"DEN Networks Limited Q4 FY17 Earnings Conference Call"

May 24, 2017

MANAGEMENT: **MR. S. N. SHARMA – CEO, DEN NETWORKS LIMITED**
MR. MANISH DAWAR – GROUP CFO, DEN NETWORKS LIMITED

Moderator: Ladies and Gentlemen, good day and welcome to the DEN Networks Limited Q4 FY17 Earnings Conference Call. This conference call may contain forward-looking statements about the company, which are based on the beliefs, opinions, and expectations of the company as on the date of this call. These statements are not the guarantees of future performance and involve risks and uncertainties that are difficult to predict.

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I now hand the conference over to Mr. S. N. Sharma – CEO of DEN Networks Limited. Thank you and over to you, Sir.

S. N. Sharma: Thank you so much. Welcome to all the analysts on the call and thanks for being part of Q4 FY17 and the Annual Results Earning Call for DEN Networks. Our focus throughout has been on collections, collections, collections that is what I have been emphasizing in all our call so far. We have continued the process of improving the collections on month-on-month basis, this has given a major boost to EBITDA where we have seen a turnaround of 241 crores on a consolidated basis vis-à-vis the previous year. The cable monetization process of DEN has gathered momentum and we have seen further improvement of 9% in our Q4 over Q3 collections. Collection efficiencies for quarter has improved by 100 bps at 96%. This is a significant improvement and places out differently vis-à-vis our competitors.

Cable subscription billing including taxes during the quarter stood at 220 crores versus 202 crores in the previous quarter reflecting an improvement of almost 9% QOQ. The quarter 4 billing including tax has significantly improved by 37% over Q1 of 161 crores of the current financial year. ARPU including taxes for DAS-1, DAS-2 and DAS-3 markets stood at 136, 98 and Rs. 73 per box. Respectively vis-à-vis 125, 95, 64 of Q3. Phase-III ARPU has grown almost 60% to Rs. 73 from Rs. 46 in Q1. That has resulted in significant improvement in monetization of Phase-III investments.

Please note that ARPUs are average for the quarter inclusive of taxes on per box per month basis and includes the impact of associates. The above ARPUs are in line with guidance given in the earlier investors call. We have seeded close to 2.80 lakh boxes in quarter 4 in cable business. With this addition, our digital base has gone up to 10.5 million boxes with strong presence of 5.5 million boxes in Phase-III and Phase-IV markets. Broadband business during the quarter, the subscription revenue has marginally improved compared to previous quarter by Rs. 1 crores to 22 crores in quarter 4. ARPU and the subscriber additions are under pressure due to intense competition from other telecom players.

Broadband business achieved its first ever quarter of positive EBITDA of Rs. 1 crores for quarter 4. The broadband subscriber base at the end of quarter 4, 2017 was 1.77 lakh. We have been able to deliver the above performance despite the competition not moving with the same agility in terms of discipline on activation income and collections from the ground. While the regional players have demonstrated their ability to move quickly, unfortunately we have not seen the same intensity from the National level MSO. As you are well aware TRAI has notified the new tariff order and same has been challenged in few jurisdictions by various stakeholders. We expect that this will delay the implementation process although we remain confident with that the order will get finally implemented soon.

In nutshell DEN continues to focus and do well on its core business of cable and broadband. We have demonstrated excellent progress on cable monetization, broadband breakeven and we hope to maintain the same momentum going forward also. Regulatory environment is positive with the introduction of new tariff order and GST. Our thrust is going to be new technology offerings to our subscriber and be the leading player amongst the MSO. We have demonstrated this by pioneering our initiatives on OTC Gaming services and developments of android based open box. We will continue to build our relationship with our LCO partners and leverage the cost base that we have in for further expansion of business.

With this, I would like to hand you over to Manish to walk us through some of the important financial numbers. Thank you, Manish.

Manish Dawar: Ladies and Gentleman, we have already circulated the presentation on Q4 and Financial Year 2016-17 performance. I will cover few highlights. As you are aware effective April 1, 2016, we have started reporting our financials as per IndAS, however, we continue to give the comparative previous quarters and the current quarter numbers on the basis of IGAAP as well IndAS consolidated and standalone results have been reviewed by the auditors. In the current financial year, we have restated the numbers of 2015-16 as well to IndAS from IGAAP. You would have seen a significant increase in the reported PAT loss amounting to almost Rs. 170 crores between IGAAP and IndAS for the previous financial year. This is mainly on account of shift in the recognition of activation income that we have talked about in the earlier quarters. Let me reassure you that this is only an accounting adjustment with no cash impact and the activation income will flow back in the profit and loss account over the next 7 to 8 years.

Quarter 4 Financial Results summary which I am about to share with you is on the basis of business overview that is IGAAP number, the IndAS numbers are also included in the presentation. We have been able to significantly reduce our net debt to 181 crores as of March 2017, compared to Rs. 358 crores beginning of the financial year. Group consolidated revenues pre-activation for full-year 2017 were up at Rs. 1176 crores from INR 1025 crores in the last financial year. Cable subscription revenue at Rs. 646 crores during the year grew by 33% versus the previous year. The cable ARPUs net of taxes and net of LCO share for the quarter were Rs.

117, 85 and Rs. 62 per box respectively for DAS-1, 2 and 3 area versus Rs. 111, 81 and 55 respectively for quarter 3. The cable subscription collection efficiency continues to remain healthy during the quarter at 96%. We would have seen an improvement of 100 basis points over the previous quarter. Consolidated pre-activation EBITDA has significantly jumped to Rs. 135 crores from a loss of Rs. 107 crores in the previous year while the comparative quarter 4 numbers are at Rs. 48 crores versus Rs. 38 crores in the previous quarter and a loss of Rs. 5 crores a year ago in the same quarter. The quarter-on-quarter EBITDA has improved by 26%. Significant improvement in cable subscription revenues has resulted in an EBITDA improvement of Rs. 125 crores in cable business on a year-on-year basis, on a pre-activation basis. Revenues for broadband business stood at INR 81 crores in financial year 2017 compared to INR 40 crores in the previous year.

On broadband business, we have been able to achieve a positive EBITDA of Rs. 1 crores during the quarter. Growth and subscriber additions cost optimization due to organizational restructuring and operational efficiencies have resulted in a significant reduction in the loss from Rs. 66 crores in the previous year to Rs. 10 crores in the current year. While we have also achieved the breakeven at operational profit level in the second half of the year. TV commerce business has achieved a marginal EBITDA of Rs. 1 crores during the year compared to a significant loss of Rs. 22 crores during the previous year.

We are reviewing the future options with respect to our TV shopping business and we will come back to you with firm plans during the quarter. In view of this, we have decided to take a noncash write-off of goodwill on TV shopping business as exceptional item in the income statement amounting to Rs. 25 crores.

The other item impacting the PAT relates to deferred tax which is again an IndAS adjustment, therefore an amount of Rs. 40 crores out of the current quarter loss will not be recurring in future, hence the PAT loss in the current quarter on an adjusted basis has narrowed down to half versus the previous quarter. We have also started to disclose our cable business phase wise EDITDA numbers in the current year presentation. You would have noticed that Phase-I pre-activation EBITDA has topped 30% versus 23% in the previous year. We expect the entire cable business to gravitate towards with EBITDA percentage over the next 2 to 3 years' time. The long outstanding judgment on Delhi entertainment tax was passed in the month of March and I am pleased to share that the same has been decided in favor of DEN and other MSOs. This resolves the contingent liability of Rs. 116 crores for DEN, that you would have noticed in the earlier annual report.

With that, I would like to open the floor for Q and A, thanks a lot.

Moderator: Thank you very much. We will now begin with the question and answer session. We have the first question from the line of Shankar Shetty from Soarang Commodities India.

Shankar Setty: Thank you for the opportunity. Can you touch base upon hurdle of seeding of set-top boxes in third and fourth phase? How is the competition behaving in III and IV Phase? Do you see more cases getting filed in TDSAT related to LCO issues. By when seeding can be expected to be completed. These are the few questions sir, and remaining I will get back to the queue

Manish Dawar: As Mr. Sharma has mentioned, we seeded 280,000 boxes.

Shankar Setty: This was the earlier part, in the present quarter to the next quarter is what I am asking.

Manish Dawar: So, we are not giving any guidance of future in terms of seeding or the financial result, however, I just indicate that overall, we have about 13 million subscribers out of which we have seeded 10.5 million subscribers already. We have taken a call that in Phase-IV we will not be seeding boxes aggressively in the remote areas so therefore we will be seeding boxes only in the peripheral towns which are neighboring to Phase-III or they are contiguous to our existing networks which are already laid. So, therefore, we will not be looking at seeding 13 million boxes which is our subscriber level, it will be less and that could be a variance of about 8% to 10%. So we expect the seeding to kind of finish once the Phase-IV seeding is finished by the other player, which is probably by end of this this year, so on competition, I would request Mr. Sharma to talk about.

S. N. Sharma: As far as Phase-IV is concerned, all the contiguous territories that we have, we hardly has any competition because Phase-III is where we dominant aggressively and Phase-IV funny thing is a mix of variety of terrain where you have cable dark areas where you have areas wherein you don't have even electricity also and then there are areas which are very-very remote and you don't have the fiber deliveries from TELCOS or any other medium to carry the RF signal, so in the mix of this whole kind of environment, the competition is not very aggressive, Court cases is history, there won't be any resistance, it is just matter of time that everybody in that area seed the box and switches off the analogue signal, the process has already been activated. TRAI and MIB are on top of it. The task force is monitoring it very closely and by year end we can say this Phase-IV thing should be completed.

Shankar Setty: Sir, in such a scenario, revenue generation from new seeding will be somewhere around end of year.

S. N. Sharma: So, Shankar, basically whenever we see the box, normally whatever gets seeded in a particular quarter that has to be accrued from the next quarter and as you know and we have seen that from our historical experience also that typically take about let say in a year's time that is what our Phase-III experience says for the revenues to come to the normal level but just to add up to Manish, the collections figure of Phase-IV are better than Phase-III, it took some time for increasing the collections in Phase-III, it took us almost a year to lift it up but where the cutting point itself in the beginning we are close to 45 to 50 Rs.

Shankar Setty: Are we planning to raise prices in one or two quarters, is the competition on the same page.

S. N. Sharma: If you see our drive in the last 12 months, that itself speaks for what you are asking.

Shankar Setty: No, that is the past one, the future part is what.

S. N. Sharma: That was the trend, that definitely gives you a hint of where we are headed for and yes if the competition also turns around and follows the same spirit**,** definitely we are looking for increasing the collections.

Shankar Setty: Okay, what is your take on falling wired broadband prices where it will sustain by what duration.

S. N. Sharma: It all depends on Talcos game plan and warfare what they are entered into, so basically it amounts to giving more and more facilities to consumer like the same consumer which was getting, he was happy with 20 MB till speed last year. As of now, he is not happy even less than 50 MB, so average speed is around that and as far as data consumption is concerned, that also is increasing, so there is definitely going to be pressure on the ARPUs of broadband.

Shankar Setty: Will it make sense for us to initiate the broadband business further.

Manish Dawar: Shankar what we need to understand is how the basic business operates for wired broadband business and wireless broadband business because that is important so that one can understand whether we should be investing in this business or not. And I think I have talked about this briefly in probably one of the earlier call. Worldwide 70% of the data consumption, I am talking about including India happens on a wired broadband line and not on the wireless line. At the same time, if you have to look at the consumption of data today, including the new telecom player, I am including the new Jio offerings and everything, the average data consumption on per handset is less than 1 GB per handset per month. If you were to look at DEN network, our average data consumption per home on a per month basis today stands at anywhere between 65 to 70 GB, so therefore that kind of data consumption is not possible on a wireless broadband line, but today let say we are facing that heat and not only us, all the players because of the latest entrant in the telecom market and plus India does not have the infrastructure for the wired line broadband business, so it makes eminent sense to remain invested in this business, to kind of make sure that this does not get expanded and gets grown but it is important, I mean we are keeping our head a little bit low so that whatever current headwinds which are there, they kind of pass and we understand where the business is going to get stabilized, so that is very important to understand that the two businesses are complementary to each other rather than let say the one technology cannot replace the other technology in terms of whatever is available today. So, we are planning to launch about 15 to 20 small towns over the next one year time where let say we are cable dominant, we have a strong presence on the cable side and we expect that therefore we will be hugely competitive also even if some external players have to come.

Moderator: Thank you. Our next question is from the line of Naval Sheth from Emkay Global. Please go ahead.

Naval Sheth: Couple of questions on what is the status on this 8.2 million billed subscribers and the difference between the set-top box seeded which is 10.5, so if you can explain in which Phases these subscribers would be and what is leading to lack of billing over here?

Manish Dawar: Naval if you were to look at the billed subscribers versus the seeded subscribers this is the loss that we have talked about in the earlier calls, so if you see in Phase-I and Phase-II our loss was (+20%), in Phase-III areas the losses are (-10%). So, what had happened initially when the digitization process got initiated for Phase-I and Phase-II towns, all the MSOs were fighting with each other for the market share position and that is the reason the box has got swapped. So that has got controlled quite a bit in Phase-III and that those numbers are really-really small, that is the reason the overall percentage is under 20%. But at the same time when we talk about let say 8.2 billable boxes, this does not include the boxes which are going in and coming out, so that is another about half a million boxes which is typically just to give you an example that let say in smaller towns when people are going on vacations, they tend to get their connections switched off, or let say during Ramzan time, the UP areas lot of connections are switched out temporarily or let say during summer vacations, so or during exam times of the school, so people tend to get their boxes disconnected and they come back. So when we talk about available boxes, we mean whatever we are able to generate revenue out of that. So therefore, from deleted boxes perspective, if you were to do a right comparison, it will be like 8.5, 8.6 million boxes versus about 10.5.

Naval Sheth: And sir this remaining boxes which are like lost, are these boxes already written-off from the balance sheet.

Manish Dawar: So, we initiated the exercise of writing-off these boxes and we started to provide for accelerated depreciation from quarter 4 of last financial year, so therefore, I would say we have almost kind of written-off about 60% to 70% of these boxes; over the next couple of quarters we will be completely on track on this one.

Naval Sheth: In terms of sir which would be the markets in Phase-I, Phase-II and Phase-III, which are still your lesser than the average ARPU at the company level.

Manish Dawar: In Phase-I, Naval Calcutta is lower than the average of the overall Phase-I. Phase-II, I think we are pretty much there except for maybe one or two towns like Faridabad and all where some court cases are going on and Phase-III our challenge remains in Kerala and Karnataka although they have also improved but I would say those two states are lower than the average.

Naval Sheth: Okay and in terms of as Mr. Sharma stated that National level MSOs are yet to come in the league of aggressive improvement in realization, so now I think there would be one more quarter where base is favorable for you guys and till when you in isolation ,can increase the ARPUs better than the industry going forward as well?

S. N. Sharma: You see Naval we have demonstrated that is what I responded also to the earlier gentleman. We have demonstrated quarter-on-quarter for last four quarters and I myself have been highlighting that the focus is entirely on collection, monetization and increasing the ARPU. The graph has been upward. I am simply waiting for them to fall in line and start doing the same. You will see a further spike from my side as far as performance is concerned. In any case, I am not leaving the path that we have selected willfully and we will follow the same course, I am sure all the intelligent people will do the same thing.

Naval Sheth: And my last question is on sir, if you can provide the total amount of outstanding activation revenues in the balance sheet which will be accounted over the period of next 8 years.

S. N. Sharma: Its 508 crores Naval.

Moderator: The next question is from the line of Kaustav Bubna from SKS Capital & Research. Please go ahead.

Kaustav Bubna: I had a question on your balance sheet. Sir this quarter your gross debt has come down substantially but your cash component has come down too, that is equals to net debt of about 180 crores, so what was the reason for this cash coming down so much and how do we see net debt going ahead in to FY18 and which is with investments into HD and open box how we are going to fund that?

Manish Dawar: So Kaustav, there are couple of factors which is contributing to this reduction in debt and obviously you would have seen the numbers – one is obviously from consolidated EBITDA perspective, last year we lost 107 crores and obviously 107 crores means you are actually funding that business, whereas this year that 107 negative is 135 crores. At the same time we raised equity from Goldman which was end of last year which was another about 140 crores so that is actually going and contributing towards bringing the debt level down. So we are expecting that we will be debt-free over the next two years although we are also trying to restructure the debt position that we have in the balance sheet to be able to bring the gross debt down and the cash down and we are trying that with various banks but given the current repayment schedule that we have, we will be debt-free over the next two years.

Kaustav Bubna: And what was the cash component, I don't have the numbers in front of me because I am outside. Your cash balance has fallen substantially from quarter 3 to quarter 4.

Manish Dawar: Yes, because that has gone to repay the debt.

Kaustav Bubna: Okay, but that is mainly, I mean that is obviously one factor, is that the only factor.

Manish Dawar: Yes, because operationally, if you see broadband in last quarter has broken even on operational basis, TV Shop has also broken even, cable is positive, CAPEX is under whatever our guided percentage amount, so that is where it has gone. If you look at cashflow you will be able to understand.

Kaustav Bubna: Yes, what was your operating cashflow figure for FY17 versus FY16?

Manish Dawar: FY17, if you look at our EBITDA was 140 crores and out of that reduced the net interest or the net treasury cost I would say which will be around 30 crores to 40 crores, so therefore operationally we have generated 100 crores of cash.

Kaustav Bubna: And last year FY16, what was it.

Manish Dawar: Last year would have been (-150).

Moderator: The next question is from the line of Rohit Dokania from IDFC Securities. Please go ahead.

Rohit Dokania: Just few questions from my side, one is you can talk about the CAPEX that you have done in FY17 and what does it look like in FY18.

Manish Dawar: The CAPEX in 17 on a gross basis Rohit on the broadband side is about 26 crores to 27 crores and on cable side again is about 100 crores, this is I am telling you on a gross basis because out of this, we seeded almost a million boxes on cable side and we have got the activation income on that. So let say coming to FY18, we expect broadband CAPEX to be almost at the same level and on cable CAPEX side will be about 30 to 40 crores. Whereas the gross number again will be almost the same number because we are planning to seed another million boxes as Phase-IV during the year.

Rohit Dokania: The other thing was if I was to look from the paying subscriber basis, so today you are about at 8.2 odd million and you also sort of articulated that you are not looking at going up to 13 million. So is it fair to say over the next 2 years you are sort of paying, you know subscriber base could probably peaked out at about 9.5 to 10 odd million?

Manish Dawar: Yes. That is the fair assumption.

Rohit Dokania: Okay sure, the other thing was can you talk about the GST impact that would have on our financials because I would assume that the e-tax will be largely paid by the sort of the LCO or the LMO and we would be bearing that 15% tax which for us now would go to 18%, which essentially means our net realization would come down, is that a fair sort of an understanding?

Manish Dawar: Rohit entertainment tax as you know is a state subject and the states where the responsibility lies with the MSOs and there are states where the responsibility lies with the LCOs. So if you were to look at the overall weighted average incidence for DEN, wherever it is MSOs responsibility that comes to about to little more than 2%. So a Service Tax of 15% and Entertainment Tax incidence of 2% and plus we have other taxes in view like your whatever, Swachh Bharat cess and other cesses and additional surcharges and octroi and those kind of things because everything is going to get subsumed in the GST, we see a nominal upside of about 1% to 2% compared to the existing scenario but let say from guidance perspective you can assume it to be neutral because I would say there will be a little more conservative view than let say may be (+2%).

Rohit Dokania: Sure sir, so when you talk about the sort of net realization during the quarters in IGAAP, you basically net out both e-tax and service tax that is applicable right.

Manish Dawar: That is right.

Rohit Dokania: The last question was you know if I look at your content cost per subscriber for the year which is net of carriage, it is about 12 odd bucks on the 8.2-odd million sort of paying subscriber base. I was just wondering how should one look at this from a 1 years to 2 year perspective in terms of this going up.

Manish Dawar: Rohit as you know this largely depends on the new tariff order in terms of when and what shape and form and how does it get implemented.

Rohit Dokania: If we assume that let say you know it is not getting implemented in FY18, let say just for argument sake then how should one look at FY18 in terms of net content cost?

Manish Dawar: If you were to look at let say without assuming any TRAI impact, from a current net level you can assume an increase of about 12% to 15% for the next year on a net basis. If you see the TRAI impact obviously that will change the entire landscape and depending on let say if that were to get implemented in the current shape and form, then the content cost will be like next to zero for us.

Rohit Dokania: Yes obviously because it will be a pass through.

Manish Dawar: Yes.

Moderator: The next question is from the line of Sanjay Chawla from JM Financial. Please go ahead.

Sanjay Chawla: I am Sanjay Chawla here from JM. Just couple of questions sir. One is the follow-up you mentioned that the number of digital customers that you have reported 10.5 million in cable is that the gross number of set-top box which is actually seeded and is not necessarily the number of active digital customers, can you clarify that please.

Manish Dawar: Yes 10.5 is the gross number of boxes that we have seeded as against that the active boxes are 8.2 and this is what I think Naval also raised earlier and I replied to it.

Sanjay Chawla: The remaining 2.3 million these boxes are inactive and in the sense you have disconnected those boxes.

Manish Dawar: Yes, it is a combination of inactive boxes, inactive is the category whereby people keep on coming in and going out and then we call something as deleted boxes where we disconnect them from the system.

Sanjay Chawla: Okay, so excluding deleted how many would you be counting as your boxes.

Manish Dawar: That will 8.6 to 8.7.

Sanjay Chawla: Okay, roughly 2 million you are saying one could consider as deleted.

Manish Dawar: Yes.

Sanjay Chawla: The second question is in your cost structure I can see an item called placement fees, can you clarify what exactly that is?

Manish Dawar: Sanjay whatever placement income we have from the broadcasters, we share a percentage of that with our distributors and that is called placement fee.

Sanjay Chawla: Okay, so is that a set percentage or depends on the markets?

Manish Dawar: Yes, depends on the market, depends on how old the relationship is, so it is not a same percentage with all the distributors. It varies from state-to-state.

Moderator: Thank you. The next question is from the line of Rahul Jagwani from SKS Capital & Research. Please go ahead.

Rahul Jagwani: Yes, can you throw some light on open box and whether that gives you some competitive advantage and secondly is how will your, will the HD boxes help any margin expansion for you guys?

S.N.Sharma: You see as far as open box is concerned this is the trend that has got up with the United States of America around one and a half years back and there have been lot of developments. In a layman's word, I would explain it, what you have today on your smart handset, your that very smart handset will become the remote to your TV and all the apps that you are able to enjoy on your small screen that is your handset screen you will get enabled on the TV screen also and using your remote you will be able to use those apps and use different contents that is being provided through RF in normal course. So there is the enhancement of service as far as viewer is concerned and besides this lot of gamming services and lot of vast value-added services will get added to the consumer experience so this is the latest trend so DEN has been taking initiatives to keep pace with the upcoming technologies and that is why we have laid thrust on open box and the teams are working, the vendors are working round the clock and we hope to launch it in quarter three of this year.

Rahul Jagwani: Okay and will HD boxes help any sort of margin expansion or anything.

S.N. Sharma: Yes, there is a special focus on HD boxes and you will see us achieving good number of seeding of HD boxes. That is going to bring in extra revenue for us and we hope to seed extensively. Our pricing is quite aggressive, our schemes that are in offering have been widely accepted by LCOs. In couple of quarters we will start giving you the numbers at which you all are going to smile and enjoy.

Moderator: Thank you. That was the last question. As there are no further questions, I would like to hand the conference back to the management for any closing comments.

Manish Dawar: Thank you very much to all of you for participating in the Conference Call. Please feel free to contact us, if you have any further clarifications or in case you need any more information, thank you very much.

S. N. Sharma: Thank you very much.

Moderator: Thank you. On behalf of DEN Networks that concludes this conference. Thank you for joining us ladies and gentleman, you may now disconnect your lines.