

CRISIL PUBLIC ISSUE REPORT

(One time assessment)

Overall Assessment of Fundamentals

Shree Ashtavinayak Cine Vision Ltd.

Evaluation Score 2.0/5.0

Public Issue of 3,300,000 Equity Shares of face value Rs 10 at a price Rs 158 per share.

Bid/Offer Opens *

Bid/Offer Closes *

Shares Offered 3,300,000

As % of post issue Equity 32.9%

Shares Outstanding (Post issue) 10,031,000

Lead Manager

Allianz Securities Limited

Registrar to the Issue

Intime Spectrum Registry Limited

Background: The company was incorporated in October 2001. It was converted to a public company in June 2004. The company is into film production and distribution. It also has a small presence in the film exhibition space.

	SACVL	Adlabs Films	Pritish Nandy	K Sera Sera	Sahara One
P/E	13.3	59.1	25.13	12.4	90.6

Market capitalisation as of March 31, 2006 and earnings for FY 2005-06 have been used for calculating P/E

Shareholding Pattern	Prior to issue		Post issue	
	No. of shares	%	No. of shares	%
Promoters	4,441,890	70.5	4,869,890	48.6
Promoter group	231,110	3.7	231,110	2.3
Other Body Corporate	1,630,000	25.9	1,630,000	16.3
Public	0	0.0	3,300,000	32.9
Total	6,303,000	100	10,031,000	100

		SACVL	
		2004-05	2005-06
Operating income	Rs Million	265.5	603.4
Operating margins	Per cent	2.0	21.1
Net profits	Rs Million	3.5	74.7
Net margins	Per cent	1.3	12.4
ROCE	Per cent	2.7	49.9
Return on Equity	Per cent	2.0	46.7
No. of equity shares	Million	2.9	6.3
Net worth	Rs Million	177	250
Return on Equity	Per cent	2.0	46.7
Basic EPS	Rs	1.2	11.9
Diluted EPS	Rs	1.2	11.9
Book value	Rs per share	62	40
Gearing	Times	0.12	0.48

Overall Evaluation

The grading assigned to Shree Ashtavinayak Cine Vision Ltd. (SACVL) reflects the inherent risks of operating in the film industry where entry barriers are low and the susceptibility of the business model to rapid changes in audience tastes and preferences on the one hand and risks arising on account of rudimentary methods used for arriving at the value of a film and its components on the other hand.

In a short span of 3 years, SACVL has created a name for itself in film production and distribution, indicating the capability of the management in its line of business. The grading is, however, constrained by its relatively short track record of proven performance, its heavy reliance on Mr. Dhilin Mehta (the managing director and major shareholder) and its under developed corporate governance system. The grading also takes into account the aggressive growth plans of the company in film production, managing which would pose a challenge to the relatively young management of the company given the competitive pressures of the sector. The timing of eventual utilisation of the funds raised through the initial public offer by the management is also open to question.

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In order to arrive at overall grade, the company has been evaluated on 3 broad parameters:

- Business prospects and financial performance
- Management capability
- Corporate governance

Business Prospects

SACVL is into the business of production and distribution of films. In distribution, its presence is largely restricted to the Mumbai territory. The company also has a small presence in the film exhibition business through tie-ups with around 25 theatres across the Mumbai territory for screening content selected by it.

Film industry revenues to increase at 12.6 per cent CAGR

CRISIL Research expects the revenues of the film industry to increase at a CAGR of 12.6 per cent from the estimated Rs 70 billion in calendar year 2005 to Rs 126 billion by 2010. This growth will be driven by increasing consumer spending on movies and entertainment, a sharp increase in the number of multiplex cinemas, better exploitation of films, increasing implementation of digital technology in cinemas, and increasing corporatisation of the industry.

Film production: Risks remain significant despite improved prospects

The economics of film production, CRISIL Research believes, has improved considerably in the last 3-4 years due to the following factors:

- Lower dependence on box office success due to the increase in the value derived from revenue streams such as satellite and home video rights, and the opening up of new sources of revenue such as mobile and internet downloads
- The easier availability of financing at lower interest rates from organised sources
- Improved production planning and scheduling
- Implementation of digital technology in cinemas, aiding in the simultaneous release of films to a larger audience

Notwithstanding the improved scenario, CRISIL Research is of the view that the risks in film production such as completion risk, financing risk, and changes in audience tastes and preferences remain significant. Moreover, if a movie produced by a production house does not fare well, it tends to affect the price the next movie of the production house fetches.

SACVL in film production: Aggressive scale expansion increases execution risk

SACVL has produced 4 films to date – “Fun2ssh”, “Agnipankh”, “Maine pyar kyun kiya”, and “Golmaal”. Over the medium-term, film production will be the major thrust area for the company, and most of its resources will be allocated for this purpose. The company has laid out aggressive plans; it intends to take up production of 3-4 medium-to-high budget films in a year.

SACVL’s business model in production centres around recovering a large part of the production costs from the sale of associated rights before a film’s release and a planned production process focusing on timely planning and execution with the responsibility of each of the members of a project clearly defined. By doing multiple projects at the same time, the company intends to save on artist and technician costs (by signing them up on a bulk basis) and production costs (the same set once constructed can be used for multiple films) and post-production costs. The company proposes to purchase some key equipment required for film production; it presently hires equipment whenever required. Producing a number of films concurrently will also, the company hopes, lower its dependence on the success of any one film.

CRISIL Research believes that SACVL has a fairly de-risked business model but it would be exposed to the risks inherent in the production business. The success of the company's growth strategy in respect of film production will be critically dependent on

- Its ability to stick to timelines and keep costs under control. Given the heavy dependence on actors and other main technicians to complete a film in time and within the budgeted cost and limited ability and willingness in the industry to enforce contracts, the company, CRISIL Research believes, would not have complete control over this aspect of production.
- Its ability to build a name as a quality production house, which would hinge upon consistent performance of its films at the box office

Having a distribution set up in the Mumbai territory and a presence in the exhibition business as well would enable the company to give greater mileage to films that are produced in-house and keep a continuous tab on the pulse of the movie going public.

Film distribution: High risks with the system skewed against distributors

The film distribution business entails higher risks than production. CRISIL Research believes that the risks assumed by a film distributor are very high since profitability is tied to the price paid for acquiring distribution rights (and there is no scientific method on the basis of which this price is arrived at) and the box office performance of a film and distributors get to see only rushes of a film before purchasing the distribution rights. Furthermore, changes in the set of leading distributors over time seem to suggest both keen competition and fast changing market fundamentals.

SACVL in film distribution: Strong presence in Mumbai territory

SACVL distributes films produced not only under its own banner but also that of other production houses. The company entered the distribution business in 2004-05, and has distributed 21 films to date. At present, its distribution activities are mainly limited to the Mumbai territory. The company has managed to achieve success (read earn profits) with around 70 per cent of the films it has distributed. In the next 2-3 years, SACVL intends to take up the distribution of 7-10 films produced by external production banners annually in addition to its own productions.

The factors that SACVL looks into before deciding to purchase a film for distribution and quoting a price are – the genre of the film, the production house, the star cast, the director, and the saleability of the music of the film, average ticket prices and the number and quality of theatres in the territory where it intends to distribute the film. The company has put in place certain strategies such as entering into different kinds of revenue-sharing agreements with theatres and selling sub-circuits within a territory to other distributors to mitigate its risks. Nevertheless, risks in distribution, according to CRISIL Research, remain high.

Financial performance

After reporting a net loss of Rs 1.5 million on a turnover of Rs 83.8 million in FY 2003-04, SACVL has turned around. The company managed to record a marginal profit of Rs 3.5 million in 2004-05, and in 2005-06, net profits of the company shot up to Rs 74.7 million. Operating margins, in 2005-06, were at a healthy 21.1 per cent. This turnaround in financial performance was achieved on the back of the company bettering its success rate in the film distribution business and the success of the film, "Maine pyaar kyun kiya" (released in July 2005), co-produced by the company in association with Sohail Khan Productions.

CRISIL Research is of the opinion that future improvements in SACVL's financial performance would be dependent on its ability to successfully execute its growth strategy in film production and continued success in its distribution business. The company plans to take up film production on a much larger

scale, while continuing to maintain a steady flow of business on the distribution side and expanding its exhibition business.

Management capability

From being a non-entity in the film industry, SACVL has managed to create a name for itself in a short span of 3 years. This indicates the capability of the management in its line of business. However, the size and scale of business SACVL intends to get into is much larger (production of 3-4 films in a year as compared to 1 film in a year previously), its ability to manage which is unproven as yet given its relatively short track record.

SACVL is also heavily dependent on its managing director and majority shareholder, Mr. Dhilin Mehta, who is the driving force behind the vision of the company. In the last couple of years, Mr. Mehta has put in place a management team to execute his growth vision for the company. But the other members of the top management are mainly responsible for day-to-day management of different functional areas.

Senior Management	Designation	Role in the company
Dhilin H. Mehta	Chairman and Managing Director	Oversees the entire operations of the company
Harshad K. Mehta	Joint Managing Director	Liasoning with financiers and co-ordinating with various departments for their financing requirements
Rupen N. Amlani	Director - Distribution & Marketing	Acquisition of distribution rights for films produced by other production houses & deciding the media strategy
Hiren J. Gandhi	Director - Production	Responsible for ensuring that films are produced as planned without time and cost over runs
Dhaval V. Jatania	Director - Business Development	Involved with both the production and distribution divisions of the company
Vipul Mehta	Deputy GM - Finance	Looking after day-to-day accounts and finance
Archana Andare	Company Secretary	Compliance with laws of the land

Corporate governance

SACVL's Board consists of 11 directors, of which six are deemed to be independent. As required by the listing agreement with stock exchanges, SACVL has also formed the Audit Committee, the Remuneration Committee, and the Investor Grievances Committee. All the three committees consist of the six non-executive independent directors.

CRISIL Research's discussions with two of the independent directors leads us to believe that corporate governance in SACVL is fairly under developed at the current juncture. Although the independent directors have a good track record in their respective professions, their ability to exercise management oversight in the films business is open to question. Moreover, none of the independent directors have any significant experience as board members. During the board meetings held to date, the independent directors have mainly given their views on matters where they are professionally qualified to offer their advice such as accounting norms to be followed and legal issues.

Independent directors	Qualification	Experience
Chandrakat K. Sachde	Retired banker	Worked with Bank of India for 38 years Currently, doing financial consultancy
Pravin S. Jani	Retired banker	31 years of experience in banking Retired from Canara Bank in 2000
Ashok V.Ladhani	Practicing Chartered Accountant	Two decades of experience as practicing CA
Nishant A. Mahidhar	Network solutions consultant	Nine years experience in IT field
Hetal N. Thakore	Advocate and solicitor	Senior partner of Thakore Jariwala & Associates
Subhash P.Rathod	Advocate	Practicing advocate & partner at M/S Devi & Associates

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Utilisation of proceeds

The proceeds of the Rs 520 million initial public offer (IPO) are proposed to be used for financing the production of films and the purchase of equipment required for films production. The promoter group intends to subscribe to an additional 0.4 million shares at the same price as the shares that are being offered to the public in the IPO.

In its draft prospectus, dated April 29, 2006, SACVL has stated that an amount of Rs 459 million (72 per cent of the IPO proceeds) would be utilised for the production of three films costing about Rs 150 million each. But CRISIL Research's understanding of cash flow patterns in film production leads us to the conclusion that the amount of finance required upfront to produce a Rs 150 million film would be much lesser (around 50 per cent of the amount). Furthermore, the company has already started production of two of these films even before the IPO has opened. The management has stated that the amount raised via the IPO will now be used for financing the production of other films planned to be produced by the company. The company proposes to keep aside Rs 141 million (22 per cent of the IPO money) for the purchase of equipment required for production and post-production activities.

Proposed use of issue proceeds

	(Rs million)
Estimated expenditure for production of 3 films	459.0
Purchase of equipment for film production	141.2
Cameras	39.6
Jimmy Jib	2.0
Lighting	16.2
Audio facility	83.4
Public issue expenses	36.0
Total	636.2

Other factors

- There are no outstanding litigations involving the company or any group company
- There are no legal notices standing against the directors or any of the promoters except for an IT notice for a sum of Rs 3.18 million against Mr. Dhilin Mehta, the managing director of the company, for the assessment year 2003-04. An appeal has been filed against the notice before the Commissioner of Income Tax on April 20, 2006.