Dimensional Securities Pvt Ltd

Date: 13th April, 2020
CMP: 233
Recommendation: BUY
Target: 375

# Inox Leisure Ltd.

## Business Update

| MARKET DATA | |
|---|---|
| NSE TICKER | INOXLEISUR |
| Networth FY20E (Rs in Crs) | 1126.2 |
| P/BV Ratio (FY20) (x) | 2.2X |
| EPS (FY20E)(Rs.) | 13.3 |
| Market Price (Rs.) | 233 |
| P/E Ratio (TTM) (x) | 18.0 |
| 52 Week High (Rs) | 510 |
| 52 Week Low(Rs) | 233 |
| Market Capitalisation (rs. Cr) | 2662 |

| AVERAGE MONTHLY VOLUME ('000) | |
|---|---|
| BSE | 9.5 |
| NSE | 106.8 |

**SHARE HOLDING PATTERN**

| | |
|---|---|
| Promoter | 51.9 |
| FII | 11.3 |
| DII | 33.8 |
| Public | 9.5 |

| RETURN (%) | 3M | 6M | 12M |
|---|---|---|---|
| Inox | -31 | -20 | -17 |
| Nifty | -33 | -29 | -31 |

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### Assessing impact of Covid-19 lock down

On expected lines, the Malls and multiplexes were among the most impacted businesses on the back of Covid-19 lock down. Even before the nationwide lock down was announced on 24th March, 2020, many states had already announced shut downs of Multiplexes at least a week prior to that. In response to anticipated fall in foot falls even the film producers pushed back the release of their movies.

It is still not clear how and when the lock down would be lifted. But what we can make out from the various commentaries made by the Chief Ministers of the states and the recent meeting chaired by the PM, the lock will be lifted only gradually commencing from 14th of April. We believe that major metros and tier II cities might continue to remain under lock down, possibly for another fortnight. Even in the case of partial withdrawal of lock down, the pecking order will be to open up manufacturing, government offices, transportation and other places of necessities. The Government will not rush in to resume schools, malls, multiplexes and other place of discretion, and we believe it might take till June-July for these places to resume normal operations.

### Focus to be on reducing fixed costs

With the business coming to a screeching halt, the focus of Inox will be on reducing the fixed costs to as low as possible. That is the reason, that company decided to invoke *force majeure* clause with all of its developers. While some of the developers have agreed, some have rejected and many of the developers have come up with 50:50 burden-sharing formula. In all cases, we expect the rental costs to come down during the period of lock down. Company is also expected to cut down on manpower costs through reducing bonus and contracted personnel.

The fixed cost component for Inox for FY20E is as follows:

| Cost Heading | Annual (Rs. Cr) | Per Month |
|---|---|---|
| Rent | 362 | 30 |
| Employee Cost | 140 | 12 |
| Upkeep & Maintenance | 122 | 10 |
| Admin overheads | 163 | 14 |
| **Total Fixed Costs** | **787** | **66** |

- We believe that company would be able to negotiate it's rental costs which is a major portion of its total fixed cost.
- Besides that, by reducing contracted employees and wages it'll also be able to make some savings in employee cost.
- Upkeep and maintenance will also be lower since the screens would not be used.
- Thus, we believe that company can possibly bring down its fixed cost per month to ~Rs. 40-45 cr., which will translate into cash burn of Rs. 90-100 cr for closure of 2-2.5 months.

Inox has a strong balance sheet with net debt of only Rs. ~35 cr (D/E of 0.05X) and the company has availed line of credit for another Rs. 100 cr which should be enough to meet its need for next 2-3 months of lock down. The management in a recent call stated that it would strive to bring down its monthly fixed cost to as low as 35 cr.



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### While near-term headwinds persist, structural story stays intact

We acknowledge that the closure of multiplexes, expectedly for 2 months, will badly hit the financials of Inox Leisure. And this kind of event is unprecedented where the footfalls have literally gone down to zilch. But we take some comfort in the fact that Inox's balance sheet is strong enough to tide through current period of slow-down. We also believe that the structural story for multiplexes is still intact in India, and once the recovery sets in we expect the foot-falls to normalize by Sept-Oct 2020.

### Valuation and View

Given the above thesis, we continue to remain optimistic on Inox Leisure's prospects and accordingly recommend a BUY on the stock. We are valuing the company's share at Rs. 356 by assigning a multiple of 18.5X to its FY22 earnings of Rs. 19.2 (excluding Ind AS 116 impact). This represents a upside potential of 53% from the CMP of Rs. 233. We are using FY22's EPS because we believe that FY21's earnings are not 'normalized' and includes an aberration which we have never seen before, and hopefully, would never see again. We have however, reduced our earnings multiple from 20 to 18.5 given the near-term uncertainly clouding company's business.

### Financial Snapshot:

| Year End | Revenue | EBITDA | EBITDA % | PAT | RoE (%) | RoCE (%) | P/E |
|---|---|---|---|---|---|---|---|
| FY18 | 1692.4 | 309.3 | 18.3% | 139.4 | 16.5% | 20.1% | 18.1 |
| FY19 | 1869.3 | 308.0 | 16.5% | 130.6 | 12.7% | 16.8% | 19.4 |
| FY20E | 1826.4 | 268.3 | 14.7% | 101.7 | 8.9% | 10.6% | 24.9 |
| FY21E | 2230.5 | 387.5 | 17.4% | 188.4 | 14.6% | 17.1% | 13.4 |

### About Company

Incorporated in 1999, INOX Leisure Limited is one of the largest multiplex operators in India promoted by Gujarat Fluorochemicals Ltd. The Company is a part of INOX Group, which is diversified across industrial gases, engineering plastics, refrigerants, chemicals, cryogenic engineering, renewable energy, and the entertainment sectors. Over the last decade, INOX has aggressively scaled up its presence through organic and inorganic expansion, growing from 2 properties with 8 screens in FY03 to 141 properties with over 600 screens as on date.

**Our investment rationale is as follows:**

**Improvement in business mix to bring more stability in revenues and margins**

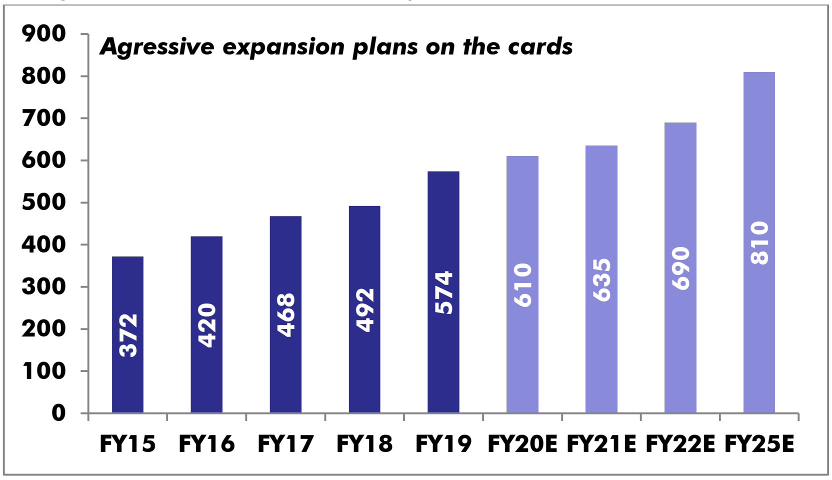
Over the last 5 years, Inox's revenue mix has changed favourably towards high margin F&B and ad income, leading to better profitability and stability in revenues. The combined share of F&B and ad revenues has increased from 23.5% to 36% from FY13 to 9MFY20. While the ad spends will hit a bump in FY21, owning to slowdown in discretionary spends and correspondingly ad spends by major players, we continue to remain optimistic about sustainability of this traction beyond FY21 and expect F&B and ad revenue growth to outpace screen addition.

- With the Television space losing market share and many single screens getting closed, the multiplexes are able to attract advertisers because of its targeted approach.
- High conversion ratio (patrons spending on F&B/total patrons going to watch the movie) and increasing spend per heads will drive F&B revenues. Focus will be on volume growth even if it loses few bps on gross margin.
- On ad sales, the focus will be on improving both; volume (increasing advertisement minutes per show) as well as realizations. Screen addition will provide scale to the company which it can leverage for getting higher realizations as its reach increases.

| Inox - Revenue mix | FY13 | FY16 | FY19 | FY20 | FY21E | FY22E |
|---|---|---|---|---|---|---|
| Net Box Office | 70.0% | 61.4% | 57.6% | 58.5% | 57.7% | 58.6% |
| F&B | 19.0% | 22.9% | 25.8% | 25.9% | 25.5% | 26.3% |
| Ad Revenues | 4.5% | 7.8% | 10.4% | 9.8% | 10.6% | 9.8% |
| Other | 6.5% | 7.8% | 6.2% | 5.8% | 6.2% | 5.3% |

**Screen addition on strong footing, aggressive expansion on the cards**

While the company will miss guidelines of 70-80 screen additions in FY20 owing to expected slow-down due to Covid-19 related lock down, the multi-year screen addition pipeline continues to remain intact. Company has laid out pipe line to add another 800-850 screens over the next 5-7 years. Most of the incremental screens will be in the newer market where their presence is relatively low. This will increase company's target market audience and also diversify their regional mix which is currently largely west focussed. And given the current period of slow-down, company could also get a better deal from its developers.




**Industry dynamics changing in the favour of multiplexes:**

***Spurt in urban middle class:*** The number of upper middle-class households (income above Rs. 600,000 p.a.), which drives the consumption of premium and semi-luxurious goods/services, is expected grow nearly 3 fold from 6.1 cr to 16.8 cr (16.8 cr households implies ~67 cr people). Moreover, even the upper crust of lower middle-income households (income between than Rs. 400,000-Rs. 600,000) is expected to grow by 36% to 13.2 cr (~53 cr people) in next decade. This implies that Inox's target market size will grow from current 9.4 cr households to 30.2 cr households.

The discretionary spend in India is going to see a surge on the back of following factors:

- Increase in the number of youth in the work force (aspirational class) whose willingness to spend is much higher than what it was 5-10 years back.
- Growth in urbanization and semi-urbanization.
- Rising income and evolving life-style.

***Going for a movie can be the cheapest outing for a family in India.***

Average cost for a family of four for different entertainment options.

| | **Cinema (Multiplex)** | **Theme park** | **Sporting event** |
|---|---|---|---|
| Entry Fees (incl GST) | Rs. 600-800 | Rs. 4000-6000 | Rs. 2500-5000 |
| F&B | Rs. 300-400 | Rs. 400-600 | Rs. 400-600 |
| Conveyance | Rs. 50 | Rs. 300-400 | Rs. 200-300 |
| **Total Cost** | **Rs. 950-1200** | **Rs. 3900-5800** | **Rs. 3100-5900** |

*(Source: Inox Leisure, Industry research)*

Thus, at a cost of Rs. 1000-1300, a movie outing can be the most affordable entertainment option for an entire family in India. Given large proportion of middle-class households, theatres should continue to attract larger audience.

**Number of visitors annually (in mns) (FY19)**

| **Cinema** | **Theme Parks** | **Sports Event** |
|---|---|---|
| **190 mn** | **30 mn** | **10-15 mn** |

(Source: KPMG, Inox Leisure, Industry research)

This gets vindicated from the current scenario where consumption has slowed down across sectors but spending on movies has remained largely unaffected;

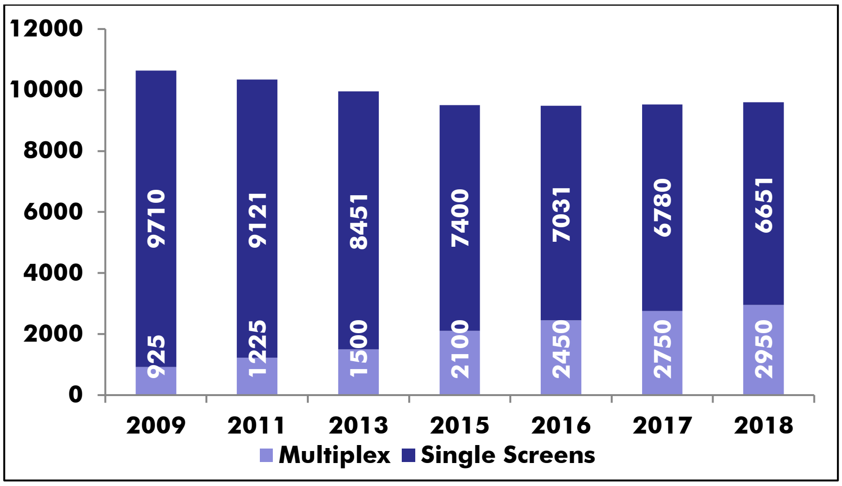
- The auto industry saw sixth straight month of negative sales.
- Air passenger traffic growth slowed down to -5% to 3% from high double digit growth before that.
- SSSG for QSRs have slowed down to 4-6% compared to 14-16% in previous 6 quarters.
- In this scenario, the number of movies earning Rs. 100 cr+ has grown 2x in last three quarters before the lockdown.

**OTT vs Theatre- Not exactly a risk to film exhibitors:** There are concerns that OTT will impact business of film exhibitors because producers might skip their film from exhibition and release them directly on OTT platform. However, the economics doesn't support these theses. For instance, Netflix bought 'exclusive' rights of 2018 super-hit Padmaavat for Rs. 20-25 cr whose Net BO collection 190 cr and Netflix bought Baahubali 2's rights for similar amount whose Net BO collection was Rs. 600 cr+. Thus, the money which a producer makes in theatricals is significantly higher (with more upside potential) compared to what it can make by selling to OTT.

Even for OTT there is a trade-off between spending for acquiring rights of a movie and creating its own content. 'Sacred Games' which received tremendous response on Netflix is estimated to have been made at a budget of Rs. 80 cr while Mirzapur was made at 35-40cr. Therefore, an OTT platform would rather be willing to create new content, over which it has a control, instead of spending lavishly on buying a movie rights over which they don't have much control. For example, Netflix paid big amount (sum undisclosed) for acquiring rights of 'Thugs of Hindustan' which turned out to be an extremely poor content.

Another thing when it comes to film exhibition, as discussed above, is that it is viewed as a family or friends' outing. There is a sense of experience attached to it which one can get only in a theatre hall. OTT is more of a leisure activity which one would resort to on his weekends or while commutation. Going for a movie in a theatre is a 2-3 time activity, which we don't think will get impacted by OTT. We'd place OTT as an add-on content consumption that people turn to 'escape' from their routine.

**Shift in market share from single screen to multiplexes:** Over the last decade, the film industry has changed significantly on technology front in every aspect of movie screening; shift towards digital print, Dolby and Atmos audio, online and computerised ticket booking, etc. Movie-going has become more of an experience than just a simple viewing for entertainment. It is because of these factors, that the multiplexes started to flourish across India. Due to their scale and adaption of technology, it became simpler and cheaper for producers to screen movies digitally compared to physical prints. Because single screen finds it difficult and unfeasible to adopt these new systems of film exhibition, they are seeing rapid shutdowns while multiplexes are gaining market share. When compared globally, the screen density ratio is lowest in India with 2 screen per million people, while the number stands at ~37 for China.




| Countries | Screen per mn |
|---|---|
| USA | 125 |
| UK | 60 |
| China | 37 |
| Brazil | 16 |
| India | 2 |

### Valuation & View

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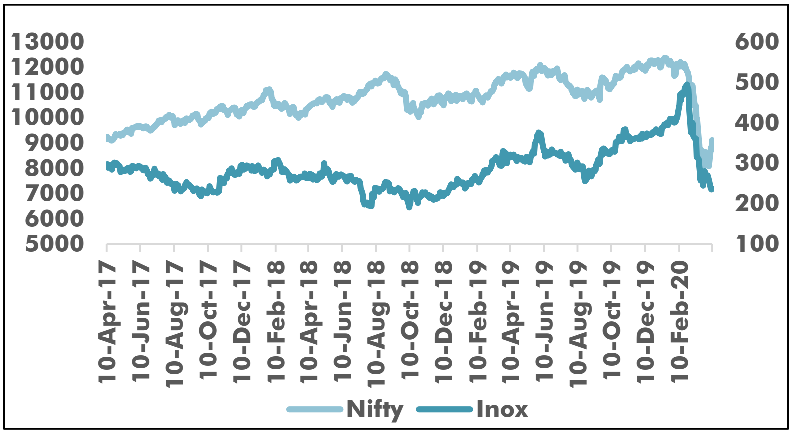
## ➢ Risks & Concerns:

- Lack/Uncertainty of content: A large chunk of the box office collection is driven because of recurring flow of strong content. Therefore, slowdown in new content or lack of good content can have a significant impact on company's revenues. Since last two years, the multiplexes have seen string of releases earning 100-300 cr at box office. To sustain the current trend of earnings, we'll need incremental big movies every year.

- The above risk has multiplier impact since lower footfalls will also translate into lower F&B and ad revenues which will have larger impact on the margins as well.

- Extension of lock down beyond 2 months. Our forecast has been made keeping in mind lockdown for 8-10 weeks. If it extends beyond that, then there will be significant divergence in company's performance from our estimates and it might also lead to further deterioration in company's balance sheet.

- Slowdown in mall construction: Majority of the multiplexes are set up in the malls and most of the company's upcoming screens are also planned in a mall. Weak sentiment in the economy could lead to muted growth in the commercial property market, impacting mall development.



## Financials (Excludes impact of Ind AS 116):

| Inox Leisure Ltd. - Statement of Profit & Loss | | | | | |
|---|---|---|---|---|---|
| **DESCRIPTION** | **FY18** | **FY19** | **FY20E** | **FY21E** | **FY22E** |
| **Net Revenue** | **1348.0** | **1692.4** | **1869.3** | **1826.4** | **2230.5** |
| EXPENDITURE : | | | | | |
| F&B Cost | 74.4 | 112.5 | 125.9 | 122.9 | 153.3 |
| *as % of Sales* | | | | | |
| Power & Fuel Cost | 95.3 | 109.7 | 124.8 | 134.8 | 147.0 |
| Employee Cost | 96.4 | 115.1 | 139.5 | 149.2 | 165.9 |
| Distributor's share | 361.2 | 444.2 | 498.7 | 481.3 | 593.3 |
| Rent Expense | 264.2 | 312.6 | 361.6 | 359.8 | 438.6 |
| Other Operating & Admin Exp | 223.8 | 258.5 | 284.6 | 284.6 | 309.2 |
| S&D Overheads | 22.4 | 30.5 | 26.2 | 25.6 | 35.7 |
| **Total Expenditure** | **1137.7** | **1383.1** | **1561.3** | **1558.1** | **1843.0** |
| **EBITDA (Ex OI)** | **210.3** | **309.3** | **308.0** | **268.3** | **387.5** |
| *EBITDA Margin* | *15.6%* | *18.3%* | *16.5%* | *14.7%* | *17.4%* |
| Depreciation | 89.8 | 95.5 | 111.5 | 127.1 | 144.4 |
| **EBIT** | **120.5** | **213.8** | **196.5** | **141.2** | **243.2** |
| Other Income | 15.0 | 14.9 | 12.9 | 15.0 | 19.4 |
| Interest | 29.5 | 23.7 | 9.9 | 11.0 | 2.8 |
| **Profit Before Taxation** | **106.1** | **205.0** | **199.4** | **145.2** | **259.8** |
| Provision for Tax | -17.0 | 65.6 | 68.8 | 43.6 | 71.4 |
| **Profit After Tax** | **123.1** | **139.4** | **130.6** | **101.7** | **188.4** |
| **Adjusted EPS** | **12.5** | **13.7** | **13.3** | **10.4** | **19.2** |

| Everest Industries- Balance Sheet | | | | | |
|---|---|---|---|---|---|
| **DESCRIPTION** | **FY18** | **FY19** | **FY20E** | **FY21E** | **FY22E** |
| Share Capital (Net of Treasury) | 63.6 | 70.2 | 70.2 | 70.2 | 70.2 |
| Total Reserves | 604.3 | 893.9 | 1024.5 | 1126.2 | 1314.6 |
| **Shareholder's Funds** | **667.8** | **964.1** | **1094.7** | **1196.4** | **1384.8** |
| | | | | | |
| Total Borrowings | 291.9 | 84.1 | 58.5 | 45.7 | 12.6 |
| Other Non Current Liabilities | 7.8 | 37.8 | 45.5 | 43.2 | 64.8 |
| **Total Non-Current Liabilities** | **299.7** | **121.9** | **104.0** | **88.9** | **77.4** |
| | | | | | |
| Trade Payables | 113.2 | 159.6 | 131.7 | 130.3 | 146.0 |
| Other Current Liabilities | 121.4 | 180.7 | 199.6 | 195.0 | 238.2 |
| **Total Current Liabilities** | **234.6** | **340.3** | **331.3** | **325.3** | **384.1** |
| **Total Liabilities** | **1202.1** | **1426.3** | **1530.0** | **1610.6** | **1846.3** |
| | | | | | |
| Fixed Assets | 825.7 | 985.6 | 1073.4 | 1069.5 | 1160.1 |
| Other Non Current Assets | 233.1 | 289.5 | 319.8 | 399.7 | 487.6 |
| **Total Non-Current Assets** | **1058.8** | **1275.1** | **1393.1** | **1469.2** | **1647.8** |
| | | | | | |
| Current Investments | 12.4 | 0.6 | 0.7 | 0.6 | 30.0 |
| Inventories | 9.4 | 12.2 | 12.0 | 11.8 | 14.8 |
| Sundry Debtors | 76.1 | 88.2 | 75.8 | 77.5 | 90.4 |
| Cash and Bank | 15.0 | 13.7 | 8.0 | 12.0 | 12.0 |
| Other Current Assets | 30.5 | 36.6 | 40.4 | 39.5 | 51.3 |
| Total Current Assets | **143.4** | **151.3** | **136.9** | **141.4** | **198.5** |
| **Total Assets** | **1202.3** | **1426.4** | **1530.0** | **1610.6** | **1846.3** |



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| Inox Leisure Ltd. - Cash Flow Summary | | | | | |
|---|---|---|---|---|---|
| **DESCRIPTION** | **FY18** | **FY19** | **FY20E** | **FY21E** | **FY21E** |
| PAT (ex OI) | 73.4 | 124.5 | 117.8 | 86.6 | 169.0 |
| Add: Depreciation | 89.8 | 95.5 | 111.5 | 127.1 | 144.4 |
| Change in WC | 10.5 | 42.0 | -21.1 | -88.8 | -64.5 |
| **Cash From Operating Activities** | **173.7** | **261.9** | **208.2** | **125.0** | **248.8** |
| **Cash from Investing Activities** | **-160.9** | **-218.1** | **-199.3** | **-123.2** | **-235.0** |
| **Free Cash Flows** | **12.8** | **43.8** | **8.9** | **1.8** | **13.8** |
| **Cash from Financing Activities** | **-11.0** | **-47.1** | **-12.7** | **2.2** | **-13.8** |
| Net changes In Cash | **1.8** | **-3.2** | **-3.8** | **4.0** | **0.0** |
| Opening Cash Balance | 13.2 | 15.0 | 11.8 | 8.0 | 12.0 |
| **Closing Cash Balance** | **15.0** | **11.8** | **8.0** | **12.0** | **12.0** |

| Inox Leisure Ltd. - Key Ratios | | | | | |
|---|---|---|---|---|---|
| **DESCRIPTION** | **FY18** | **FY19** | **FY20E** | **FY21E** | **FY22E** |
| EBITDAM (%) | 15.6% | 18.3% | 16.5% | 14.7% | 17.4% |
| ROE (%) | 18.8% | 16.5% | 12.7% | 8.9% | 14.6% |
| ROCE (%) | 11.7% | 20.1% | 16.8% | 10.6% | 17.1% |
| Receivable days | 17 | 16 | 15 | 15 | 14 |
| Inventory Days | NA | NA | NA | NA | NA |
| Payable days | 46 | 43 | 43 | 43 | 40 |
| Total Debt/Equity(x) | 0.4 | 0.1 | 0.1 | 0.0 | 0.0 |
| Current Ratio(x) | 0.6 | 0.4 | 0.4 | 0.4 | 0.5 |
| Interest Cover(x) | 4.1 | 9.0 | 19.8 | 12.9 | 88.1 |
| Adjusted P/E Ratio | 19.2 | 17.5 | 18.0 | 23.2 | 12.5 |
| Price/ Book value | 3.3 | 2.4 | 2.2 | 2.0 | 1.7 |

## ANALYST CERTIFICATION

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