weak credit profile of these counter-parties, the collection risk factor is high.

Fixed assets and goodwill details

Fig 23 – Gross fixed assets (Rs m)

Tangible	At end-FY19	Additions	Re-classified on account of Ind AS 116	Transfer of investment property	Disposals	Translation	Held for sale	At end-FY20
Buildings	1,386	588	-	68	-	-	198	1,844
Plant & Machinery	5,508	528	-	-	114	127	29	6,020
Furniture & Fittings	486	52	-	-	7	6	17	520
Vehicles	280	10	-	-	18	3	-	275
Equipment	985	127	-	-	8	3	-	1,107
Computers	1,499	209	-	-	36	6	6	1,672
Aircraft	773	-	-	-	-	-	773	-
Leasehold Improvements	999	277	-	-	10	-	-	1,266
Right to use assets	-	180	1,123	-	-	-	-	1,303
Total	11,916	1,971	1,123	68	193	145	1,023	14,007

Source: Company, Anand Rathi Research

Fig 24 – Goodwill & other Intangible assets

	At end-FY19	Additions	Transfer on acquisition	Disposals	Translation	Held for sale	At end-FY20
Goodwill	5,470	-	-	-	4	49	5,425
Trademark	322	-	-	-	-	-	322
Customer list & websites	1,081	-	-	-	-	-	1,081
Software	1,864	932	-	4	103	-	2,895
Channels	172	57	-	-	-	-	229
Total	8,909	989	-	4	107	49	9,952

Source: Company, Anand Rathi Research

Other important highlights from the annual report

Contingent liabilities

With the sale of the sports business, corporate guarantees had been reduced to nil in FY18 but have risen in FY19 and FY20 as the company had invested in NCDs (of ~Rs445m) issued by Zee Learn, which would be redeemed over 18 months. Also, it provided loans to group companies. Disputed direct taxes have also come down.

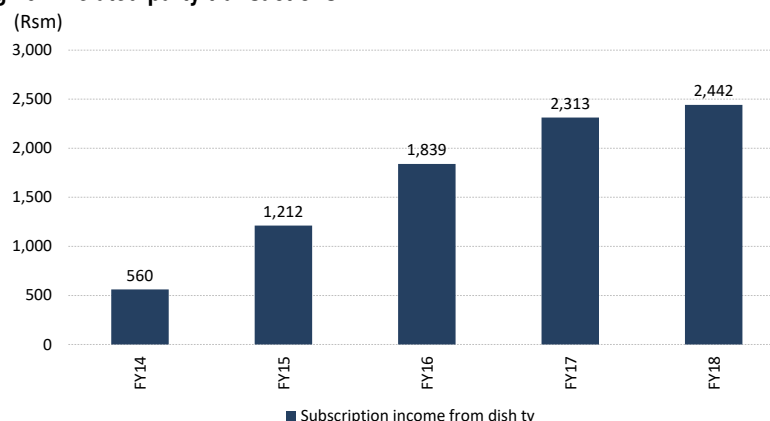
Fig 25 – Contingent liabilities (Rs m)

	FY16	FY17	FY18	FY19	FY20
Corporate guarantees					
For subsidiaries	21,374	4,018	0	1,137	1,637
For other related parties	800	1,039	1,037	0	336
Disputed indirect taxes	497	495	536	585	585
Disputed direct taxes	5,985	5,431	4,746	3,352	676
Claims against the Group not acknowledged as debts	948	611	650	440	317
Legal cases against the Group	Not ascertainable	Not ascertainable	Not ascertainable	Not ascertainable	Not ascertainable

Source: Company, Anand Rathi Research

Related-party transactions

Subscription income from Dish TV to Zee increased to Rs4.84bn in FY19 (vs. Rs2.4bn in FY18). In the FY20 annual report, the company did not disclose subscription income from Dish TV, as the latter is not a related party any more. Our estimates suggest this should be Rs5bn+ in FY20 (~20% of the domestic subscription income)

Fig 26 – Related-party transactions

Source: Company, Anand Rathi Research

Updates on subsidiaries

In FY20, the company had eight direct and indirect domestic subsidiaries and twenty overseas subsidiaries, one associate company and one joint venture.

During the year the company

- bought the balance 26% stake in Zee Network Distribution (the erstwhile Zee-Turner) from Turner International Pvt. Ltd., making ZND a wholly-owned subsidiary on 9th Aug'19
- On 31st Mar'20, Eves Multimedia, Inc., the overseas subsidiary of Essel Vision Productions, a wholly-owned subsidiary, was dissolved and wound up.
- Subsequent to the financial year, Zee TV USA, Inc., the overseas subsidiary of Zee Multimedia Worldwide (Mauritius), a wholly-owned subsidiary, was dissolved and wound up, effective 1st May'20.

Fig 27 – Financials of key Indian subsidiaries

Particulars (Rs m)	Date of Acquisition	Holding (%)	FY19			FY20		
			Revenue	PBT	PAT	Revenue	PBT	PAT
Zee Turner	31-Dec-01	74	0	-1	-1	0	26	31
Essel Vision Productions	10-Sep-10	100	5,130	100	79	4,673	1,568	1,553
ZEE Digital Convergence	23-Sep-04	100	17	-13	-13	11	-1	-1
Zee Unimedia	01-Apr-16	100	0	-5	-6	0	-3	-3
India Webportal Pvt. Ltd.	10-Dec-10	100	0	-3	-3	0	-1	-1

Source: Company, Anand Rathi Research

Fig 28 – Financials of key international subsidiaries

Particulars (Rs m)	Date of Acquisition	Holdings (%)	FY19			FY20		
			Revenue	PBT	PAT	Revenue	PBT	PAT
Asia TV	30-Sep-99	100	1,451	94	68	1,694	110	84
Asia Multimedia Distribution, Inc.	26-May-14	100	247	24	17	258	23	17
Zee TV South Africa (Proprietary)	30-Sep-99	100	277	14	14	299	46	46
Asia TV, USA	09-Nov-15	100	2,139	68	68	1,734	-1,602	-1,280
ATL Media	31-Mar-00	100	2,735	-57	751	3,722	-4,112	-4,103
Taj TV	22-Nov-06	100	0	-539	-550	0	37	34
Asia Today	19-Jan-06	100	2,657	-564	-568	2,725	-1,294	-1,289
Zee Entertainment Middle East FZ-LLC	04-Sep-05	100	1,839	430	430	1,425	160	160

Source: Company, Anand Rathi Research

Updates on corporate governance

In FY20, the Board comprised eight directors: one executive, three non-executives, four independent. In FY20, after the stake sale by the promoter, a few independent directors resigned, offering as the reason concerns related to the balance sheet. The company then inducted on the Board members with expertise in law, media and finance. Another material development was the resignation of Subhash Chandra and the appointment of R Gopalan, an independent director as Chairman of the Board.

Fig 29 – Board of Directors – details

Name	Designation	Committee membership	Remuneration (Rs m)	% increase in remuneration	Ratio to the median
FY19					
Subhash Chandra	Non-executive chairman	None	3	9	2.80:1
Subodh Kumar	Non-executive director	Nomination & remuneration, Risk management & CSR	3	9	2.80:1
Punit Goenka	MD and CEO	Risk management, Stakeholder relationships, CSR & Finance sub-committee	82.95	9	77.5:1
Ashok Kurien	Non-executive director	Audit, Stakeholder relationships & Finance sub-committee	3	9	2.80:1
Manish Chokhani	Independent director	Audit	3	9	2.80:1
Mrs Neharika Vohra	Independent director	Nomination & remuneration	3	9	2.80:1
Sunil Sharma	Independent director	Audit & CSR	3	9	2.80:1
Adesh Kumar Gupta	Independent director	Audit, Nomination & remuneration and Risk management	3	9	2.80:1
FY20					
Subhash Chandra	Chairman emeritus	None	4.77	59	4.15:1
R Gopalan	Chairman	Audit	2.44	NA	2.12:1
Punit Goenka	MD and CEO	Risk management, Stakeholder relationships, CSR & Finance sub-committee	90.018	9	78.42:1
Ashok Kurien	Non-executive director	Audit, Stakeholder relationships, CSR and Nomination & remuneration	5.54	85	4.82:1
Manish Chokhani	Independent director	Audit, Nomination & remuneration and Risk management	5.54	85	4.82:1
Piyush Pandey	Independent director	Stakeholder relationships, CSR and Nomination & remuneration	0.1	NA	0.09:1
Mrs Alicia Yi	Independent director	Nomination & remuneration	NA	NA	NA
Adesh Kumar Gupta	Independent director	Audit & Risk management	5.54	85	4.82:1

Source: Company, Anand Rathi Research

Promoter pledges

After the stake sale, the promoters' stake has shrunk to 4.77% (~16.4% pledged) from 38.2% in FY19 (~66% pledged)

Fig 30 – Promoters' pledges have increased

Shareholding	in FY17		in FY18		in FY19		in FY20	
	%	Pledged % pt. of holding	%	Pledged % pt. of holding	%	Pledged % pt. of holding	%	Pledged % pt. of holding
Essel Infraprojects	0	0	0	0	0	0	0	0
Sprit Infrapower & Multiventures Pvt. Ltd.	0	0	0	0	0	0	0	0
Cyquator Media Services Pvt. Ltd.	25.14	16.94	25.14	21.87	22.8	25.28	0.84	0.64
Essel Media Ventures	10.71	0	10.71	0	10.71	0	3.45	0.14
Essel Holdings	4.83	0	3.31	0	0.18	0	0.18	0
Essel International	2.39	0	2.39	0	1.47	0	0.14	0
Essel Corporate	0	0	0.07	0	3.04	0	0.16	0
Total	43.07	16.94	41.62	21.87	38.2	25.28	4.77	0.78

Source: Company, Anand Rathi Research

Factsheet

Fig 31 – Factsheet

Year-end: Mar	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21
Revenue split (%)					
Advertisements	59	58	60	53	32
Subscriptions	35	34	35	38	57
Others	6	8	5	9	11
Revenue split (₹ m)					
Advertisements	11,867	12,247	12,308	10,389	4,211
Subscriptions	7,088	7,235	7,137	7,414	7,443
Others	1,126	1,739	1,042	1,708	1,466
Y/Y growth (%)					
Advertisements	4	1	-16	-15	-65
Subscriptions	37	19	15	31	5
Others	5	11	22	-28	30
Advertising revenue split (%)					
Domestic revenues	95	95	94	95	91
International revenues	5	5	6	5	9
Subscription revenue split (%)					
Domestic revenues	88	89	89	89	89
International revenues	12	11	11	11	11

Source: Company, Anand Rathi Research

Valuations

Its leading status in Hindi GEC and various sub-segments, specifically, regional content, gives Zee a unique position in the media sector. Also, it obtains a scarcity premium as the other two competitors are unavailable to investors in the secondary market. Sun TV is the only comparable.

We believe that the media eco-system is evolving in favour of content companies and, therefore, the ability to consistently procure and build popular content would be even more valuable in future. Also, advertising expenditure (translating for Zee into revenue) is expected to rise due to the better economic environment in H2 FY21 and FY22.

We now value Zee at 10x FY22e EV/EBITDA and retain our Buy rating, with an unchanged target price of Rs220.

Risk

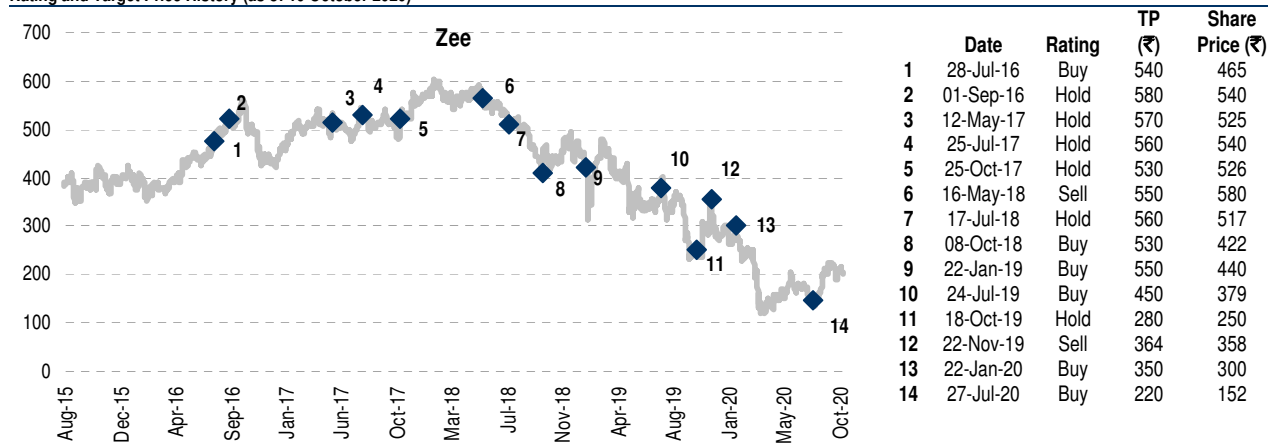
- Any loss in content rating in the flagship/leadership genres.
- Keener competition on the OTT front.
- Weaker-than-expected ad/margin recovery.

Appendix

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