



“Videocon D2H Limited Q2 FY17 Earnings Conference Call”

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Moderator: Ladies and Gentlemen, Good Day and Welcome to the Videocon D2H Limited Q2 FY17 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing ‘*’ then ‘0’ on your touchtone phone. I now hand the conference over to Ms. Nupur Agarwal, Head of Investor Relations. Thank you and over to you ma'am.

Nupur Agarwal: Good morning and welcome everyone to Videocon D2H's Q2 fiscal 17 results conference call. We have with us senior management of the company represented by Mr. Saurabh Dhoot – Executive Chairman; Mr. Anil Khera – the CEO; Mr. Rohit Jain – Deputy CEO and Mr. Avanti Kanthaliya – the CFO. I would now hand over the call to Mr. Dhoot for his opening remarks.

Saurabh Dhoot: Thank you all for joining our results call for the quarter ended September 30th 2016. On behalf of our board members and the management team, I welcome you all. I also take this opportunity to wish you a very Happy and Prosperous Diwali. Diwali is the biggest festival of India and it is towards the end of this week. In fact, it is the time of the year when consumer spending is at its peak similar to Christmas in the U.S. So hence on that note, as you will be following that very closely, let me share the results for Q2 FY17.

I am pleased to report that our EBITDA grew 37%; this is in spite of expected increase in service tax which would impact ARPU. Net subscribers increased by 230,000 in line with a guidance of 225,000 and net subscribers today totaled more than 12.52 million. The company has added almost 0.6 million gross subscribers. Revenue from operations came in at INR 7.76 billion, this is after adjusting for the change in accounting treatment of entertainment tax to bring it in line with industry practice. Rohit will explain this in more detail later.

On an apple-to-apple basis, from operations revenue for Q2 FY17 would have come in at INR 8.32 billion, that is up 20.6% year-on-year. Subscription and activation revenue came in at INR 7.11 billion. On an apple-to-apple comparison, subscription and activation revenue would have come in at INR 7.67 billion. That is 21.9% year-on-year growth. Adjusted EBITDA grew 37.3% year-on-year to INR 2.63 billion. This is in spite of the expected increase in service tax and it is ahead of our guidance of INR 2.6 billion.

One of the things in fact I am most proud of that adjusted EBITDA margins came in at 33.8% during the quarter that is 380 basis points, up year-on-year on an apple-to-apple comparison. We have achieved a PAT of INR 148 million and free cash flows of INR 199 million in this quarter. As you can see from this quarter's results, it reflects really on our strategic imperatives. They will continue to be very important especially in light of the significant growth opportunity in form of Phase-IV digitization.

Firstly, working on Phase-IV ambitions with our efforts over the past few quarters, we now boast an unparalleled distribution network of over 230,000 retailers that support our Pan India brand. This has really helped by our extensive marketing efforts and strong partnership associations and ground work done by our salesforce in the last 2 quarters in preparation for Phase-IV. Our superior customer service continues to drive revenues, most of you all know that we are the only pay-tv operator with the captive service infrastructure network unrivaled by many and this clearly gives us the best installation, and repair turnaround times in the industry. This track record and brand support which we have from this service deliverables is really helping us keep churn suspension controlled and really supporting our gain in market leadership in Phase-IV, Phase-III markets.

For our consumer facing business, we believe in localization by adding more regional and local channels and premiumization in terms of our HD offering. This third aspect, focus on content is continues to be very important and for Phase-III and Phase-IV markets with the kind of bandwidth the technology and the proprietary content we have to fill in gaps, we really have a lot more to offer and lot more under plans to offer for regional markets and regional content. We have in fact taken a massive HD channel expansion especially in the last quarter and also other channels and especially regional channels in this quarter which we have already launched and these are going to be margin accretive even in Phase-IV and Phase-III markets. We continue to lead the market in technological innovations and this is always going to play a very long role in creating great shareholder value.

Lastly, the DNA of the organization and focus in execution is such that we continue to enhance operational efficiencies and improve overall margins. You can clearly see that from the incredible margin improvement in the quarter. Few quarters back, we told you we would achieve EBITDA margins over 30%. I am happy to share that the team has got it done.

On a different matter, regulator TRAI released the first draft of a comprehensive new tariff order. This covers content pricing guidelines for distribution of content from broadcasters through distribution platforms and from platforms to the end customer. Well, I will ask Mr. Khera to talk about this in much more detail. I believe the regulator has worked really hard to protect the interest of consumers. As we have discussed in the past, there is significant difference in what DTH industry pays for content as compared to cable. In fact, adjusted for carriage revenues, the DTH industry has been paying a lot more than cable. The origination of this tariff order is to create complete transparency and have a level playing field in commercial parity among distribution platforms especially cable and DTH. Clearly this order being the first draft will be trashed out overtime, will have its own challenges and implementation process, but we will monitor this closely and keep you updated.

Coming onto guidance, with the strong macro outlook favoring us, I am excited that I can give a guidance for the quarter ended December 2016, Q3 FY17. We expect net subscriber addition of 400,000 in Q3 FY17. We expect EBITDA to grow 34% year-on-year to Rs. 2.68 billion in Q3 FY17. We continue to maintain our overall guidance for fiscal 2017 which is to be PAT

and free cash flow positive for the year. This is assuming gross subscriber base addition of at least 2.5 million in the current fiscal of course.

Thank you. With that, let me hand over the call to Mr. Khera for to give us an industry and business update.

Anil Khera:

Thank you, Mr. Saurabh Dhoot. We are pleased to share that during the quarter, the must talked about and awaited GST bill was introduced in the upper house and the amendments required to the current proposed bill were discussed and got approved. This was a significant development on GST front and the legislation process moved one step forward. There was no new information on the GST rate or the implementation process or timeline provided at that time. The government aims to progress on GST bill during the current fiscal year with a view to implement GST starting April 2017. The GST bill is likely to be tabled in Parliament for final approval during the winter season that starts in November. This would include final details of the GST bill such as tax rate. This is a significant development for DTH industry and for the country. The last year, a panel headed by Chief Economic Advisor recommended a GST rate of around 18%. GST is also likely to subsume other form of indirect tax such as entertainment tax. If this rate gets implemented, we could see margin improvement to the tune of 300-400 basis points. Moreover, GST reforms aim to improve ease of doing business in India by simplifying the tax structure. This is an important legislative step and we welcome this approval.

Talking about the tariff order; as Mr. Saurabh Dhoot mentioned, earlier this month the regulator released a Comprehensive Tariff Order. This is a draft tariff order and TRAI, which is the regulator, has asked all the stakeholders to give their views by November 14, 2016. We expect the final tariff order to come in the current fiscal year as the regulator seems keen to implement this starting April 2017. The draft regulation proposes that the distribution platforms on a fixed distribution fee and an additional capacity fee depending on number of channels carried and a commission for pay channel distributed by the platform service providers. In essence, the content cost most likely may become a pass-through expense and the discount on channel pricing from the broadcasters will be regulated. The primary objective of this tariff order is to bring transparency and commercial parity in content deals with distribution platforms such as DTH and cables. This could also imply that cable will no longer be able to underprice its products to the end consumer. We are currently very carefully reviewing all aspects of the tariff order and need some clarification from the regulators.

As Mr. Saurabh Dhoot highlighted in his opening remarks, we at Videocon D2H are extremely committed to enhancing revenue realization through a differentiated content offering. Keeping in line with our focus on premium product offering, during the past few months we added 15 high definition channels to our platform, besides addition of 8 to 10 standard definition channels, taking the total high definition channel count to 60 high definition channels and services. The channels are from wide genre with specific focus on regional languages in various large states including Maharashtra, West Bengal and Tamil Nadu. We are targeting to

add many more high definition channels to our platform in near future. This will strengthen our premium bouquet offering in sports, Hindi and regional languages keeping in line with the trend of regional high definition channels getting more viewership. We are confident that this will further strengthen our high definition market share.

Lastly, the government seems turn on deadlines of Phase-IV digitization which is 31st December 2016. This is a huge opportunity ahead of the industry, as we believe there are 45 to 50 million analog cable homes covered in this phase. Having said this, I would like to emphasize that DTH industry continues to grow its subscriber base regardless of digitization implementation; however, digitization helped to us improve the timing of this subscriber additions. The higher transparency in subscriber reporting due to successful completion of digitization Phase-I, II and III and with the deadline for Phase-IV digitization nearing the analog cable will no longer be able to underprice its product to the end consumer, creating a room for ARPU growth in the years to come.

I now hand over to Mr. Rohit Jain for the financial update.

Rohit Jain:

Thank you, Mr. Khera. Before we go into the details of the results, we wanted to highlight about the tax change Mr. Saurabh Dhoot talked about. We have implemented a small change in the reporting mechanism, some of you might have already seen this in the 6-K filing we have done some time back. We have started netting off entertainment tax on the revenue line. This was previously reported under operating expense. This change has been implemented to adopt what is becoming widely an industry practice now and also to prepare for GST arrival given that the assumption is GST will subsume entertainment tax as well. This would lead into some optical change for metric such as ARPU and content cost as a percentage of revenue. We had provided pro forma metrics for the last 6 quarters along with the results for ease of analysis. This is available in our investor presentation which you will find on our corporate website. In addition to that, we have also started reporting ARPU on total revenue basis. This is primarily done to incorporate investor feedback that we have received consistently to make it easier for them to be able to calculate ARPU.

With that, going into details of the results, the total revenue for the quarter came in at INR 7.76 billion, key components being, subscription and activation came in at INR 7.11 billion, carriage revenue came in at INR 258 million. This is almost a 32% growth from last year and ad revenue came in at INR 82 million. Q2 FY17 adjusted EBITDA grew 37.3% year-on-year to 2.63 billion. Adjusted EBITDA margin came in at 33.8% for the quarter. On a like-to-like basis, margin would have been 31.5% which is 380 basis points up year-on-year. Content cost came in at 38.7% of revenue; this is a 200 basis point improvement over last year. Fixed cost as a percentage of revenue came in at 15%, an improvement of 160 basis points over last year.

We are excited continuing a theme of profitability. We are reporting a net profit of INR 148 million compared to a net loss of INR 246 million during the same quarter last year. ARPU, which is now as we said on total revenue, came in at Rs. 209. This is 5.4% growth over last

year. As the old definition, this would have come in at Rs. 216 just for the analysis purpose. This is obviously in spite of the fact that there was half a percent impact on account of increase in service tax that the company was aware of that something government has announced couple of quarters back.

Monthly churn for the last 6 months came in at 0.72%, this is compared to 0.82% for the 6 months last year. Hardware subsidies came in at INR 1,869 per subscriber. The CAPEX for Q2 FY17 was 1.72 billion, adjusted EBITDA less CAPEX came in at INR 907 million. During the quarter as we had shared last time as well, we paid down term loans amounting to INR 2.75 billion further. As of now, we have term loans of INR 19.12 billion and total cash and short term investments of INR 3.76 billion.

We are excited the results are in line with our overall strategy of improving efficiency and margin enhancement. To conclude, our net subscriber addition came in at 230K as against the guidance of 225K and EBITDA came in at INR 2.63 billion as against INR 2.6 billion.

With this, we conclude our opening remarks. We open the floor for questions now.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. We will take the first question from the line of John Rodrigues, Individual Investor. Please go ahead.

John Rodrigues: I just wanted to ask the questions about, what is the plan relating to the progress on debt refinancing?

Saurabh Dhoot: As you aware in the H1 of this year, there has already been a substantial reduction in gross debt but other than that, I believe you are talking about cost of debt enhancement. So on that point, we currently have a net debt of INR 15.36 billion that has highest interest rate of around 13% plus, which we all feel is high compared to the quality of our balance sheet. So, we have evaluated different avenues to refinance debt with the aim to lower interest cost. We also recently with the new regulations by the RBI and the new investor appetite coming in from masala bonds, given the nature of our requirement and the regulatory aspects in India, we are currently evaluating a masala bond and in the process of appointing bankers for a masala bond issue, the board has already given a resolution to that fact. So, in fact that seems like the most efficient way to refinance the domestic debt and naturally it will unlock and come in at a cost far better than what we are paying right now. So I think that, we will be working on this solution.

Moderator: Thank you. The next question is from Peter Okin from Stifel Nicolaus. Please go ahead.

Peter Okin: I have a question. In July, you put up good numbers, your stock was at \$9 in the US, it advanced a little bit and now with this quarter you put another quarter out, very good quarter. I think you start trades, at about 7 times EBITDA, you are growing at over 30%, seems like the

valuation here at \$8.47 cents is very low. I would like to know what you think about the results you are putting up versus the valuation you are seeing in the market and what the company plans to do about it, because in your press release, I see Mr. Dhoot mentioned these imperatives doing are driving our success creating sustainable shareholder value. I am just not seeing the shareholder value here and I was wondering, are you frustrated by that and based on that, you think it is going to take consolidation in the industry in India and if you do think it is consolidation, when you first see that consolidation starting to happen?

Saurabh Dhoot:

Thank you, Peter. I share and empathize with the disappointment that you and us and a lot of investors would feel, considering as you rightly pointed out the performance of the company with regards to the current multiple which is presently there on our stock. At the outset, I am sure as we continue to deliver strong growth quarter-on-quarter, short-term technicalities, and I will call them short-term technicalities, will solve for themselves and our stock price is bound to mirror our growth. It is bound to mirror the fundamentals which market has given in this entire sector for Indian media companies having this in this sector in India at around almost 10 times forward earnings for host of media companies in India and I believe that it will follow this performance and the share price will definitely reflect that. We are also planning US road show in mid to end November, normally we would have traveled immediately after result, but we are reporting results just before Diwali, hence the delay and the board has already constituted an IPO committee to look at an Indian listing as well, as this is the home market and it is consistent with a strategy of having a listing in home market as well. Naturally, we feel there are lot of avenues which are there, which we can work on other than just purely consolidation. Consolidation is a different matter; I have already spoken on that. In the past that we believe in the industrial logic of consolidation for sure, but what I am saying here that fundamentally even purely on the basis of existing market metrics, we believe that our communication and our performance will reflect on the stock based on the existing benchmarks in the Indian stock market. Thank you.

Peter Okin:

Do you feel your current valuation is too low? The stock does not trade based on the numbers you are putting up. So how long do you think it will take for the markets to realize that and it seems that it has been a long road, would you work on consolidation in the near term, what we decide as an investor that has been out here for year and a half, seeing you guys put up great numbers but not getting justified in the market place, something might need to change.

Saurabh Dhoot:

Yes, like I said, I agree with you, the fundamental value does not get reflected on the stock to date at the price on which you trade right now. As you can see on the basis of the trading, you can clearly see that these are short-term technical aspects probably related to that. People have given me feedback related to having more research coverage which we have also worked on in the US. And I believe that this quarter-on-quarter growth, we are attracting new investors on almost weekly basis. We are going to have a communication program with our shareholders in the end of November. What I am saying is that I believe lot of these measures would address this, bring it in line with what the market benchmarks are already there for Indian media companies which are listed in India and that couple of turns higher at what we are trading right

now on the platform and I believe that shortly we will have that result. As far as consolidation, I have already told you that we have always encouraged consolidation, we believe in consolidation in the industry. I believe the industrial logic is significant when you have 25-30 million subscribers on a platform, the kind of scale benefits and the advantages and the synergies are significant, highly value accretive, but that value is beyond the fundamental value of our business which anyway is discounted today. So naturally that will be further accretive, but on a standalone basis today itself there is a significant opportunity in the stock today and it will reflect that.

Moderator: Thank you. We have the next question from Thomas Claugus from Ampla Capital. Please go ahead.

Thomas Claugus: The entertainment tax was moved from an expense to netting it out of the revenue and what I was asking was, did the entertainment tax rate that you guys used change at all, or it just moved from one area of the income statement to netting off the revenue or did the rate actually change, that is what I am trying to understand?

Rohit Jain: No, it just simply moved from an expense item to netting off that is the only change as far as entertainment tax is concerned. Like I said, lot of place you would notice in the industry had moved in the direction, largely this is also preparedness for sort of moving into the GST system at some point, but it is just change of clubbing as far as entertainment tax is concerned.

Thomas Claugus: And then just last question on this, what is the chance that the rate goes up or down or stays where you guys have calculated because I guess you guys believe the government is charging more than what you guys calculate and then as per this new draft resolution, what is the outlook on entertainment tax going forward or what it looks like as of today just if you can give us clear picture please?

Rohit Jain: So as of today, entertainment tax varies, it is a state subject. In various states, the rates and the calculation differs. And there are times it can vary a little bit depending upon what various changes might happen, but naturally what is expected is once GST comes in, one believes in sometime in 2018-19, the government of India is obviously aiming for 2017. In that case, whole entertainment tax variance goes away and all of it gets subsumed into one common rate of taxation. What that common rate of taxation is going to be, is not finalized by the government as of now. As Mr. Khera said on the call earlier, various economic advices have come up with the rate of 18%; however, the committee needs to deliberate on that and finalize it, so it is not something that we know as of today but once that happens, this completely goes away.

Thomas Claugus: In that case 18% is better than what you are paying today, correct? I mean it is 300 or 400 basis points lower.

Saurabh Dhoot: Yeah if comes in at 18%, it will be 300-400 basis point lower, potentially yes.

Moderator: Thank you. As there are no further questions from the participants, I now hand the conference over to Nupur Agarwal for closing comments.

Nupur Agarwal: Well, thank you everyone for dialing into this call. Happy Diwali.

Moderator: Thank you. Ladies and gentlemen, on behalf of Videocon D2H Limited, that concludes this conference call for today. Thank you for joining us and you may now disconnect your lines.