ICRA

Media and Entertainment

June 2020

Impact of COVID-19 - Pain, Hope and Opportunities

Subrata Ray
+91 22 6114 3408
subrata@icraindia.com

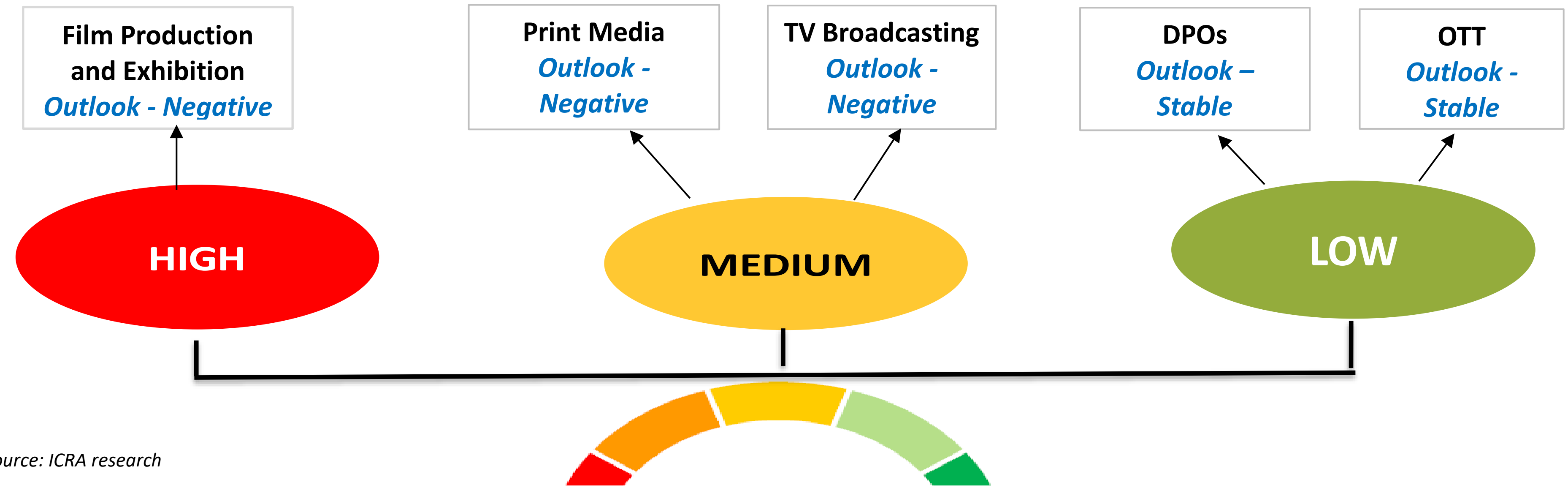
Kinjal Shah
+91 22 6114 3442
kinjal.shah@icraindia.com

Sakshi Suneja
+91 22 6114 3438
sakshi.suneja@icraindia.com

OUTLOOK

ICRA has a negative credit outlook for the film production and exhibition, print media and television (TV) broadcasting segments of the Indian Media and Entertainment (M&E) industry. Besides the direct impact by way of lost sales due to the shut-down of cinema halls, given the adverse impact on the overall economy, sharp reduction in advertisement spends in April and May 2020, which will continue over the short-term. This, in turn, will dampen the revenues and profit margins of the aforementioned segments of the Indian M&E industry in FY2021. The impact of the COVID-19 pandemic on the distribution platform operators (DPOs) will be limited as subscribers will to hold on to their current subscription packages. Over-the-top (OTT) platforms are also placed favourably vis-a-vis other segments and are witnessing spike in consumption. The credit outlook for these segments is thus stable.

Exhibit 1: Credit Outlook for various segments of the Indian M&E industry



Source: ICRA research

FILM PRODUCTION AND EXHIBITION SEGMENT

Within the M&E industry, the film exhibition segment has been impacted the most with the pandemic. While the virus fears had already impacted the footfalls in theatres in the month of March 2020 by 30-40%, mandated closure of cinema halls across states starting March 10, 2020 has brought the film exhibition business to a complete standstill. Shutdown of cinema halls has also resulted in the film producers having to defer their movie releases.

The film exhibition industry is characterised by high fixed costs. Around 40-45% of the total cost of the film exhibitors (primarily multiplexes) is fixed in nature, with lease rental being the major component accounting for 20-22% of the total cost.

Exhibit 2: Revenue Break-up for Exhibitors

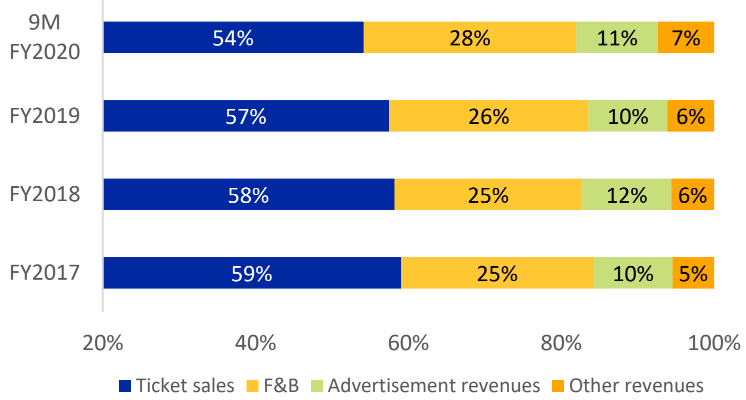
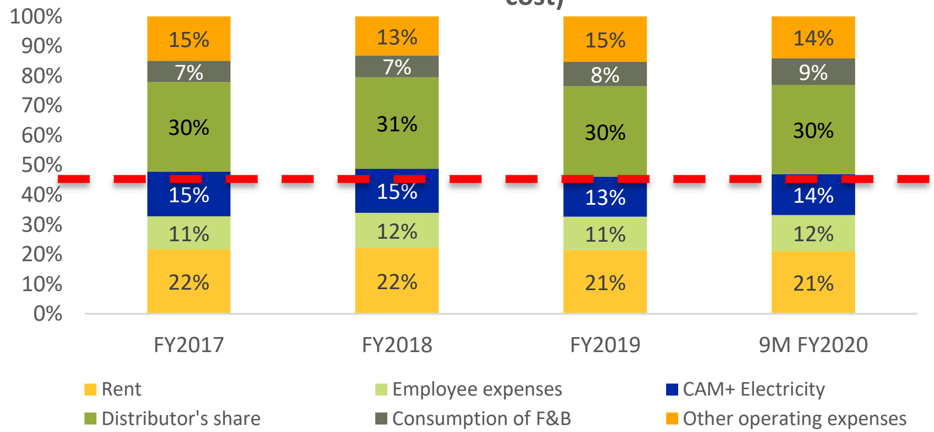


Exhibit 2: Key Cost Elements for Exhibitors (As % of total cost)



Source: ICRA research

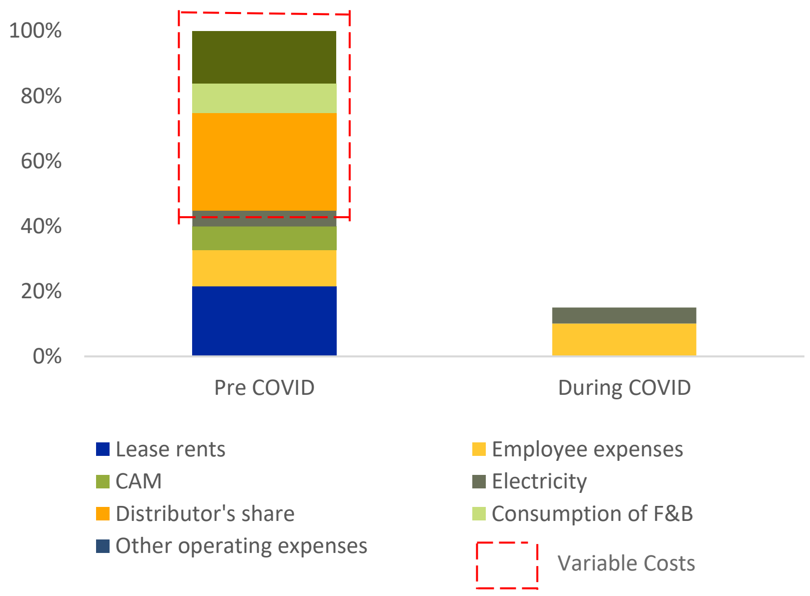
Closely linked with the prospects of the film exhibition industry are the digital equipment providers, who receive monthly lease rentals for the digital equipment provided to the exhibitors, share of advertisement revenues from the exhibitors for the contracted screens and virtual print fee (VPF) from the film producers on a per show basis. With the shutdown of theatres, the advertisement revenues and VPF income for these digital equipment providers have completely stopped, though the lease rentals (which comprise ~11% of the total revenues of digital equipment providers), would get offset against the minimum guarantee advertisement revenue sharing by the equipment providers.

Such shutdown of operations is thus a significant credit negative for the industry.

Measures taken to drive down costs

To minimise the impact on losses and cash outflows, most of the multiplexes have invoked force majeure clauses in their rental agreements, so that they do not have to pay rental and common area maintenance (CAM) charges during the period of lockdown. Furthermore, film exhibitors are attempting to make their cost structure variable to the extent possible by negotiating a variable rental structure with the mall owners, to manage their cash outflow, once the operations resume. Salary rationalisation and pay cuts have also been undertaken by exhibitors to manage their second largest fixed cost component. Discretionary repairs and maintenance and capital expenditure have also been deferred to H2 FY2021/FY2022 to conserve cash. Overall fixed expenses have been curtailed by an average by 2/3rd (of earlier levels) during the Covid-19 pandemic.

Exhibit 4: Reduction in costs of Film Exhibitors



Source: ICRA research

Outlook

Cinema halls were the first ones to shut down, even before the lockdown started, and are expected to be amongst the last segments to witness relaxations. ICRA expects this segment to witness a complete loss of revenues in Q1 FY2021. Even after the theatres resume operations post the lockdown, occupancy will remain sub-par as consumers stay away from crowded places. Low footfalls will translate into lower ticket sales and F&B revenues, which together constitute around 82-85% of the total revenues of an exhibitor. Corporate advertisement spends will also witness a decline, adversely impacting the advertisement revenues of film exhibitors. Overall, ICRA estimates a 60-65% YoY degrowth in revenues in FY2021 for the entities engaged in the film exhibition industry.

Furthermore, low footfalls once cinema halls resume operations will result in lower box-office collections, adversely impacting the revenues of film producers. Weak revenue prospects for film producers might also limit their ability to invest in new and niche content. However, amid shut-down of cinema halls, some producers are also opting for movie releases on OTT platforms, so as to monetise content.

Low footfalls, along with increased marketing and promotional spends (as exhibitors attempt to attract patrons to movie halls) and increased overheads as various social distancing norms become effective, are expected to constrain the operating profit margins of exhibitors.

Whereas lower box-office collections will impact the profit margins of the film producers. Sub-par occupancy will additionally impact return on capital employed (ROCE) of film exhibitors.

The key challenge for the exhibitors in the near-term is revival in consumer confidence, so that they feel safe and comfortable going to the cinemas, without any dilution in the overall movie watching experience. Besides, film producers releasing their films on OTT platforms also reduces the attractiveness of cinemas. For producers, the key near-term challenge is ramping up of the content pipeline and restarting the on-hold projects, which have been pushed back due to the pandemic.

ICRA expects the credit metrics for the film production and exhibition segments to weaken materially, though ICRA-rated portfolio has a healthy credit profile

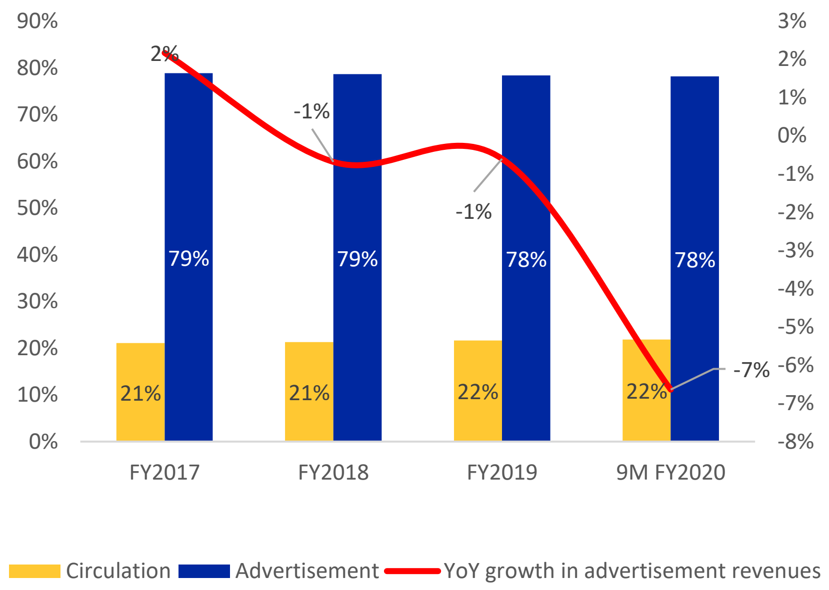
PRINT MEDIA SEGMENT

For the print segment, circulation revenues were adversely impacted by ~40% on YoY basis in April 2020, amid distribution challenges due to the on-going lockdown restrictions. Furthermore, advertisement revenues, which were already pressurised during FY2020 amid subdued economic conditions, declined by ~60-70% YoY in April 2020.

To control costs, companies are cutting back on the number of pages and merging supplements, to save on newsprint cost. Digital consumption of news has seen an upswing, with companies temporarily freeing up its subscription to maintain readership.

There has been an elongation of working capital cycle owing to delays in recovery of advertisement debtors, including government entities and an increase in receivable period for private clients by ~20 days.

Exhibit 5: Revenue Mix for Print Media Companies

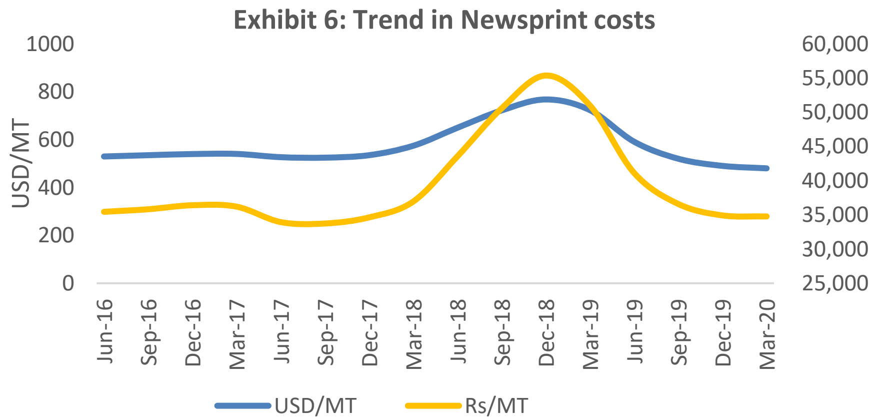


Source: ICRA research

Newsprint Costs

Newsprint cost represents the single largest cost component for print media companies, accounting for 40-45% of total cost. Around 60% of the newsprint consumed by the Indian print entities is imported. After peaking in Q3 FY2019 due to rise in demand of virgin pulp based newsprint in China, following the ban on import of waste paper, newsprint prices have started easing from Q4 FY2019 onwards. The price, as of March 2020, was down by 34% YoY to US$ 480/MT.

Currently, most of the companies have visibility of low-cost supplies for the next 5-6 months, which provides breather on the cost front. Import duty on newsprint has also been reduced to 5% in the Budget 2020 from earlier rate of 10%, though rupee depreciation could limit the benefits.



Source: ICRA research

Outlook

While circulation revenues will recover gradually in subsequent quarters as lockdown restrictions ease, advertisement revenues will witness a sharp contraction in FY2021. Expected longer demand revival in key advertising sectors including automobiles, real estate and consumer durables, will keep advertisement revenues in check. ICRA expects a 25-30% YoY degrowth in revenues of the entities engaged in the print media segment.

With ~78% of total revenues of this segment being contributed by advertisement, a decline in the same will adversely impact the profit margins of print media companies.

Retention of readership, amid difficulties in circulation is key challenge being faced by the print media segment, besides volatile newsprint costs. Furthermore, advertisement revenues also remain dependent on the pace of revival in the economy.

While credit metrics are expected to weaken, ICRA-rated entities have strong liquidity to weather the impact.

TELEVISION BROADCASTING SEGMENT

Subscription revenues, comprising 30% of the total revenues of TV broadcasters, are holding steady as consumers have increased their TV viewing (led by movies and news genre) during the lockdown.

Advertisement revenues have, however, been adversely impacted by 25-60% (vis-a-vis average monthly revenues) depending on genre in April 2020. While news and movies genre are on the lower end of the spectrum, with an average decline of 25-30% in advertisement revenues, general entertainment channels (GECs) and sports channels have witnessed a sharp 55-60% reduction in advertisement revenues in April 2020. This is in turn explained by the absence of fresh content (given the shutdowns and travelling restrictions) and deferment of high viewership driving sports events including the Indian Premier League (IPL), UEFA 2020, Olympics 2020, among others. Decline in advertisement revenues for segments like news and movies is on account of curtailed advertisement spends by sectors including automobiles, real estate and consumer durables.

There has been an elongation of working capital cycle of the TV broadcasters. There are delays in recovery of advertisement debtors, including government entities and an increase in receivable period for private clients by ~30 days

Exhibit 7: Revenue Mix for Television Broadcasters

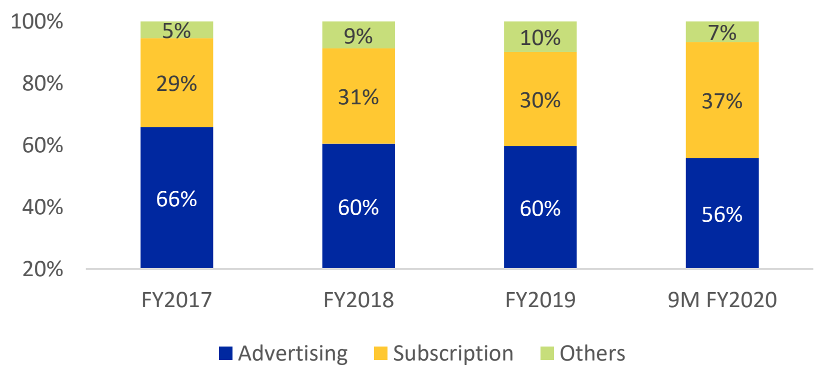


Exhibit 8: Decline in Advertisement revenues in April 2020

Source: ICRA research

Outlook

Subscription revenues for television broadcasters will hold steady as consumers are likely to continue their TV viewing during lockdown. However, in case of a prolonged economic slowdown, rationalisation in subscription spends cannot be ruled out, especially for low income groups, as cord-cutting increases in an adverse economic environment.

Advertisement revenues will witness a sharp contraction in H1 FY2021, though some recovery is expected in H2, as economic activity and growth resume. ICRA thus expects TV broadcasting industry to witness YoY degrowth of 18-25% in revenues in FY2021.

Since advertisement revenues account for more than 55% of revenues (and even 100% in case of free-to-air channels), decline in these, will adversely impact the revenues and profit margins of TV broadcasters, though cost-saving on fresh content creation (which accounts for ~35-40% of revenues) during the period of lockdown provides some respite.

Production of fresh content is a key challenge currently being faced by TV broadcasters. Given the shutdowns and travelling restrictions, the GECs are facing issues with programming and are relying on re-runs as pipeline of fresh content has dried up. Timely ramp up in fresh content remains critical for retention of subscriber base.

Overall ICRA expects a moderate impact on credit metrics of entities engaged in the TV broadcasting segment.

DISTRIBUTION PLATFORM OPERATORS (DPOS) SEGMENT

The impact of COVID-19 on the credit profile of DPOs has been limited as subscribers are holding on to their current subscription packages. New subscriber acquisitions have, however, been impacted as very few new installations are being carried out by DPOs, though the same is expected to resume once the lockdown restrictions ease. DPOs have also rationalised their costs towards call centre/customer service, to comply with the social distancing norms.

Collection efficiency for DPOs (barring small local cable operators) has improved during the current period, as subscribers are clearing the payments on time to maintain continuity in TV viewing. Increased proportion of online recharges has been observed, with reluctance towards cash transactions during the pandemic.

Outlook

Overall, revenues for DPOs will remain flat in FY2021, with range-bound operating profit margins, resulting in minimal impact on their credit metrics. Prolonged lack of fresh content may, however, increase subscriber churn towards DD Freedish.

OVER-THE-TOP (OTT) PLATFORMS

The current lock-down has led to a surge in consumption of OTT platforms, as consumers stay home. While earlier, OTT viewing was largely restricted to the commute time of the travellers, its consumption has spiked with people now staying indoors and also on weekends owing to lack of other avenues of entertainment.

While currently OTT platforms have an advertisement revenue dominated business model, the current crisis provides an opportunity to increase the proportion of paid subscription, led by the new habit formation of at-home OTT viewing. To attract new subscribers, OTT platforms are currently offering some of the premium (and paid content like first episodes of new series) free of cost.

Furthermore, with the shut-down of cinema halls and expected aversion to outdoor viewing of films, OTT (especially large platforms) are also being considered by the film producers for their film releases.

A shift in advertisers' preference towards online platforms (vis-a-vis linear platforms) is also expected as they attempt to garner more eyeballs and especially, after the deferments and cancellations of various sports programmes which were to be aired on linear TV.

OTT platforms however, face the risk of drying up of fresh and quality content. Platforms with large content library are thus better placed to ramp up subscribers during the current crisis.

ICRA, however, expects OTT to remain supplemental to TV viewing, given the relative high cost of wired interned (which has a penetration of only 8% as on September 2019) and high price OTT content vis-a-vis monthly cable/direct-to-home (DTH) prices in India.

ABOUT ICRA

ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange.

Alliance with Moody's Investors Service

The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder. The participation of Moody's is supported by a Technical Services Agreement, which entails Moody's providing certain high-value technical services to ICRA. Specifically, the agreement is aimed at benefiting ICRA's in-house research capabilities, and providing it with access to Moody's global research base. The agreement also envisages Moody's conducting regular training and business seminars for ICRA analysts on various subjects to help them better understand and manage concepts and issues relating to the development of the capital markets in India. Besides this formal training programme, the agreement provides for Moody's advising ICRA on Rating-products strategy, and the Ratings business in general.

The ICRA Factor

Our services are designed to

- Provide information and guidance to institutional and individual investors/creditors;
- Enhance the ability of borrowers/issuers to access the money market and the capital market for tapping a larger volume of resources from a wider range of the investing public;
- Assist the regulators in promoting transparency in the financial markets;

ICRA

Business Contacts

Mr. L. Shivakumar
E-mail: shivakumar@icraindia.com
Tel: +91 22 6114 3406 / +91 98210 86490

Mr. Jayanta Chatterjee
E-mail: jayantac@icraindia.com
Tel: +91 80 4332 6401/ +91 98450 22459

Media and Public Relations

Ms. Naznin Prodhani
E-mail: communications@icraindia.com
Tel: +91 124 4545 860

Registered Office:

1105, Kailash Building, 11th Floor,
26, Kasturba Gandhi Marg,
New Delhi - 110 001
Tel: + 91 11 2335 7940-45

Corporate Office:

Building No.8, 2nd Floor,
Tower A, DLF Cyber City Phase II,
Gurgaon- 122 002
Tel: +91 124 4545300

Ahmedabad

1809-1811, Shapath V,
Opposite Karnavati Club
S.G. Highway, Ahmedabad - 380015
Tel: +91 79 4027 1500/01

Bengaluru 1

'The Millenia', Tower- B, Unit No. 1004,
10th Floor,1 & 2 Murphy Road,
Bengaluru - 560 008
Tel: +91 80 4332 6400

Bengaluru 2

2nd Floor, Vayudooth Chamber,
15-16, Trinity Circle, M.G. Road,
Bengaluru - 560 001
Tel: +91 80 4922 5500

Chennai

5th Floor, Karumuttu Centre,
634, Anna Salai, Nandanam
Chennai - 600 035
Tel: +91 44 4596 4300

Hyderabad 1

No. 7-1-58, 301, 3rd Floor, 'CONCOURSE',
Above SBI-HPS Branch, Ameerpet,
Hyderabad - 500 016
Tel: +91 40 4920 0200

Hyderabad 2

4A, 4th Floor, SHOBHAN,
6-3-927, A&B Somajiguda,
Raj Bhavan Road,
Hyderabad – 500082
Tel: +91 40 40676500

Kolkata

A-10 & 11, 3rd Floor,
FMC Fortuna 234/3A,
A.J.C. Bose Road,
Kolkata -700 020
Tel: +91 33 7150 1100/01

Mumbai

3rd Floor, Electric Mansion
Appasaheb Marathe Marg,
Prabhadevi,
Mumbai - 400 025
Tel: +91 22 6169 3300

Pune

5A, 5th Floor, Symphony,
S. No. 210 CTS 3202 Range Hills Road,
Shivajinagar,Pune - 411 020
Tel: +91 20 2556 0194, 020 6606 9999

Email: info@icraindia.com
Helpdesk: 9354738909
Website: www.icra.in/ www.icraresearch.in