PhillipCapital

Eros International Media Ltd (EROS IN)

Blockbuster in the making

INDIA | MEDIA | INITIATING COVERAGE

6 July 2015

EIML is a leading player in the Indian movie industry— it acquires, co-produces, and distributes Indian movies across all formats such as cinema, TV, and digital new media. EIML's business model is built around securing content through co-productions and acquisitions and monetizing this through its distribution network across multiple formats along with its existing library of over 2,000 movies. With a de-risked business model, robust movie pipeline, and extensive distribution network, EIML is all set to benefit from increased discretionary spending and rising video consumption on multiple platforms. We expect 21% earnings growth CAGR over FY15-17 and initiate coverage with a BUY rating and TP of Rs 658 (17x FY17E earnings).

Integrated studio model ensures monetization through the value chain: EIML is the only listed player in the Indian media space that operates on a vertically integrated studio model controlling content as well as distribution and exploitation across all formats globally. The company generates revenues across all phases of the movie-release cycle and it has adopted a successful multi-platform content-monetization model, ensuring revenue generation even a year after the movie's release. This makes the business model less risky vs. traditional broadcasting or multiplex businesses. Also, given its strong library content, we view EIML as one of the prime beneficiaries of rising video consumption on multiple platforms. Over the last few years, the company has successfully scaled up its library revenues (5-year CAGR of 49%) and we expect this trend to continue, which should translate into structurally higher margins and cash-flow conversion.

To benefit from structural changes in Indian movie distribution: We believe that the ecosystem for monetization of movie content is getting stronger across the value chain driven by growth in multiplexes, digitisation of Indian cable, and emergence of new digital platforms. With its unique strategy of co-producing and acquiring 65-70 movies a year, EMIL is in a good position to benefit from this structural change. Its business model of acquiring or co-producing movies rather than investing in significant in-house production capability allows EIML to simultaneously work on more than one production with key talent. This is because the producer/co-producer takes the lead on the time-intensive process of production, allowing EIML to build its movie slate more rapidly.

Strong movie pipeline to drive revenue CAGR of 20% over FY15-17: Driven by a strong slate of movie releases planned over the next couple of years, we are forecasting 20% revenue CAGR for EIML over FY15-17. For EIML, *Tanu Weds Manu Returns,* a medium-budget movie release in May has already been a blockbuster; hence, we expect the company to report robust profit numbers in Q1FY16. EIML schedule for the rest of FY16 is strengthened by tent-pole releases around festive holidays (Eid – Salman-Khan starrer *Bajrangi Bhaijan*, Christmas - Sanjay Leela Bhansali's *Bajirao Mastani*); alongside, the company also plans to release a number of other regional movies. We believe the company should comfortably clock at least 20% revenue growth in FY16.

Earnings growth to drive the valuation: Driven by strong movie-pipeline over the next couple of years, we expect EIML to register 21% earnings CAGR in FY15-17 and therefore sustain its current valuation multiple of 17x (FY16E earnings). We assign a target price of Rs 658, based on 17x FY17E earnings. Despite higher growth and better revenue visibility, EIML is trading at discount to global peers, which in our opinion is unjustified. We see the gap narrowing soon.

Poor box office performance remains the biggest risk: EIML still derives ~38% of its revenue from domestic theatrical collection; hence, poor box-office performance of any movie that it distributes can significantly dent the financial performance of the company.

BUY

CMP RS 544

TARGET RS 658 (+21%)

COMPANY DATA

O/S SHARES (MN) :	93
MARKET CAP (RSBN) :	50.3
MARKET CAP (USDBN) :	0.8
52 - WK HI/LO (RS) :	567 / 207
LIQUIDITY 3M (USDMN) :	2.2
PAR VALUE (RS) :	5

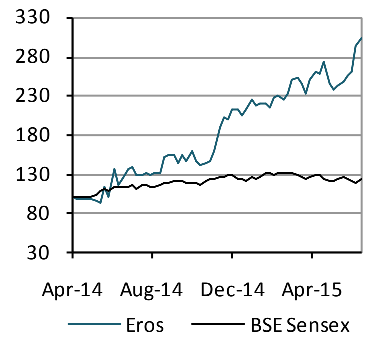
SHARE HOLDING PATTERN, %

PROMOTERS :	74.4
FII / NRI :	19.7
FI / MF :	1.0
NON PROMOTER CORP. HOLDINGS :	1.9
PUBLIC & OTHERS :	2.9

PRICE PERFORMANCE, %

	1MTH	3MTH	1YR
ABS	20.1	29.1	133.5
REL TO SENSEX	19.2	27.8	122.6

PRICE VS. SENSEX



Source: Phillip Capital India Research

KEY FINANCIALS

Rs mn	FY15	FY16E	FY17E
Net Sales	14,212	16,807	20,035
EBIDTA	3,486	4,287	5,125
Net Profit	2,471	2,970	3,604
EPS, Rs	26.5	31.9	38.7
PER, x	20.5	17.1	14.1
EV/EBIDTA, x	15.2	12.5	10.5
P/BV, x	3.4	2.9	2.4
ROE, %	16.7	16.8	17.1
Debt/Equity (%)	28.7	28.5	26.0

Source: PhillipCapital India Research Est.

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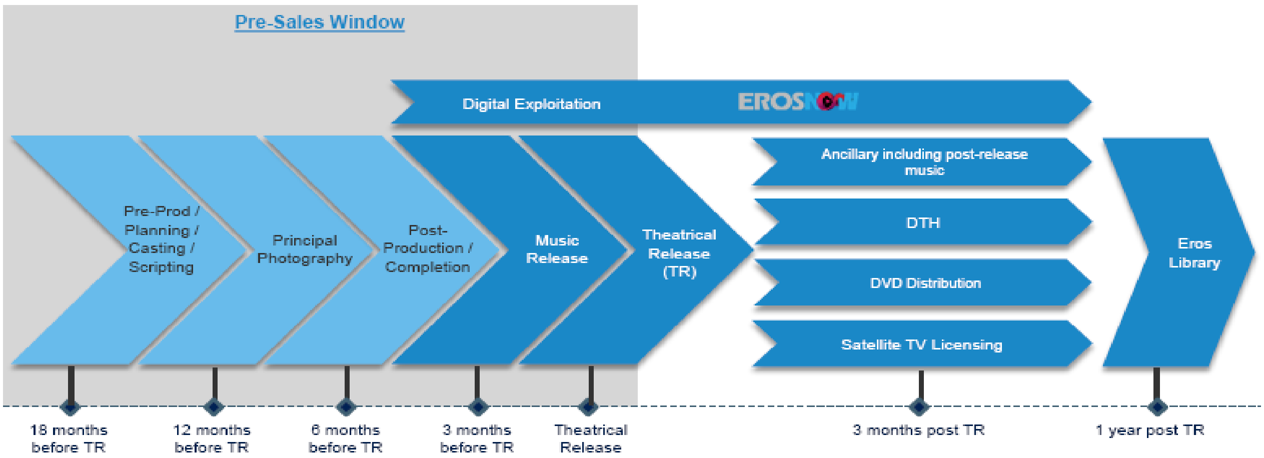
Integrated studio model = monetization through the full value chain

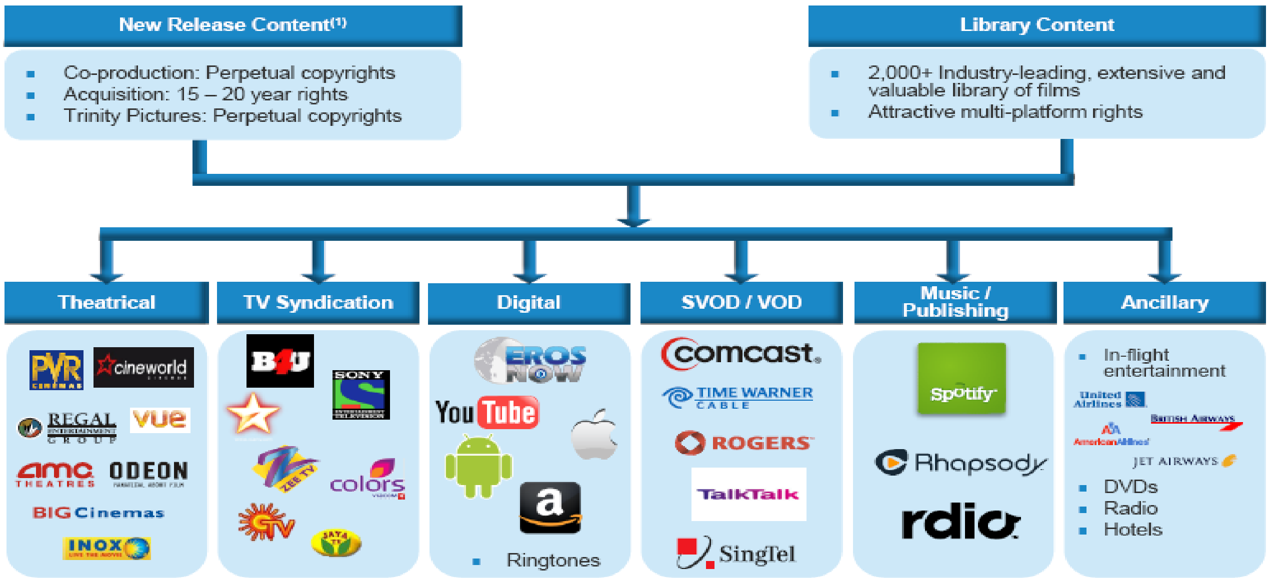
EIML is the only listed player in the Indian media space that operates on a vertically integrated studio model controlling content as well as distribution and exploitation across all formats globally. The company generates revenues across all phases of the movie release cycle and it has adopted a successful multi-platform content monetization model thereby ensuring revenue generation even after a year of movie release (refer to below two tables for details) making the business model less risky as compared to that of a traditional broadcasting or multiplex business.

Maximize monetization through the release Windows



Source: Company, PhillipCapital India Research

Successful multi-platform content monetization model



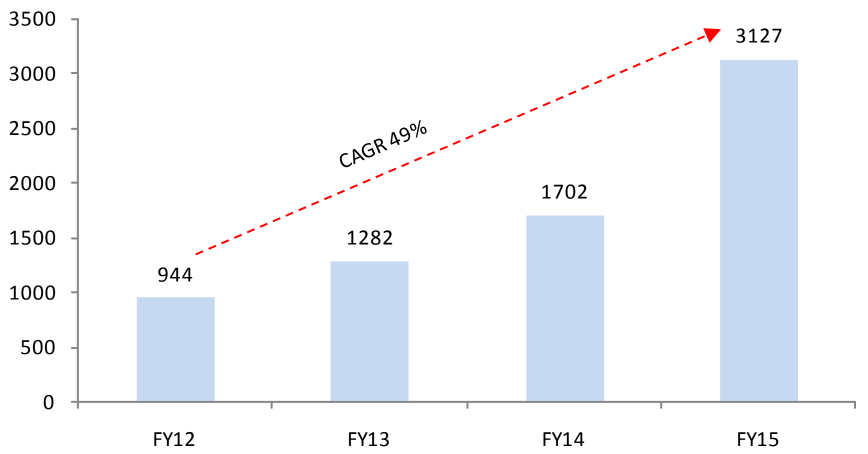
Source: Company, PhillipCapital India Research

Movies are one of the most popular content among Indian audiences and EIML has used this to its advantage. The management has been in the movie-distributing business for the last 30 years and built relationships with all the stakeholders in the value chain, thereby giving them access to top talent and production companies. EIML has participated in 60-70 movies per year over the last three years and its portfolio strength is seen from the fact that three of the top-10 box office successes in each of these years were EIML's. As a result, the company has built a deep library that includes some of the most desirable content in India. It has also amassed the rights to over 2,000 movies in its library, while two of its largest Indian competitors only have combined ~200 movies. EIML partially de-risks its portfolio by diversifying the movie slate based on genre, budget, and language.

The company's first-mover advantage into multiple distribution channels sets it up for outsized growth vs. peers – and it's important to point out that the company is relatively insulated from deep-pocketed competitors/entrants, as the bulk of its key library rights are locked up for the next several years. Overall, we expect that the production of more high-budget movies will not only boost theatrical revenue, but also accelerate topline growth through some of these downstream outlets (especially TV syndication, digital, and SVOD/VOD).

Multiple paths to monetization allow EIML to leverage its library: Over the past decade, EIML has built a unique and valuable library of over 2,000 movies — it has a dominant market share in the Indian movie industry. Over the years, contribution from library revenues has increased to 22% in FY15 from 10% in FY12 due to increased demand for Indian movie content on television in India, as the number of DTH subscribers increased and as the cable industry migrates toward digital technology. This has resulted in a significant increase in demand for premium content such as movies and sports and a resultant increase in licensing fees payable to the company by satellite and cable television operators. Historically, EIML has monetised its revenue stream through sale of satellite rights to leading broadcasters.

Catalogue revenue (Rs mn)



Source: Company, PhillipCapital India Research

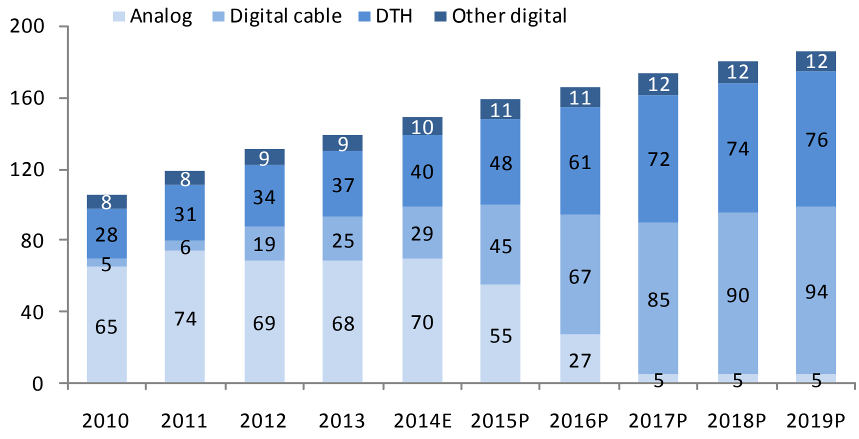
The company is looking at developing multiple revenue streams. According to the management, leading multisystem operators (MSOs) have started acquiring content for their movie channels after the implementation of digitization in major cities. Various industry sources suggest that digital subscribers (both cable and DTH) are expected to increase at annual rate of 20% over the next 4-5 years, auguring well for movie-oriented content providers; with its extensive movie library, EIML is well positioned to benefit from this structural demand.

List of MSO specific movie channels

Hathway	InCable	Den	Digicable
Hathway movies	CVO	Den Movies	Digi Picture
Hathway Classic	Indigital Classic	Den Classic	Multiplex
Hathway Hitz	Indigital North	Den Talkies	Space Movies
Hathway Utsav	Indigital South		

Source: Company, PhillipCapital India Research

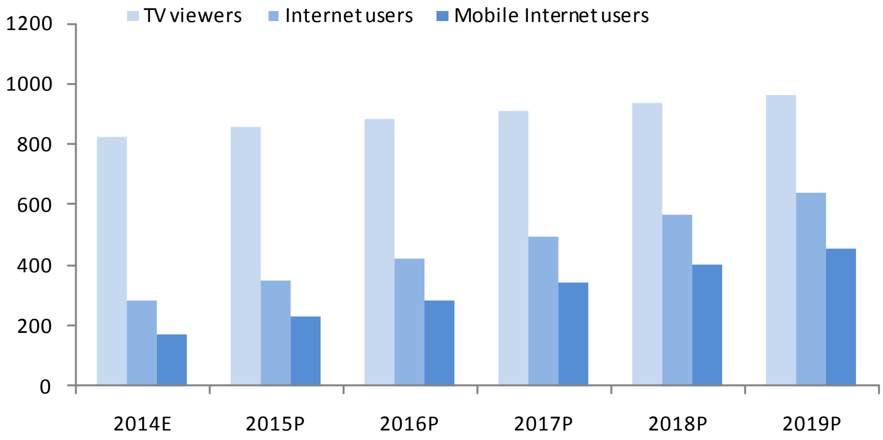
Good growth in digital cable and DTH subscribers augurs well for movie content



Source: FICCI KPMG 2014, PhillipCapital India Research

Mobile usage adds another layer of potential consumers: Internet penetration is extremely low in India at only 20%, a function of both poor infrastructure and low consumer purchasing power. By contrast, broadband penetration in China is 44% and in the US, it is 86%. Driven by increased adoption 3G/4G technology, mobile internet users should compound at 21% from FY14-19. Increased internet penetration and cheaper data rates could open up further avenues of monetization for EIML — this is an upside risk to our estimates.

Strong mobile internet user growth to usher demand for content in digital platform



Source: FICCI KPMG 2014, PhillipCapital India Research

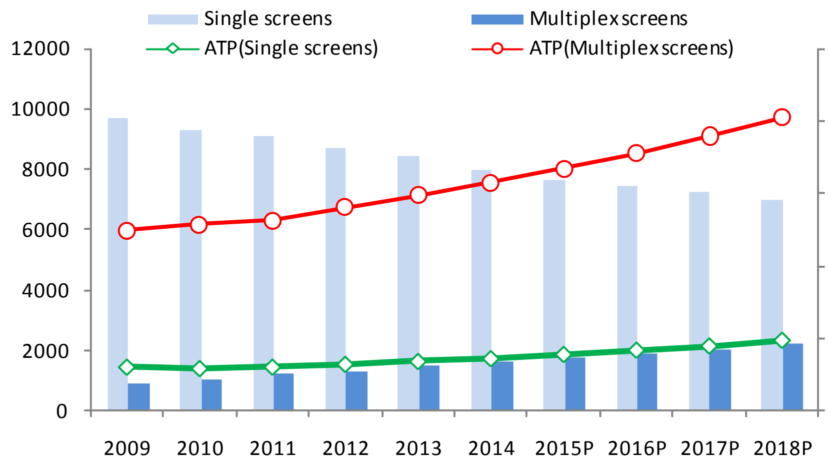
We expect the growth rate of this revenue stream to moderate to 17% over the next couple of years due to higher revenue contribution from the domestic theatrical segment (with many high budget movie releases in FY16/17). We believe that this segment would continue to be of significant importance to the company as it has high margins and provides revenue visibility.

Movie distribution ecosystem undergoing radical changes, more monetizing opportunities becoming realistic

Increased penetration of multiplexes: The number of multiplex screens has seen a CAGR of 25% over four years, but when compared to USA, UK, France, and Spain, India is significantly under-screened. Mumbai and Bangalore have a higher number of screens per million at 23 and 21 respectively while cities such as Hyderabad and Chennai have only about 6, indicating huge opportunity. The current number of multiplex screens stands at 1,200 and we expect these to see a CAGR of 12% from CY14-16. Increased penetration of multiplexes in India will drive domestic theatrical collections at a CAGR of 10% in FY15-17E because of:

- Higher ticket prices in multiplexes (4-5 times that of single screens)
- Occupancy levels in multiplex screens is 30-35% compared to 20-25% in single screen theatres
- Most multiplex screens are equipped to exhibit digital print, hence releasing the movie in a multiplex screen is more cost efficient for the distributor vs. single screen theatres

Growth trends and outlook in average ticket prices and number of screens



Source: UFO Moviez RHP, PhillipCapital India Research Estimates

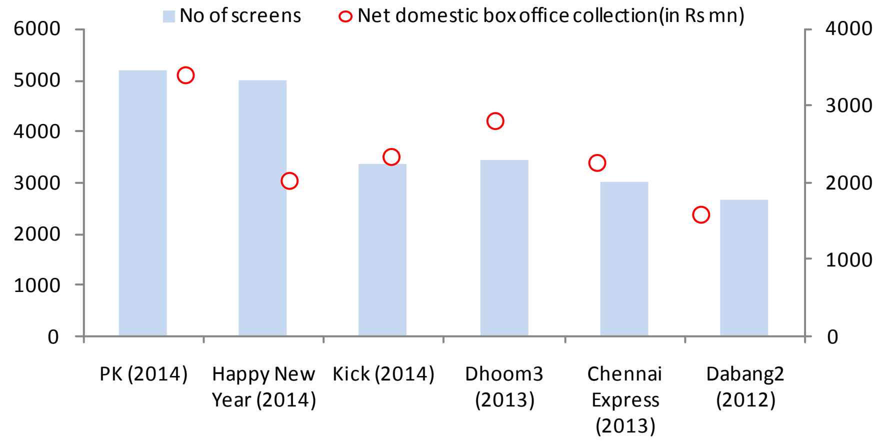
Digitisation has enabled more screens per movie release: The Indian movie industry has very quickly adopted digital cinema, leading to a wider scale of release for a movie without incurring incremental costs. Since the interest of moviegoers in the movie is highest in the opening week, movies releasing in more than 4,500 screens attract more people on the first day itself. The first week and weekend contribute almost 60-80% of a movie's total collections. Even within the first week, the trend is skewed towards the weekend. Consequently, the moneymaking window for a movie has narrowed to the first week itself; therefore, to rake in a higher domestic box office collection, the scale of the movie release matters the most.

Aided by digital prints, number of screens available is increasing

Movie	Year	No of screens	Growth
Hum Aapke Hain Kaun	1994	500	
3 Idiots	2009	1000	2x in 15 years
Dabangg2	2012	2638	2.5 in 3 years
PK	2014	5200	2x in 2 years

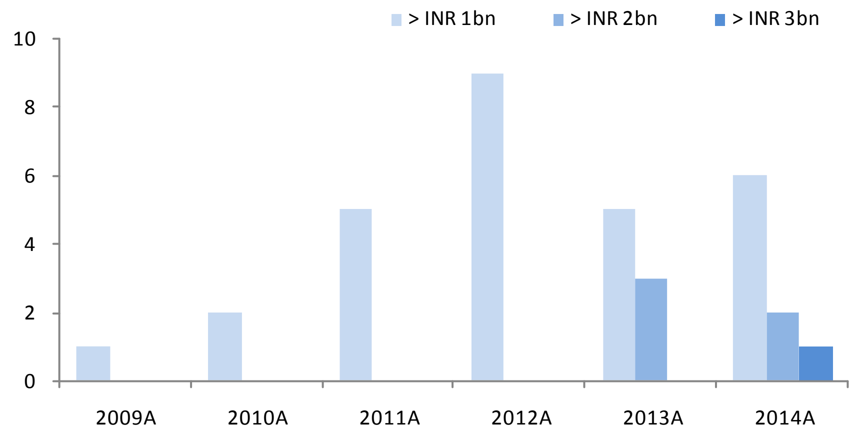
Source: Media articles, PhillipCapital India Research

Wider release ensures higher net box office collection



Source: UFO Moviez RHP, PhillipCapital India Research

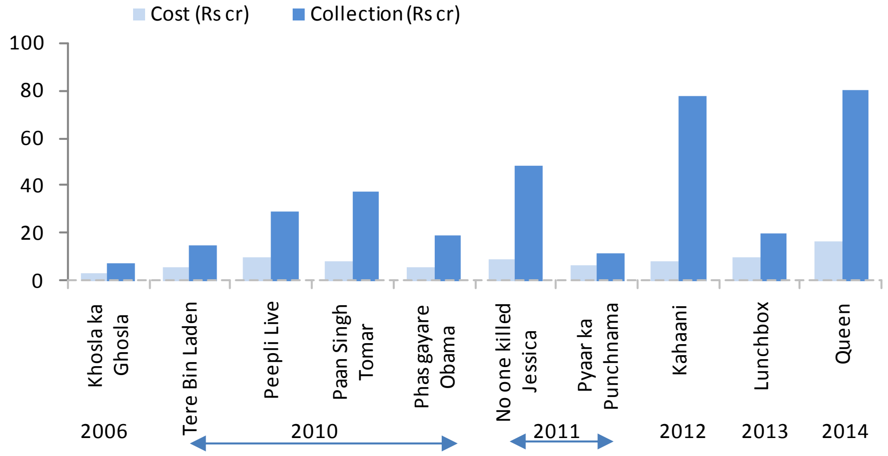
Number of movies with Rs 1bnr+ net box office collection has risen significantly



Source: Company, PhillipCapital India Research

Small-budget or niche-content movies have also benefitted due to digitisation: Small budget content-driven movies are witnessing wider acceptance and popularity in recent years. These movies usually rely on content and performance for success and not on the presence of a big star-cast. The growth in these kinds of movies is based on improving awareness amongst a discerning audience, advent of corporates in movie business, promotion of new talent by big studios, and new themes. However, part of the credit for the recent success that many of these movies have seen goes to digitization. Digitization of movies and the associated lower cost of distribution have enabled such movies with tight marketing budgets to affect releases in theatres across the country. Wider reach and lower distribution costs have helped push the growth of small-budget niche-content movies. A few recent examples of such movies include Khosla ka Ghosla (2006), Paan Singh Tomar (2010), No One Killed Jessica (2011), Kahaani and Vicky Donor (2012), and The Lunchbox (2013).

Trend of some small-budget movies in recent years



Source: Company, PhillipCapital India Research

Structural changes bode well for EIML's unique business model: We believe EIML can continue to leverage its well-established relationships in the industry to source a wide variety of content in a growing market. EIML currently acquires movies two ways — (1) by acquiring rights for movies produced by others, generally through a license agreement or (2) by co-producing movies with a production house (typically referred to as a banner), usually owned by a top Indian actor, director, or writer, on a project-to-project basis. EIML regularly co-produces and acquires movie content from some of the leading banners in India including Red Chillies Entertainment, Illuminati Films, Nadiadwala Grandson Entertainment, Excel Entertainment, affiliates of Vinod Chopra Films and Alumbra Entertainment Media. Regardless of the acquisition method, over the past five years, EIML has obtained exclusive global distribution rights in all media for a minimum period of 5-20 years from the Indian initial theatrical release date.

EIML's primary focus is on sourcing a diversified portfolio of movies that will be commercially successful. The company generally co-produces high-budget movies and acquires rights to more medium- and low-budget movies. The business model of acquiring or co-producing movies rather than investing in significant in-house production capability allows EIML to work on more than one production with key talent simultaneously. This is because the producer or co-producer takes the lead on the time intensive process of production, allowing the company to scale its movie slate more effectively. The following table summarizes typical terms included in the acquisition and co-production contracts.

Typical terms included in the acquisition and co-production contracts

	Acquisition	Co-production
Movie Cost	Negotiated "market value"	Actual cost of production or capped budget and 10-15% production fee
Rights	5-20 years	Exclusive distribution rights for at least 20 years after which Eros shares control over the further exploitation of the movie, and co-owned copyright in perpetuity, subject to applicable copyright laws
Payment terms	10-30% on signature; balance on delivery or in instalments between signing and delivery	In accordance with movie budget and production schedule
Recoupment waterfall	"Gross" revenues less 10-20% EIML's distribution fee (% of cost /gross revenues) less print & advertising costs (actuals) less cost of the movie equals Net revenues, generally shared equally	Generally same as acquisition, except sometimes Eros also charges interest and/or a production or financing fee for the cost of capital and overhead recharges

EIML secures distribution or intellectual property rights to a diverse portfolio of over 75 movies annually— 10-20 are mainstreams Hindi movies and the rest are in regional languages such as Tamil, Telugu, Marathi, and Punjabi. Over the years, EIML has consciously increased the focus on high- and moderate-budget movies — this is because better production values and high-profile stars attract larger audiences and carry higher appeal for television and digital licensing. All this not only leads to favourable pre-licensing, but also higher margins. The company also acquires selected catalogue rights to augment the size of its library further.

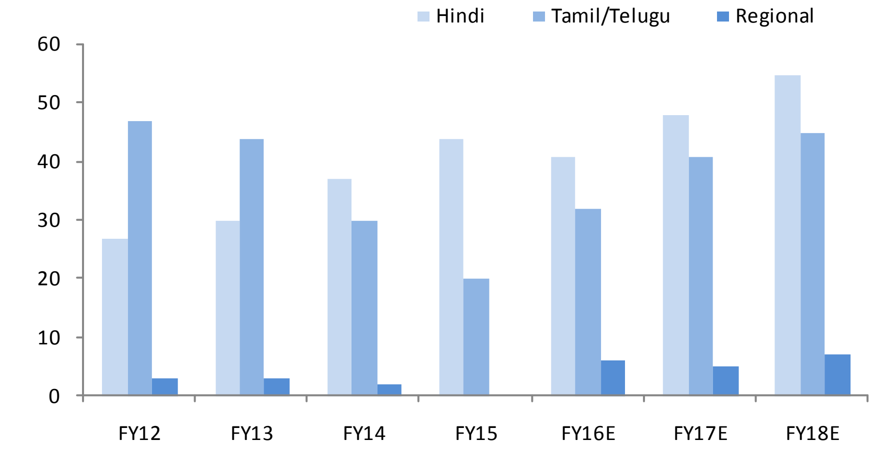
Strong movie pipeline – focus back on big-budget movies but selectively: EIML has been able to significantly scale up its movie slate for FY16 and FY17. Group-level financing has been augmented by the recent listing and follow-on fund raising by the ultimate holding company - Eros Plc - in CY14. Including regional movies, we estimate at least eight big-budget movies scheduled for release in FY16. While the market for Hindi satellite rights has been cooling off over the past 3-4 quarters, regional movies remain on a strong footing.

EIML's movie pipeline for FY16 and FY17

Releases in FY' 16 to date	Release date	
Gabbar is back (overseas)	Q1 FY' 16	
Uttama Villain (Tamil)	Q1 FY' 16	
Tanu Weds Manu Returns	Q1 FY' 16	
Masss (Tamil)	Q1 FY' 16	
Aga Bai Arechaa 2 (Marathi)	Q1 FY' 16	
Dil Dhadakne Do (Overseas)	Q1 FY' 16	
Release title	**Star Cast / (Director/Producer)**	**Tentative release date**
Life of Josootty (Malayalam)	Dileep, Jyothi Krishna, Rachana Narayankutty (Jetthu Joseph)	Q2 FY' 16
Bajrangi Bhaijaan	Salman Khan, Kareena Kapoor (Kabir Khan)	Q2 FY' 16
Rajini Murugan (Tamil)	Sivakarthikeyan (Ponram)	Q2 FY' 16
Bangistan (Overseas)	Ritesh Deshmukh, Pulkit Samrat, Jaqliene Fernandis(Karan Anshuman)	Q2 FY'16
Hero	Sooraj Pancholi, Adheya Shetty (Nikhil Advani)	Q2 FY'16
Singh is Bling (Overseas)	Akshay Kumar, Kareena Kapoor, Amy Jackson (Prabhu Deva)	Q3 FY'16
Bajirao Mastani	Ranveer Singh, Deepika Padukone (Sanjay Leela Bhansali)	Q3 FY' 16
Gabbar Singh 2 (Telegu)	Pawan Kalyan (K. S. Ravindra)	Q4 FY'16
Aligarh	Kangana Ranaut (Hansal Mehta)	Q4 FY'16
Dictator (Telugu)	Balakrishna (Srivaas)	Q4 FY'16
Naale (Malayalam)	Fahad Fazil, Malavika S Mohan, Isha Talwar, Mukesh (Shiju S Bawa)	Q4 FY'16
Perai Thedai Natkal (Tamil)	Ashok Selvan (Abraham Prabhu)	Q4 FY'16
Enkitta Mothathe (Tamil)	Natarajan Subramaniyam Rajaji and Vijay Murugan (Ramu Chellappa)	Q4 FY'16
Housefull 3	Akshay Kumar, Abhishekh Bachchan, (Director-Sajid-Farhad)	FY' 17
Shivay	Ajay Devgn (Ajay Devgn)	FY' 17
Untitled	Kajol (Ajay Devgan Productions)	FY '17
Farzi	Shahid Kapoor, Kiriti Sanon (Raj Nidimoru and Krishna D.K.)	FY' 17
Banjo	Riteish Deshmukh, Nargis Fakhri (Ravi Jadhav)	FY '17
Raabta	Sushant Singh Rajput (Dinesh Vijayan and Homi Adjania)	FY'17
Jugaadu	Harman Baweja and others	FY'17
Untitled	Saif Ali Khan (3 movies)	FY'17

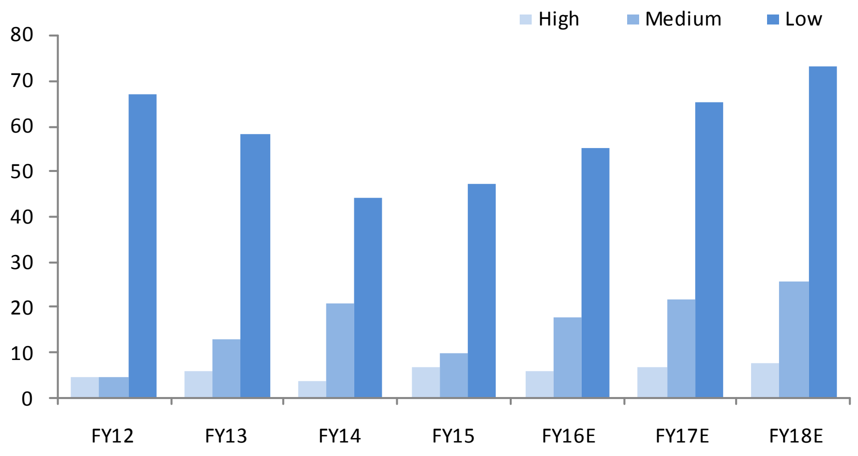
Source: Company, PhillipCapital India Research

EIML movie slate by language



Source: Company, PhillipCapital India Research

EIML movie slate by budget category

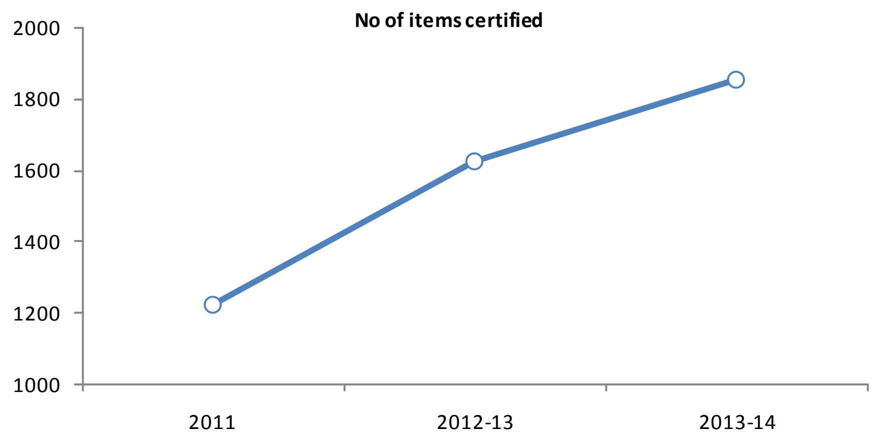


Source: Company, PhillipCapital India Research

Regional movie foray widens choice and increases addressable market

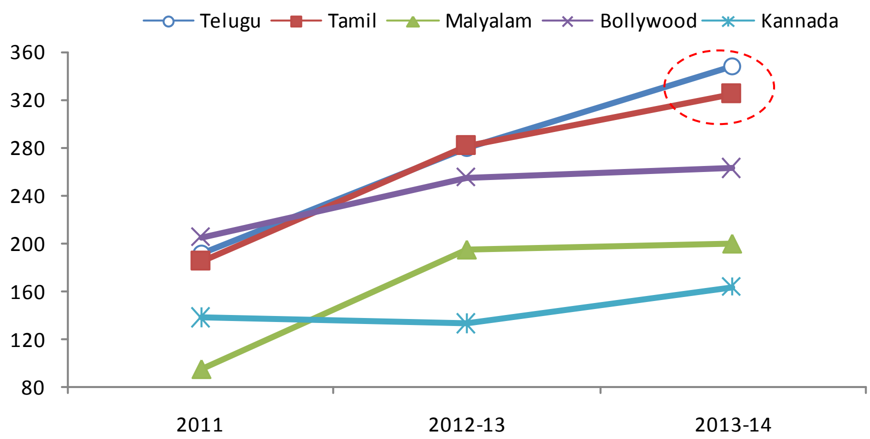
Market for regional movies is becoming stronger – good play for large studios: As per data available from the film federation of India, the Indian film industry has grown 23-24% annually between 2011 and 2013-14 in terms of number of movies certified. Growth in regional movies such as Tamil, Telugu, Malayalam, and Punjabi has generally outstripped the growth in Hindi movies. Although the high growth in Punjabi movies is also a factor of a small base, the number of Tamil and Telugu movies produced in the country are now higher than the number of Bollywood movies. Tamil movie industry is also seeing growth in reach with a wider scale of release – 'Lingaa' (movie distributed by EIML) was released across 4000+ screens resulting in higher box office collection. Tamil and Telugu movie industries face the challenge of not being able to offer enough cinema screens to a movie considering on an average 4-5 movies are released every week. This is where large studios add value with their strong reach in domestic and international markets.

Trend and break up of movies certified



Source: UFO MovieZ RHP, PhillipCapital India Research

Trend and break up of movies certified



Source: UFO MovieZ RHP, PhillipCapital India Research

Top-10 grossing Tamil and Telugu movies

Movie	Language	Total Distributor Share(in Rs mn)
Robot	Tamil	1600
I	Tamil	120
Magadheera	Telugu	830
Sivaji	Tamil	800
Lingaa	Tamil	800
Attarintiki Daaredi	Telugu	750
Thuppakki	Tamil	690
Kaththi	Tamil	680
Singam 2	Tamil	670
Gabbar Singh	Telugu	610

Source: Media articles, PhillipCapital India Research

Increasing presence in regional movies shielded the company from the CY14 slowdown: EIML has been progressively increasing its presence in regional movies in both domestic as well as international markets. Historically the company was targeting regional movies for overseas release only but off late, it has been increasing its focus on the domestic market as well. Currently the company is focussing more on Tamil and Telugu movies (as they are the next biggest market after Hindi movies) but it has plans to grow its presence in Malayalam, Marathi, Punjabi and other languages. EIML enters into minimum guarantee deals with regional/smaller distributors in southern markets. Minimum guarantee for distribution in select regions along with pre-sales of TV satellite rights enables EIML to recover 70-100% of the cost of the movie before the release.

In FY15, EIML witnessed 20% earnings growth yoy, against a backdrop of India's weak box office performance (box-office collection for the movie industry declined in FY15). EIML's impressive earnings growth was primarily because of focus on Tamil/Telugu movies and niche Hindi movies with good content.

De-risked business model through diversification of revenue stream

Sale of cable and satellite movie rights even before theatrical release: EIML sells the C&S rights of the movie even before it is released in theatres at a pre-negotiated price, generally by bundling releases in a package that is licensed to satellite television operators for a specified period (usually 5-7 years) — this reduces dependence on domestic box-office performance. Through this method, EIML is able to recover 20-30% of the cost of the movie, thereby reducing the dependence on domestic theatrical collections. EIML has already pre-sold C&S rights for most of its FY16-17 movie releases.

Why do broadcasters pay such a high price?
Screening of the world premiere (on TV) of a big-ticket movie not only acts as a GRP booster, but also attracts new viewers, which in turn boosts a channel's advertising revenue. For EIML, the robust competition among rival channels for viewership (which in turn attracts more advertisers) and the launch of new movie channels will ensure continued demand for prime movie content in FY17 as well.

Sale of international theatrical right of a movie to the holding company: Selling international distribution right to the parent company i.e. Eros International Plc, even before the release of the movie, helps EIML to recover 30% of the cost of the movie. EIML sells international distribution rights to its ultimate holding company at 30% of the movie's cost (+30% mark-up) even before the movie is released for domestic screening, thereby insulating itself from the risk of domestic box-office performance. The scheme of agreement with the parent company also provides certainty to cash flows. Through its wide distribution network, Eros International Plc is able to release the movie (across all formats) in 50 countries, including the expatriate South Asian population concentrated in UK, USA, Canada, Dubai, South Africa, Australia and Singapore.

Scheme of arrangement of EIML with Eros International Plc
Eros International Plc will unconditionally acquire, exclusive international distribution rights for Indian movies (movies produced co-produced or acquired within the territory of India Nepal and produced, co India, Bhutan excluding Tamil movies) for which EIML holds distribution rights
Guaranteed Fee
Minimum guarantee fee to be paid = 30% of the production/acquisition cost to EIML + mark-up of 30%
Retaining All Domestic Rights
Indian movie rights and India television rights within India shall be retained by EIML
Profit-sharing agreement
Gross proceeds (net of minimum guarantee fee, commission of 20% of gross proceeds and distribution expenses) received by Eros International Plc will be shared between Eros International Plc and EIML in a 70:30 ratio
Non-Compete
Eros International Plc will not produce, co-produce or acquire movie rights in any Indian movie and Tamil language movie for exploitation within India, Nepal and Bhutan without first providing Eros India the right to independently participate in or acquire such a business opportunity
Tenure
The Relationship Agreement may be reviewed on an annual basis, and is valid for an initial period of five years, automatically renewable for successive two year terms

Source: Company, PhillipCapital India Research

EIML pre-sells most other ancillary rights (like music and digital platform): This helps the company recover 10% of the cost of the movie. Given the largest visibility and the strength of the slate of movies to be released, EIML is able to sell other ancillary rights (digital and music) of the movie well before the movie is released.

To conclude, by pre-selling C&S rights, international distribution rights, and other ancillary movie rights, EIML recovers almost 45-85% (100% for regional) of the production cost of the movie thereby reducing the dependence on domestic theatrical performance.

Case Study: EIML was able to recover investment despite poor box office performance

Movie: Action Jackson	(Rs Cr)
Cost of production (A)	65
Publicity & advertisement expenses (B)	10
Total cost to EIML (A)+ (B)	75
International right (C)	25
Net domestic box-office collection	58
EIML's share (D)	26
Music and other ancillary right (E)	5
Satellite right (F)	25
Total revenue accrued to EIML - (C)+ (D)+ (E) +(F)	81
ROI	8.60%

Source: Media articles, PhillipCapital India Research

ErosNow is potentially the most important driver

It is ideally positioned to capitalise on growing internet penetration and benefits from high barriers to entry. ErosNow is an online content provider that was launched in August 2012. Since then the service has ramped up its offerings to over 1,000 movies and 6,500 music videos. The rest of EIML's movie library is in the process of being converted to the desired format and uploaded to the platform. The company plans to make all of its own movie content available on the ErosNow format. EIML also has contracts with partners such as Viacom 18 Media, Zee TV, and UTV for TV content. ErosNow content is currently available over an increasing number of platforms across India, as the company recently signed contracts with Asianet Broadband, GTPL, RailTel and Chromecast. The ErosNow platform has also continued to enhance its content offering with catch-up shows now available from Sony and SAB TV, Colors, Zee TV, Hum TV and several other leading television channels. We expect Eros to enter into deals with more Indian studios over time to gain access to more content.

There are currently two levels of service: (1) an ad-supported free service; and (2) a subscription-based premium service that gives customers access to additional content and some original programming. ErosNow currently has 14mn users (this, when the company hasn't even officially launched the marketing campaign, which will kick off this July around the latest exclusive movie premieres as well as original shows) signed up to its platform, of which ~2-3% are paying fees of Rs 150 per month for full access to content, including new releases. It hopes to eventually convert a similar 10% of its potential audience in India to fee-paying customers. It is likely to reduce its subscription price from current Rs150/month to attract these users. ErosNow is the sole OTT player in Indian-language movies, and improvements in India's broadband and wireless infrastructure should provide the catalyst for subscriber growth.

In June 2014, EIML announced the acquisition of TechZone, a mobile value-added service provider that complement Eros' digital efforts. Techzone is an aggregator, developer and distributor of entertainment content via mobile platforms.

- A mobile monetization business offering direct billing, which the company plans to integrate into Eros Now – this is a mobile wallet service, eliminating the need for credit card payments
- Ringback tones, where customers pay the telecom operator for ring tones (presumably to incorporate Eros music) for which Eros gets a cut.

ErosNow's features/metrics outperform international platforms/South Asian peers

Metrics	EROS NOW	NETFLIX	hulu	BIGFLIX	spuul
Daily Time on Site per Visitor (Min)	4.0	5.5	5.0	2.1	2.2
Features					
Premium Movies	✓	✓	✓	✓	✓
Free Movies	✓	✗	✓	✓	✓
Short-form Content	✓	✗	✓	✗	✗
Original Content	✓	✓	✓	✗	✗
Catch-up TV	✓	✗	✓	✗	✗
Live Stream Events	✓	✗	✗	✗	✗
Music Content	✓	✗	✗	✗	✗

Source: Company, PhillipCapital India Research

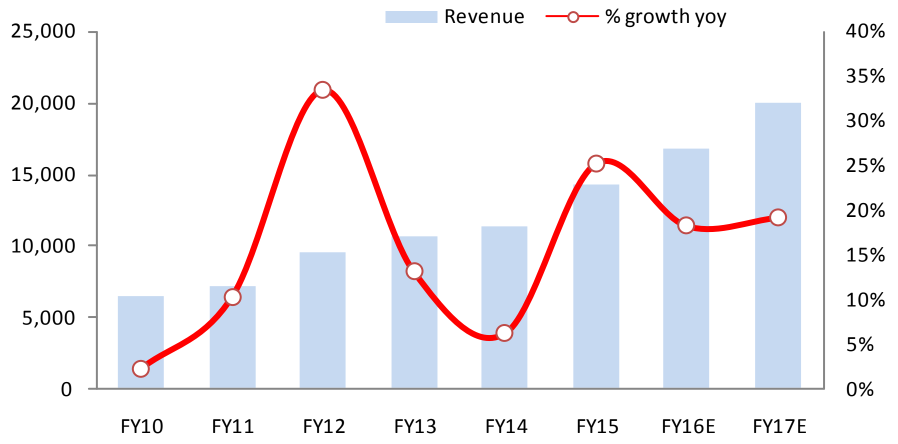
Financials

Strong movie pipeline to drive revenue CAGR of 16% over FY15-17: : Driven by a strong slate of movie releases planned over the next couple of years, we are forecasting 20% revenue CAGR for EIML over FY15-17. For EIML, *Tanu Weds Manu Returns,* a medium-budget movie release in May has already been a blockbuster; hence, we expect the company to report robust profit numbers in the Q1FY16. EIML schedule for the rest of FY16 is strengthened by tent-pole releases around festive holidays (Eid – Salman-Khan starrer *Bajrangi Bhaijan*, Diwali and Christmas - Sanjay Leela Bhansali's *Bajirao Mastani*); alongside, the company also plans to release a number of other regional movies. We believe the company should comfortably clock at least 20% revenue growth in FY16.

EIML has also strategically pushed a few of its releases and also lined several big-budget movies thereby providing visibility to FY17 revenues as well. We are forecasting 20% revenue growth in FY17.

We have not yet factored potential monetization of the ErosNow platform and revenue from recent Chinese deals in our estimates.

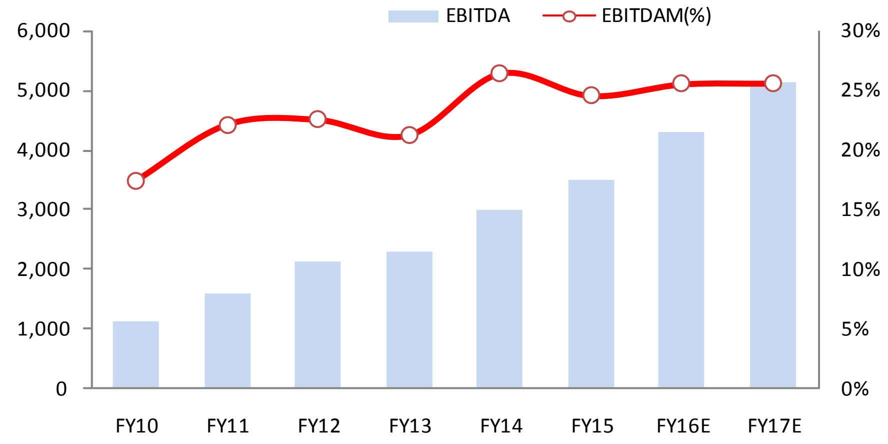
Revenue growth assumption



Source: Company, PhillipCapital India Research Estimates

Stable EBITDA margins to drive EPS growth, in line with revenue growth: We conservatively assume stable EBITDA margins over FY15-17, despite 190bps decline in FY15 (which was driven by non-recurring write-off of content advances and bad debts). We are assuming that cost inflation moves in line with revenue growth. We believe that our forecast is conservative and has multiple upside triggers (such as higher contribution from high margin catalogue and satellite sales and faster than expected monetization of ErosNow platform). Driven by strong revenue growth and stable EBITDA margin we forecast EPS growth of 21% over FY15-17.

Annual movement of EBITDA and EBITDA margins



Source: Company, PhillipCapital India Research Estimates

Valuation

Despite higher growth and better revenue visibility EIML is trading at discount to global peers: EIML is the only listed player in the Indian media space, which makes content agnostic of the platform. Adoption of a studio model helps monetize content across all platforms, making the business model less risky as compared to that traditional broadcasting or multiplex businesses. Huge movie library of 2,000+ titles makes it well positioned to benefit from the emergence of various new digital platforms (cable, smartphone) and any potential monetization of the library via this emerging platform can significantly add to earnings, as the cost associated with providing this services is very minimal (EIML already has all of its titles in digital platform). Despite higher growth and better revenue visibility, a less-risky business model, and huge option-value associated with its ErosNow business, EIML is trading at significant discount to Indian media peers and global peers — this, in our opinion is unjustified and we expect the gap to close in the near future.

Trading at a significant discount to global peers

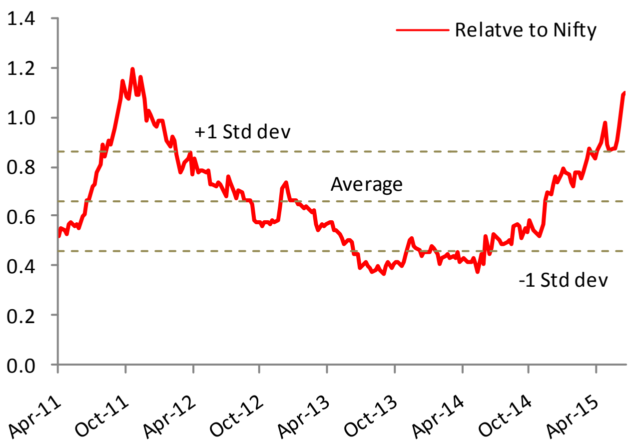
	P/E			P/B			ROE		
	FY16E	FY17E	FY18E	FY16E	FY17E	FY18E	FY16E	FY17E	FY18E
Lions Gate	22.6	19.0	16.1	6.1	5.5	5.1	25.4	27.0	22.4
Walt Disney	22.5	19.9	18.0	4.1	3.7	3.5	18.2	21.5	18.2
Viacom	11.5	10.1	9.1	7.8	7.9	7.9	60.3	73.7	82.1
Dreamworks	-69.7	37.1	31.1	2.2	2.1	2.0	-4.5	4.1	6.4
21st Century Fox	19.2	16.5	13.5	3.9	3.6	3.6	24.1	22.6	27.8
Eros Plc	23.7	18.5	14.8	1.7	1.5	1.4	6.6	7.9	10.1
PVR Cinemas	39.3	23.4	19.2	5.5	4.6	3.4	15.0	20.1	19.8
Inox Leisure	32.4	18.7		2.2	2.0		7.0	10.9	
EIML	**17.1**	**14.1**	**11.1**	**2.9**	**2.4**	**2.0**	**16.8**	**17.1**	**18.1**

Source: Bloomberg, PhillipCapital India Research Estimates

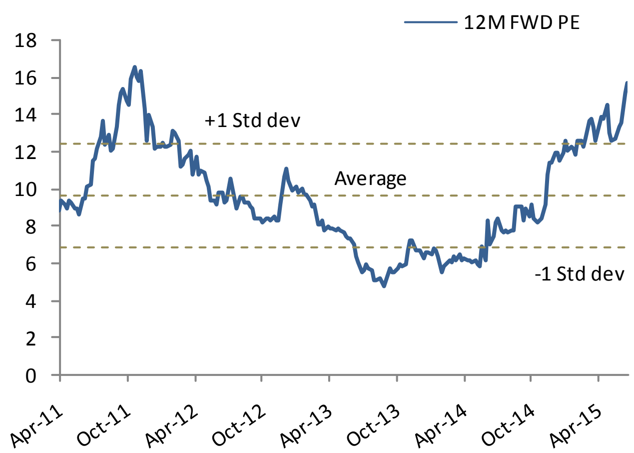
Robust financial performance to narrow the valuation gap with global peers

EIML has shown robust financial performance over FY11-15 —revenue/EBITDA/PAT saw CAGRs of 19%/25%/20%. We expect it to continue its growth trajectory and see EPS CAGR of 21% over the next couple of years. The company should sustain its current P/E multiple (currently trading 17x FY16E earnings). We arrive at a price target of Rs 658 based on 17x FY17E earnings, implying 21% upside from current level.

Relative to Nifty



12-month forward P/E



Source: Company, PhillipCapital India Research Estimates

Investment Risk & Concerns

Poor domestic box office performance of a movie remains the biggest risk: EIML derives 38% of its revenue from domestic theatrical collection; hence, poor box-office performance of movies co-produced/acquired by EIML can significantly impact financials.

Delay in completion of a project can stretch the financial requirement: EIML works on a co-production/acquisition led model. Any delay in the completion of the project (or delay in theatrical release of the movie) can significantly increase the working capital requirement, which in turn will have a negative impact on interest costs.

Declining bargaining power with exhibitors can impact revenues/margins: The multiplex exhibition industry has seen significant consolidation over the past few years, resulting in the emergence of three large players (PVR Cinemas, INOX Leisure and Carnival Cinemas). Earlier, the industry was working on a standardised profit-sharing formula; in recent years, deals are struck project-wise. If exhibitors are able to exact better terms of trade from EIML, it will impact revenues and margins

Any dispute with any production house can have a negative impact: The movie industry is relationship driven. EIML is able to acquire/co-produce most of its projects because of long-standing relationships with most production houses in the country. Any dispute with them can have a negative impact on business volumes.

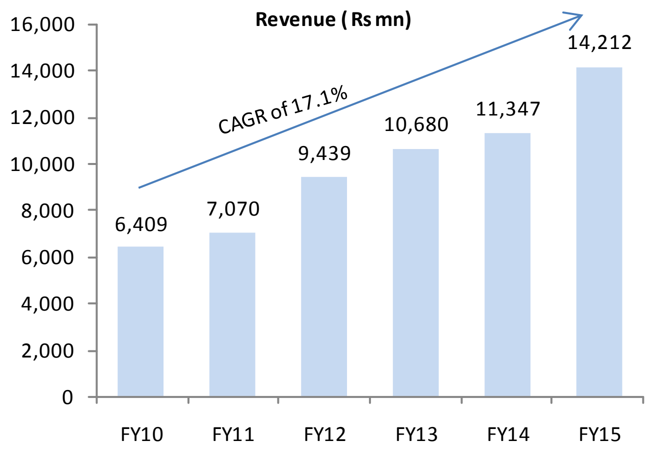
Company overview

EIML is a leading global company in the Indian movie entertainment industry that acquires, co-produces, and distributes Indian movies across all available formats such as cinema, television, and digital new media. EIML is part of Eros International Plc, which became the first Indian media company to raise capital and be listed on the New York Stock Exchange.

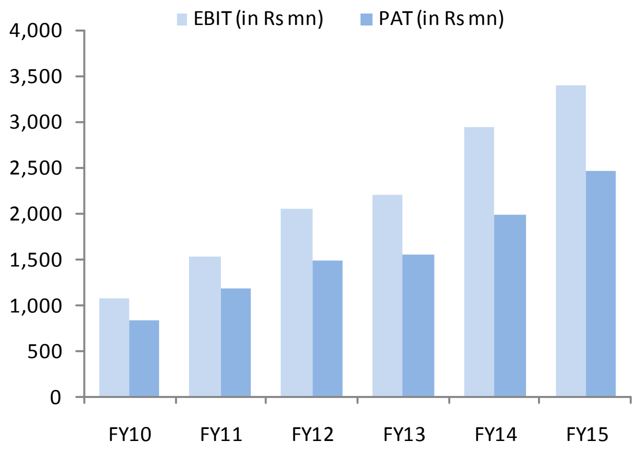
EIML has over three decades of experience in establishing a global platform for Indian cinema. The company has a competitive advantage through its extensive and growing movie library of 2,000+ movies, which include Hindi, Tamil, and other regional-language movies for home entertainment distribution. EIML has also built a dynamic business model by combining the release of new movies every year with the exploitation of its movie library. The company has released more than 210+ movies over the last 3 years.

The company has a diversified revenue mix wherein theatrical contributes to 38%, overseas contributes to 31%, and TV and others contribute to 31% of its revenues.

Strong Historical Revenue growth



with solid track of profitability



Source: Company, PhillipCapital India Research Estimates

Financials

Income Statement

Y/E Mar, Rs mn	FY14	FY15	FY16e	FY17e
Net sales	**11,347**	**14,212**	**16,807**	**20,035**
Growth, %	6	25	18	19
Other income	0	0	0	0
Total income	11,347	14,212	16,807	20,035
Raw material expenses	-7,733	-9,400	-11,125	-13,366
Employee expenses	-282	-359	-398	-439
Other Operating expenses	-335	-967	-996	-1,105
EBITDA (Core)	**2,998**	**3,486**	**4,287**	**5,125**
Growth, %	32.5	16.3	23.0	19.5
Margin, %	26.4	24.5	25.5	25.6
Depreciation	-50	-69	-62	-59
EBIT	**2,947**	**3,417**	**4,225**	**5,066**
Growth, %	34.1	15.9	23.7	19.9
Margin, %	26.0	24.0	25.1	25.3
Interest paid	-331	-384	-354	-372
Other Non-Operating Income	50	199	0	0
Non-recurring Items	0	0	0	0
Pre-tax profit	**2,670**	**3,232**	**3,956**	**4,807**
Tax provided	-737	-762	-996	-1,210
Profit after tax	**1,933**	**2,470**	**2,960**	**3,597**
Others (Minorities, Associates)	64	1	10	6
Net Profit	**1,997**	**2,471**	**2,970**	**3,604**
Growth, %	29.2	23.7	20.2	21.3
Net Profit (adjusted)	**1,997**	**2,471**	**2,970**	**3,604**
Unadj. shares (m)	92	93	93	93
Wtd avg shares (m)	93	93	93	93

Balance Sheet

Y/E Mar, Rs mn	FY14	FY15	FY16e	FY17e
Cash & bank	1,544	1,697	2,256	2,409
Debtors	2,053	5,257	6,218	7,412
Inventory	40	1,369	1,619	1,930
Loans & advances	6,408	12,021	14,216	16,946
Other current assets	1,402	201	201	201
Total current assets	11,446	20,545	24,510	28,898
Investments	80	0	0	0
Gross fixed assets	33,693	40,471	49,024	59,161
Less: Depreciation	-23,285	-28,330	-34,885	-42,700
Net fixed assets	10,408	12,141	14,139	16,461
Total assets	**21,934**	**32,686**	**38,650**	**45,359**
Current liabilities	3,452	11,032	13,009	15,466
Total current liabilities	3,452	11,032	13,009	15,466
Non-current liabilities	6,384	6,820	7,956	8,828
Total liabilities	9,835	17,852	20,964	24,294
Paid-up capital	920	925	925	925
Reserves & surplus	11,167	13,897	16,758	20,144
Shareholders' equity	12,099	14,834	17,685	21,064
Total equity & liabilities	**21,934**	**32,686**	**38,650**	**45,359**

Source: Company, PhillipCapital India Research Estimates

Cash Flow

Y/E Mar, Rs mn	FY14	FY15	FY16e	FY17e
Pre-tax profit	2,670	3,232	3,956	4,807
Depreciation	50	69	62	59
Chg in working capital	-891	-1,365	-1,429	-1,777
Total tax paid	-220	-244	-642	-781
Cash flow from operating activities	**9,083**	**12,529**	**11,210**	**13,416**
Capital expenditure	-8,959	-11,138	-10,373	-12,407
Chg in investments	2	80	0	0
Cash flow from investing activities	**-7,858**	**-11,090**	**-10,413**	**-12,449**
Free cash flow	1,226	1,439	798	967
Equity raised/(repaid)	1	5	0	0
Debt raised/(repaid)	491	-82	783	443
Dividend (incl. tax)	0	0	109	218
Cash flow from financing activities	**68**	**-170**	**404**	**-34**
Net chg in cash	1,294	1,269	1,202	933

Valuation Ratios

	FY14	FY15	FY16e	FY17e
Per Share data				
EPS (INR)	21.4	26.5	31.9	38.7
Growth, %	29.2	23.7	20.2	21.3
Book NAV/share (INR)	129.8	159.2	189.9	226.3
FDEPS (INR)	21.4	26.5	31.9	38.7
CEPS (INR)	22.0	27.3	32.6	39.3
CFPS (INR)	16.7	16.0	20.9	24.8
DPS (INR)	-	-	(1.0)	(2.0)
Return ratios				
Return on assets (%)	10.7	9.9	8.9	9.1
Return on equity (%)	16.5	16.7	16.8	17.1
Return on capital employed (%)	12.7	13.5	13.5	13.8
Turnover ratios				
Asset turnover (x)	0.7	0.8	0.8	0.8
Sales/Total assets (x)	0.6	0.5	0.5	0.5
Sales/Net FA (x)	1.2	1.3	1.3	1.3
Working capital/Sales (x)	0.6	0.5	0.6	0.6
Receivable days	66.0	135.0	135.0	135.0
Inventory days	1.3	35.2	35.2	35.2
Working capital days	207.5	200.7	200.8	200.8
Liquidity ratios				
Current ratio (x)	3.3	1.9	1.9	1.9
Quick ratio (x)	3.3	1.7	1.8	1.7
Interest cover (x)	9.0	8.9	15.7	19.6
Dividend cover (x)			(31.9)	(19.4)
Total debt/Equity (%)	35.8	28.7	28.5	26.0
Net debt/Equity (%)	23.1	17.2	15.7	14.6
Valuation				
PER (x)	25.4	20.5	17.1	14.1
PEG (x) - y-o-y growth	0.9	0.9	0.8	0.7
Price/Book (x)	4.2	3.4	2.9	2.4
Yield (%)	-	-	(0.2)	(0.4)
EV/Net sales (x)	4.7	3.7	3.2	2.7
EV/EBITDA (x)	17.6	15.2	12.5	10.5
EV/EBIT (x)	17.9	15.5	12.6	10.6

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