

July 6, 2018

Buy

Sun TV Network

Industry: Media | Industry View: Positive



Company Update

The sun is rising again...

Sun TV is in a phase of robust earnings growth after a long period of political uncertainty. Although the company has been losing market share in all of its geographies, we have off late seen resilience in its Advertising business on the back of inventory utilization, low base and rapid shift to commissioned model from slot sale model. Subscription revenues are now showing a good traction driven by the digitization wave covering almost 50% of Tamil Nadu (TN) although there has been delay in it. Also the challenging political environment for proliferation of digitization which was prevalent till a year back has been eased with the demise of Jayalalithaa and Sun TV having signed a deal with Arasu cable. With the downward revision in the franchise fees by the BCCI and good performance by their team, the IPL business is expected to post spectacular results from FY19E onwards. Launch of new regional channel, increase in film investment are additional levers for topline to get an incremental push. We believe that with a topline and bottomline CAGR of 17% each in FY17-20E period, the company should be able to narrow down its discount with its peer Zee Entertainment. We maintain BUY rating on the stock with a target price of ₹1,032, valued at 25x times on FY20E earnings, while the stock is trading at 19.4x at CMP of ₹ 772.

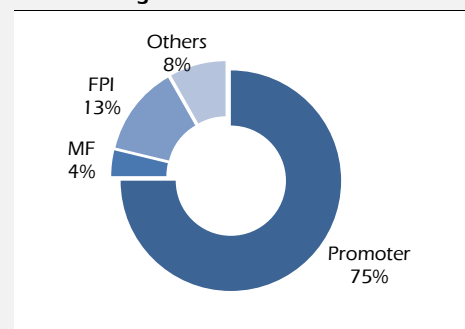
Advertising revenues to accelerate further on various positive drivers-

- Revenue from advertising and broadcast fee grew 23% YoY in Q4FY18 to ₹ 3.6bn on the back of yield expansion/inventory utilization, low base and higher ad volumes. Sun TV witnessed growth across markets, with its key market TN (60% of ad revenue and ~50% viewership market share) growing in sync with the overall ad growth.
- Management attributed the recent viewership share losses across markets to IPL feeds in regional languages and is confident of regaining share with fresh programming post the cricketing mega-event which is expected to show its impact from Q1 FY19. In Tamil Nadu, the launch of new channel Colors Tamil (5-6% market share) has led to little market share loss over there. Deep inroads by Star (Karnataka, AP, Kerala and TN) and Zee (Karnataka, AP and TN) have also led to market share loss for Sun. With focus on holding on to its core audience base, the company is strategically planning to launch a number of high-value fiction properties across markets to improve its share.
- Sun TV will continue with its shift to commissioned programming in TN, with one new programme in primetime and two in non-primetime slots during the quarter under its new model. In all, 20% of shows are based on the commissioned model. This will boost ad revenue growth (and content costs). In the near future, two more shows will be added on the commissioned model. Over time, Sun expects 50:50 split between the commissioned and slot-sale models in prime slots.
- To counter competition, Sun management plans to launch a second Tamil GEC with differentiated content in FY2019E. It will also foray into a new regional market (mostly Bangla or Marathi) for a capex of ₹ 1-1.3bn. It is encouraging that the company is focused on protecting market share; execution of this strategy will be key to success (especially in Bangla/Marathi GEC given Sun's inexperience outside

Stock Data

Current Market Price (₹)	772
12 month Price Target (₹)	1032
Potential upside (%)	34
FV (₹)	5
Reuters	SUNTV BO
Bloomberg	SUTV. IN
Market Cap (₹ bn)	314
52-Week Range (₹)	1,098 / 652

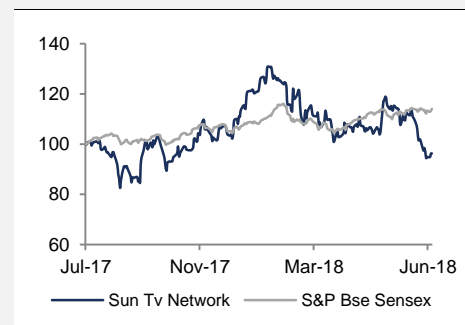
Shareholding Pattern



Fiscal YE

	FY17	FY18	FY19E	FY20E
Revenues (₹ bn)	26.5	29.6	35.3	42.2
EBITDA margins (%)	66.9	67.6	69.1	70.0
PAT margins (%)	37.9	37.6	38.9	38.4
EPS (₹)	25.6	28.5	35.0	41.3
EPS growth (%)	14.7	11.1	23.2	18.3
P/E (x)	31.2	28.1	22.9	19.4
P/B(x)	7.8	6.7	5.8	5.1
EV/EBITDA (x)	17.2	15.4	12.5	10.1
ROCE(%)	33.4	32.5	34.9	37.3
ROE (%)	24.9	23.7	25.5	26.5
Dividend yield (%)	39.3	40.0	42.0	45.0

Relative Price Performance



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south). Separately, Sun has committed ₹ 2.5-3 bn to produce two movies (one with Rajinikath by Diwali 2018 and one with Vijay by Q4 FY19/Q2 FY20) over the next 12-15 months. Rising multiplex penetration has improved the outlook for film production, prompting the company to re-enter the business. The thesis is credible but we are aware that big budget films have their own share of risks. We need to gauge this case closely.

- Sun saw a flurry of downloads of SunNXT app initially, but some customers have moved away. Sun will not produce digital-only content in the near term. The south Indian markets are likely to be predominantly TV-driven in the medium term; hence they will not invest heavily in OTT platform, while Sun is mulling to charge the existing SunNxt OTT platform. Sun continues to explore partnerships with telcos and other channels. This may add a new stream of revenues to the top line.
- Management reiterated that next fiscal ad growth would be in double digits and they appeared very confident of maintaining or even improving market-share in Tamil Nadu (TN)

Subscription revenues to expand on TN digitization wave moving at a good pace

- Sun's subscription revenues have grown by 23% in Q4 as digitization wave has proliferated in TN with market conditions easing over there. DTH and cable subscription revenue rose 19.9% and 46.5% YoY, respectively on catch-up revenues from Arasu cable. The management indicated that Arasu cable is taking some serious steps on the ground to implement digitization and expects a large part of digitization in TN to be completed by the end of CY18.
- With the deal between Arasu cable and Sun TV finalised for digital subscription pay-out, we anticipate a strong growth in subscription revenues over the medium term. Management indicated that digitization is progressing at a good pace in Tamil Nadu and should be completed over the next 12 months. A higher preference towards DTH should aid in Sun TV realizing a higher ARPU.
- Digitization has raised digital cable HHs in TN, from 1m to 4.5m as at end-March. Another 9-10m will be largely digitized by end-CY18; further, while there are 5m paid DTH HHs. With more than ~50% (~ 10 mn) of the 22 mn households yet to be digitized, the potential in non-Tamil Nadu southern markets is equally exciting. We expect rapid conversion of analog HHs to digital ones as MIB begins to pressurize Arasu Cable to do so.
- With digital cable players paying ₹~25 per subscriber per month to Sun TV, we believe this conversion could add at-least ₹.4bn of incremental revenues. The digital deal with Arasu will raise Sun's ARPU to ₹ 30-60 from current ₹2 thus providing a huge upside for Sun's subscription business. Furthermore, rise in Arasu's ARPU (double from current Rs70) has also increase tariff headroom for DTH players, due to which Sun's topline will benefit from this as well.
- Political winds are not as adverse as they were earlier, as the ruling AIADMK party is in its second term and no longer as strong as it was during Jayalalithaa's time.

IPL to be a game changer-

IPL contribution to PAT increasing sharply in FY19, as expected, is a tailwind. Q1 FY19 should be a substantially strong quarter, considering ~Rs900m increase in IPL revenue YoY (based on the new TV rights deal between BCCI and Star) and IPL franchisee cost set at 20% revenue share (~₹ 480m) vs. ₹ 855m fixed-fee earlier. This would lead to a favorable performance at EBITDA level itself. With team performance having improved in FY19, the company stands a very good chance to post a spectacular show on this business division.

Outlook and Valuation

Sun has been posting strong set of numbers since last two quarters. On the advertising business, despite loss of market shares across board, inventory utilization, improvement in yields and low base led to robust growth. Subscription revenues are on an up-move on TN digitization wave. Going forward, these two businesses along with their levers are believed to provide impetus to the financials of Sun. Additionally, IPL turnaround with higher revenues and lower costs will aid margin performance. Higher ARPUs at subscription business with Arasu issue settling will lead to mammoth incremental revenues and profitability. In order to tackle competition from Zee and Star, entry into new geographies, launch of new Tamil GEC, differentiated content and higher emphasis on commission based model may lead to better market share revival and topline growth. Though these may lead to higher content costs, operating leverage may lead to higher margins. We remain sanguine on the company and expect strong double digit growth in bottomline in FY19-20E. We maintain BUY rating on the stock.

Risks and Concerns

- Competition from Star, Zee and Colors intensifying may add extra pressure on market share growth, thus limiting prospects for further topline growth
- Uncertainty regarding success of new channel launch in non South markets.
- Slower than expected spread out of digitization in TN market
- Increasing movie capex may pressurize the bottomline and at the same time success of big movies remains a risk.
- Political environment becoming difficult may limit subscription revenues growth.
- Entry of Reliance Industries into broadband business may lead to some threat to Sun's DTH business (25% of topline in FY18).

Sun TV Market shares

(%)	Q4 FY16	Q1 FY17	Q2 FY17	Q3 FY17	Q4 FY17	Q1 FY18	Q2 FY18	Q3 FY18	Q4 FY18	Q1 FY19*
Regional GEC (All day)										
Sun TV	69.1	67.2	62.8	64.2	63	59.5	51	54.3	48.9	46.2
Gemini	20.4	21.8	28.2	29.6	30	28.2	24.8	23.6	23.9	20.8
Udaya	18.4	18.3	18	11.7	12.9	14.2	16.7	16.1	17.6	18.1
Surya	8.4	9.4	15.5	13.9	13.4	13.6	17.3	21.3	16.4	15.3
Primetime										
Sun TV	71.6	70.3	66.8	69.1	69.4	64.9	51.8	55.4	49.5	46.0
Gemini	10.4	11.9	21.3	24.6	24	20.2	17.8	17.8	17.6	13.6
Udaya	15.6	16.7	15.8	5.4	5.8	10.1	15	16.1	12.6	13.4
Surya	2.6	4.3	12.2	9.2	8.5	8.2	13.3	17	11.6	8.5
Movies & Music										
Udaya Comedy	10.4	10.3	9.6	12.1	10.9	13.2	14.1	13.8	14.3	15.5
Udaya Movies	37.5	38.3	33.6	30.1	31	34.6	36.6	37.1	37.4	32.7
Sun Life	10.5	8.9	9.5	10.1	10.1	11.2	10.5	10.9	13.4	13.5
Sun Music	16.2	16.4	16.3	17.7	16.3	15.4	13.5	12.7	11.7	12.5
Gemini Life	8.4	8	7.4	7.6	7.9	9.6	9.3	9.9	8.2	6.4
Gemini Movies	38.7	39.3	33	34.8	32.2	27.3	26.6	24.8	25.7	21.7
Gemini Music	13.1	11.8	10	11	10.8	10.9	11.5	12.3	12.1	9.8
News										
Udaya News	4.1	4.7	5.2	4.9	4.7	5.2	4.7	5.5	4.1	2.7
Gemini News	0.7	0.6	0.5	0.5	0.6	0.7	0.8	0.9	1.0	1.0

* OTD

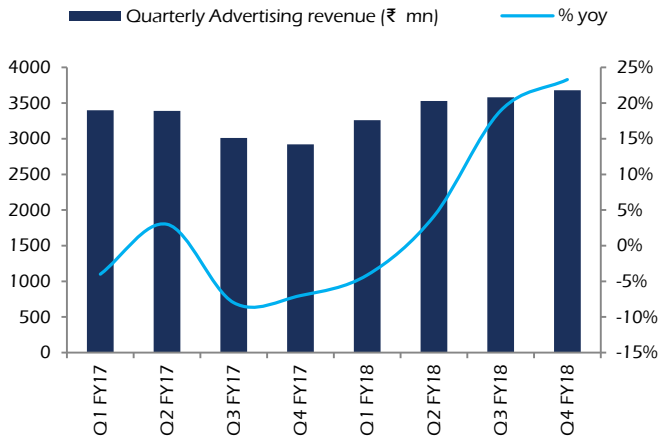
Source: BARC, LKP Research

Revenue breakup

(₹ mn)	FY 14	FY 15	FY 16	FY 17	FY 18	FY 19E	FY 20E
Advertising Income	11,944	12,507	13,207	12,720	13,950	15,624	17,811
% yoy		4.7%	5.6%	-3.7%	9.7%	12.0%	14.0%
Domestic Subscription Income	6,419	7,742	9,742	9,619	11,211	13,601	16,771
% yoy		20.6%	25.8%	-1.3%	16.6%	21.3%	23.3%
O/w Analog plus digital revenues	1,999	2,099	2,225	3,049	3,830	4,596	5,515
% yoy		5.0%	6.0%	37.0%	25.6%	20.0%	20.0%
O/W DTH revenues	4,420	5,643	7,517	6,570	7,381	9,005	11,256
% yoy		27.7%	33.2%	-12.6%	12.3%	22.0%	25.0%
Broadcast Fees	1,410	1,438	1,510	-	-	-	-
% yoy		2.0%	5.0%	-	-	-	-
Program Licensing Income	1,327	1,659	2,157	1,540	1,694	1,779	1,868
% yoy		25.0%	30.0%	-28.6%	10.0%	5.0%	5.0%
Movies and others	250	370	475	198	310	930	1,581
% yoy		48.0%	28.4%	-58.3%	56.6%	200.0%	70.0%
IPL	1,055	1,002	963	1,490	1,468	2,202	2,863
% yoy		-5.0%	-3.9%	54.7%	-1.5%	50.0%	30.0%
Radio	1,353	1,652	1,920	891	998	1,148	1,354
% yoy		22.1%	16.2%	-53.6%	12.0%	15.0%	18.0%
Total consolidated revenues	23,758	26,370	29,974	26,458	29,631	35,283	42,248
% yoy		11.0%	13.7%	-11.7%	12.0%	19.1%	19.7%

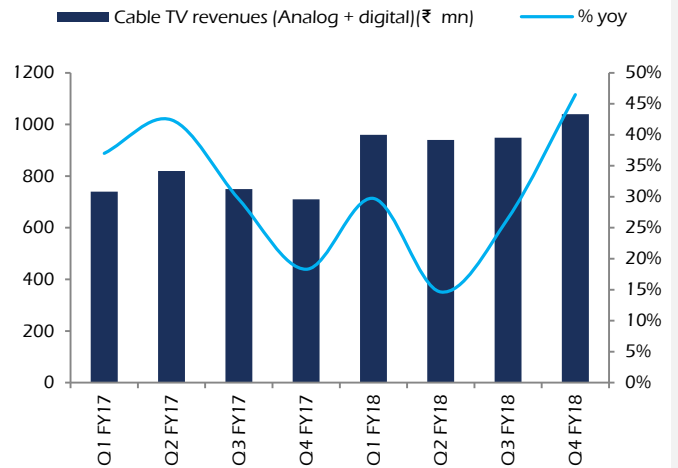
Source: Company, LKP Research

Quarterly Advertising revenue trend



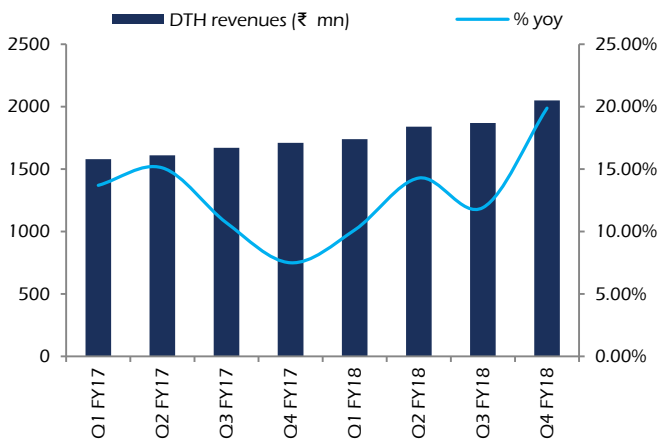
Source: Company, LKP Research

Cable TV growth (Analog + digital)



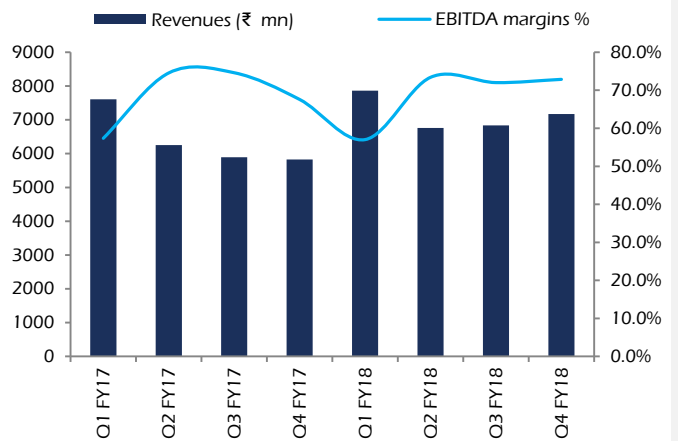
Source: Company, LKP Research

DTH revenues



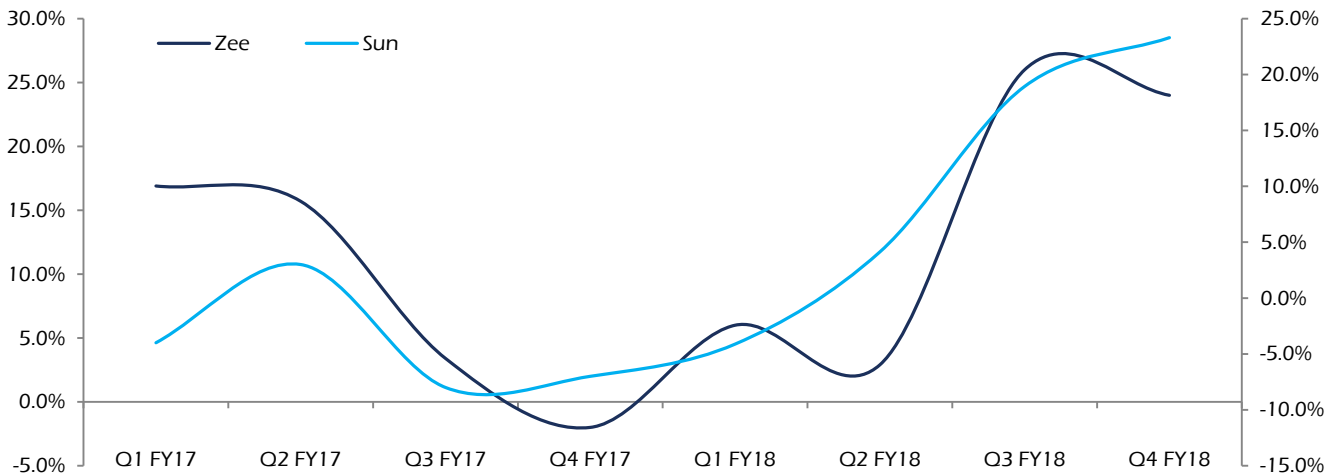
Source: Company, LKP Research

Revenues v/s EBITDA Margins



Source: Company, LKP Research

Quarterly advertising revenues comparison (Zee v/s Sun)



Source: Company, LKP Research

Financials

Income statement

YE Mar (₹.mn)	FY 17	FY 18	FY 19E	FY 20E
Total Revenues	26,458	29,631	35,283	42,248
Cost of revenue	3,193	3,883	4,305	5,070
Employee Cost	2,735	3,145	3,599	4,225
Other Exp	2,831	2,564	2,999	3,380
EBITDA	17,699	20,039	24,381	29,574
EBITDA Margin(%)	66.9%	67.6%	69.1%	70.0%
Other income	1,538	1,423	1,390	1,350
Depreciation	4,005	4,500	5,292	6,337
Interest	10	11	12	12
PBT	15,222	16,951	20,466	24,574
PBT Margin(%)	57.5%	57.2%	58.0%	58.2%
Tax	5,203	5,823	6,754	8,355
Adj PAT	10,020	11,128	13,712	16,219
Adj PAT Margins (%)	37.9%	37.6%	38.9%	38.4%
Exceptional items	0.0	0.0	0.0	0.0
PAT	10020	11128	13712	16219
PAT Margin (%)	37.9%	37.6%	38.9%	38.4%

Key Ratios

YE Mar	FY 17	FY 18	FY 19E	FY 20E
Per Share Data (₹)				
Adj. EPS	25.6	28.5	35.0	41.3
CEPS	35.9	40.0	48.5	57.4
BVPS	103.1	120.0	137.1	155.7
DPS	12.1	13.7	17.6	22.3
Growth Ratios (%)				
Total revenues	7.0%	12.0%	19.1%	19.7%
EBITDA	2.1%	13.2%	21.7%	21.3%
PAT	14.7%	11.1%	23.2%	18.3%
EPS Growth	14.7%	11.1%	23.2%	18.3%
Valuation Ratios (x)				
PE	31.2	28.1	22.9	19.4
P/CEPS	22.3	20.0	16.5	13.9
P/BV	7.8	6.7	5.8	5.1
EV/Sales	7.8	6.7	5.8	5.1
EV/EBITDA	17.2	15.4	12.5	10.1
Operating Ratios (Days)				
Receivable Days	106.6	131.1	120.0	110.0
Payables day	10.0	10.3	10.7	10.9
Net Debt/Equity (x)	(0.20)	(0.08)	(0.17)	(0.21)
Profitability Ratios (%)				
ROCE	33.4%	32.5%	34.9%	37.3%
ROE	24.9%	23.7%	25.5%	26.5%
Dividend payout	39.3%	40.0%	42.0%	45.0%
Dividend yield	1.5%	1.7%	2.2%	2.8%

Source: Company, LKP Research

Balance sheet

YE Mar (₹. mn)	FY 17	FY 18	FY 19E	FY 20E
EQUITY AND LIABILITIES				
Shareholder's funds				
Share capital	1,970	1,970	1,970	1,970
Reserves and surplus	38,350	44,954	51,755	59,216
Total networth	40,321	46,924	53,725	61,186
Non current liabilities				
Long term borrowings & prov	0	0	0	0
Deferred tax liabilities	556	770	870	970
Other long term liabilities	134	131	126	121
Current liabilities				
Current liabilities & provisions	935	1,007	1,247	1,528
Other current liabilities	1,872	3,926	3,867	4,051
Total equity and liabilities	43,815	52,756	59,834	67,855
ASSETS				
Net block	7,697	7,169	5,877	5,040
Capital work in progress	16	474	524	594
Long term investments	6,026	6,238	6,638	7,138
Long term loans & advances	637	291	391	591
Other non current assets	2,391	3,327	3,827	4,427
Total non current assets	21,188	21,744	21,702	22,635
Current assets				
Inventories	11	9	3	10
Trade receivables	7,726	10,639	11,600	12,732
Cash and cash bank	7,883	3,726	8,868	12,814
Investments	5,454	15,152	16,152	18,152
Short term loans and advances	971	1,043	1,103	1,163
Other current assets	585	449	399	349
Total current assets	22,627	31,012	38,132	45,221
Total Assets	43,815	52,756	59,834	67,855

Cash Flow

YE Mar (₹ mn)	FY 17	FY 18	FY 19E	FY 20E
PBT	15,222	16,951	20,466	24,574
Depreciation	3,996	4,500	5,292	6,337
Interest	10	11	12	12
Chng in working capital	52	(4,736)	(768)	(1,153)
Tax paid	(4,985)	(5,823)	(6,754)	(8,355)
Other operating activities	(1,447)	(1,144)	(1,244)	(1,344)
Cash flow from operations (a)	12,848	9,758	17,005	20,071
Capital expenditure	(1,280)	(4,429)	(4,050)	(5,570)
Chng in investments	(2,627)	(1,735)	(1,600)	(2,900)
Other investing activities	(3,150)	(133)	(596)	1,021
Cash flow from investing (b)	(7,057)	(6,298)	(6,246)	(7,449)
Free cash flow (a+b)	5,791	3,461	10,758	12,622
Inc/dec in borrowings	0	211	95	95
Dividend paid (incl. tax)	(4,743)	(5,342)	(6,911)	(8,758)
Other financing activities	0	0	0	0
Interest paid	(10)	(11)	(12)	(12)
Cash flow from financing (c)	(4,753)	(5,141)	(6,828)	(8,675)
Net chng in cash (a+b+c)	1,038	(1,681)	3,930	3,946
Closing cash & cash equiv.	6,618	4,938	8,868	12,814

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