UFO Moviez India Limited
Q4&FY19 Earnings Conference Call

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Moderator: Ladies and Gentlemen, Good Day and Welcome to the UFO Moviez India Limited Q4&FY19 Earnings Conference Call hosted. 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, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Vikram Ramalingam from Maybank Kim Eng Securities. Thank you and over to you, Sir!

Vikram Ramalingam: Thank you, Raymond. Good Afternoon, Ladies and Gentlemen. Maybank Kim Eng Securities is pleased to host the management team of UFO Moviez to discuss the Q4&FY19 Results.

We have with us from the management, Mr. Kapil Agarwal - Joint Managing Director and Mr. Ashish Malushte - Chief Financial Officer.

Mr. Agarwal, will give us a brief overview of the results and the business. Thank you and over to you, Sir!

Kapil Agarwal: Thank You, Vikram. Greeting everyone and thank you for joining us on UFO's Q4&FY19 earning call.

Let me run you through the headline numbers and key operating highlights for the quarter and full year before we open the floor for questions.

In Q4FY19, Consolidated Revenues grew 19.7% to ₹1,939 Mn. EBITDA increased 13.8% to ₹656 Mn. PBT grew 17.0% to ₹480 Mn and PAT increased 29.7% to ₹335 Mn.

Total Advertisement revenues in Q4FY19 was higher by 3.6% at ₹805 Mn. In Cinema Advertisement revenues stood at ₹717 Mn. Corporate advertisement revenues grew by 9.9% during the quarter. Inventory utilization stood at 6.85 minutes per screen per show compared to 7.39 minutes in Q4FY18.

In Q4FY19, Caravan Talkies advertisement revenues grew 414.1% to ₹88 Mn compared to ₹17 Mn in Q4FY18 driven by higher realizations and increased utilization of vans. Caravan Talkies reported positive EBITDA during the quarter compared to losses in the past.

During the fiscal year, Consolidated Revenues grew by 3.3% to ₹6,169 Mn. EBITDA stood at ₹1,683 Mn compared to ₹1,729 Mn in FY18 and PAT was higher by 5.9% to ₹665 Mn.

The Total Advertisement revenues grew by 11.1% Y-o-Y to ₹2,372 Mn and In-Cinema Advertisement revenues grew 4.1% Y-o-Y to ₹2,131 Mn during the year. Corporate advertisements revenues grew by 15% during the year while Government revenues declined by 4% primarily on account of the code of conduct for general elections. Inventory utilization stood at 5.54 minutes per screen per show compared to 5.19 minutes in FY18.

Moving to balance sheet items, as on March 31, 2019, Net Cash stood at ₹1,189 Mn as compared to ₹1,095 Mn as on March 31, 2018. Also, the Capex intensity during the year has been low at ₹401 Mn compared to ₹654 Mn in FY18. The Company's net cash flows from operations stood at ₹976 Mn as compared to ₹946 Mn as on March 31, 2018.

In line with our capital distribution philosophy, the Board has enhanced the dividend to 150% for the fiscal year 2019. Further, the Board has also declared a one-time special interim dividend of 150% in view of the availability of cash. As a result, the total dividend for the year is ₹30 per share i.e. 300% dividend for the fiscal year 2019 which includes an interim dividend of 275% and a final dividend of 25%. This translates to a payout of ₹1,025.35 Mn including dividend distribution tax.

On the Scheme of Arrangement and Amalgamation between UFO and Qube, the petition for the merger with Qube was dismissed by NCLT in January and subsequently we started exploring alternate options to combine UFO and Qube. However, on account of the current market conditions and decline in our stock price, the comparative value of Qube requires a similar write down which is not in line with the expectations of the shareholders of Qube. Hence at this stage there is a standstill. However, the Managements and Promoters of both companies are convinced of the benefits of the unified operations and will continue the efforts to unify both Companies.

Further, I would like to highlight that the Advertisement Sales Teams have started socializing the outcomes of the market research with the select advertisers. Initially the plan was start the outreach immediately after concluding of the merger of UFO and Qube. Since such unification of the two businesses has been deferred, UFO has begun socialization of the market research activities on its own.

With that, I open the floor to take your questions.

Moderator: The first question is from the line of Kunal Patel from Equilligence Capital Advisors.

Kunal Patel: The first question is regarding the NCLT order. Reasons for dismissing the merger were very strong. Can you talk in detail on the issues like shareholding, stamp duty, certain transactions routed through different entities and is there any tax angle to it?

Kapil Agarwal: We believe and have been advised by our lawyers, that there was no substance in the various issues raised by NCLT in its order. Therefore, we have already appealed at NCLAT to overturn that order, particularly the invalid observations made by NCLT.

Kunal Patel: As per my understanding, political parties have to stop advertising the day Election Commission announced the election dates till the elections are over. However, I could see advertisements from political parties in my city last month, can you clarify this?

Kapil Agarwal: The moment elections are declared, the model code of conduct applies. So, the Government stops advertising, the Government cannot promote their schemes to lure voters. However, political parties are free to advertise and normally they advertise closer to the election dates. The model code of conduct came into force sometime in early March while the elections started end April.

Kunal Patel: Why were we expecting a decline in revenue from the Government or political parties this quarter?

Kapil Agarwal: Political parties start advertising closer to the election dates. When the model code of conduct comes into being, elections are at least 1.5 months away. Political parties only advertise closer to the election dates and Government business stops immediately when the model code of conduct applies. However, we are pleased that the decline is not as much as we were expecting.

Ashish Malushte: And we had a high base in Q4FY18.

Kunal Patel: So, we seen higher advertisement growth in this quarter, right?

Kapil Agarwal: That is right. In the month of March, there were practically no political advertisements. However, we could partly substitute this with more advertisements from public sector undertakings and others.

Kunal Patel: Lastly, thanks for the generous dividend for the year but I believe dividend is a very expensive way to distribute cash. Why didn't we go for buyback, which is a far better and cheaper option, given the stock price right now?

Kapil Agarwal: As mentioned in the opening remarks, both the management and promoters of Qube and UFO are convinced about the benefits and are continuing to make efforts to create a unified operation. Currently, the expectation of Qube's shareholders does not match our stock price. Admittedly, buyback is a much better option for shareholders and for the Company. However, if we did a buyback at this stage, it would take a few months to complete the process and after that for one year, as per SEBI guidelines, there is an embargo on raising new share capital. If any combination has to take place in the next few months, we may need to issue shares to the Qube promoters. If you remember, the external shareholders owning 55.29% of Qube were selling their shares for cash while promoters were to be issued new shares by way of a share swap or merger. So, a buyback may have restricted the possibilities of a combination with Qube for at least 1.5 years. Therefore, we decided to declare dividend at this stage and not do a buyback, because the combination with Qube is probably more beneficial to shareholders of UFO than doing a buyback.

Moderator: The next question is from the line of Urmil Shah from IDBI Capital.

Urmil Shah: The Corporate advertisement for Q4 also appears to have remained soft. And now that almost two months are over in the current quarter, what kind of revival are we seeing here? Also, if you could indicate the outcome of your market research activities and the early feedback from select clients?

Kapil Agarwal: First of all, I would like to re-emphasize that ours is not a quarterly business, it is an annual business. In Q1FY19, there was negative growth of 3%, Q3FY19 showed 40% growth and Q4FY19 showed 10% growth. But overall, there was 15% growth in FY19, which is in line with our expectation. We will refrain from talking about Q1 but over the year, we will see reasonable growth in Corporate advertisements. So far as market research is concerned, both UFO and Qube had appointed Nielsen and we were planning to start the outreach immediately after the merger. We kept deferring the outreach, hoping that the merger or a combination in one form or an other will happen, despite the rejection by NCLT in January. However, as the transaction has been deferred, we have started socializing the market research numbers with select advertisers, which is as recent as last week. We will wait to get reactions because there were quite a few advertisers who, for the want of data, were not advertising with us. Our effort is to attack that select set of large advertisers, like multinational Companies and more organized players, socialize them with this data and try to grow them.

Urmil Shah: Any colour on the kind of metrics which this report covers - that would also be helpful.

Kapil Agarwal: There are two parts of this data. One is the number of audience and second is the audience profile. So, we have first concentrated on the numbers and now we are asking Nielsen to work on the profile, which we will be officially publishing in the next few weeks.

Urmil Shah: There has been significant improvement in Caravan's performance. Your outlook on this business would be helpful?

Kapil Agarwal: About 1-1.5 years ago, when we were at the lowest ebb of operations in Caravan and everybody was very concerned that this business was losing money, we had said two things. One, that we have in-principle decided not to do any further Capex in that business. That commitment we have stood by. However, we also took it as an opportunity to enhance our revenue. As the vans were selling at low cost, we toughened our prices and also, changed the profile of the vans in this period. So, we converted a lot of vans, with a bit of Capex, to LED vans. Earlier, shows could happen only in the evening, so the vans could be operated for very limited time. We enhanced the utility for a 360-degree service during the day and we could command a much higher price. So, because of LED vans and other efforts, we have seen higher utilization as well as higher per van realization. We hope to utilize all the vans in the near future and that is very important. The good part is that good Corporates, who used to be our clients initially, have come back and are consistently using and experimenting with this medium again - companies like Pepsico - and we are trying to build the traction. We should be able to eventually not only utilize these vans but also expand the number of vans.

Urmil Shah: If you could share the number of vans that were on an average operational for the year. Secondly, is the non-advertisement share in Caravan substantial right now, basically activation and other activities?

Kapil Agarwal: Basically, there is no distinction between advertising revenue and non-advertising revenue. There is a principal sponsor and the van is painted on three sides with the sponsor's advertisements. For example, Pepsi advertises on two or three sides and on one side is the LED screen. These vans are moving hoardings in a way. They go from village to village, place to place, with Pepsi visibility on the outside. They have programs, activations, door knocks, research, etc. promoting their products during the day. We basically do the costing and give a combined price. This is primarily advertising combined with additional services to build traction. The on-screen advertising of other products, when the van is sold to one client, is very limited right now. In the future, we are expecting that also to build up.

Ashish Malushte: In Caravan, operating van days have gone up from 7,412 in FY18 to 13,350 in FY19. It is an 80% increase.

Moderator: The next question is from the line of Anand Bhavnani from Unifi Capital Pvt Ltd.

Anand Bhavnani: Just wanted to understand, you have challenged the NCLT order. Can you give us some timeline as to when we can expect some updates?

Kapil Agarwal: The next hearing is scheduled for 10th of July.

Anand Bhavnani: As we have challenged the NCLT order, are we changing anything in the way we operate, to make it simpler for us to get a stay on the order and proceed with the merger? Or are we challenging the order in its entirety and continue to have the same structure as in the past?

Kapil Agarwal: Firstly, there is absolutely nothing wrong that we were doing and we believe that points mentioned in the NCLT order are erroneous. It is an erroneous judgment. We used the best lawyers, best accounting firms and best advisors available in the Country who advised us. Therefore, we have challenged the order in its entirety. We believe there is nothing that we need to change at our end because there was nothing ab-initio.

Anand Bhavnani: On the matter of VPF going forward, how do you see this contention on VPF evolving?

Kapil Agarwal: Apart from the sunset under the Hollywood contract, and since the IPO in 2015, we have been sensitizing the market that we do not foresee any changes happening in the VPF structure in the near term, next 2-3 years at least. We may decide to voluntarily start giving concessions if our advertisement revenue builds up beyond a point. It is too early to talk about it. And as you have seen, despite the substantial sunset impact, we have been able to maintain profitability. That means our perpetual revenue has been consistently going up; despite a substantial impact of VPF sunset, this impact has been fully absorbed. So, we can only expect a way up in future after the last leg of the sunset closes.

Anand Bhavnani: What is the timeline for the last leg of sunset?

Kapil Agarwal: About a year and half.

Ashish Malushte: The balance impact would be in the range of ₹140-160 Mn.

Kapil Agarwal: ₹140-160 Mn is over the next 1.5 years. That is our estimation. The sunset impact is not a defined figure, it is a contract with a studio. The actual impact will depend on how many movies from those studios are released, what is the release pattern, how long the movie works, what Hindi movies are released where we collect VPF. So, ultimately it is just a guidance.

Anand Bhavnani: Lastly, we have been seeing that increasingly there has been targeting of single screen theaters by multiplexes to bring them under their fold. So, how are we combating this and if you can give us some sense of our effort in this direction?

Kapil Agarwal: We have really not seen any major trend in multiplexes targeting single screens; it is a very small number. There are two kinds of single screens. One is low grade, low premium or low revenue screens. If those screens are attacked by our competitors, we let them go. Over the last six years, the number of multiplex screens has almost doubled in our case, from 690 screens in FY14 to 1,194 screens in FY18 and now we are at 1,266 screens. Multiplex chains are largely concentrating on top 150 cities, their target market is very different, while we are present in ~1,200 cities and towns across the Country.

Anand Bhavnani: For each of the three segments - advertising, distribution and equipment, what are the challenges you foresee in FY20 and how are we trying to address them?

Kapil Agarwal: Our three revenue streams are from exhibitors, distributors and advertisers. On distributor revenue, to the extent of the sunset, they will be negatively impacted. This year, distributor revenue has gone down but non-sunset revenue is slightly up and sunset revenue is down. But this is partly offset, because of digitization as more movies are getting released, more regional movies, 100-200-300 crore movies. Number of movies released last year was ~1,800 which in the last 10 years have gone up dramatically from 600-700 movies. More movies released mean more VPF revenue for us. So, VPF revenue - non-sunset is going up marginally. But, we have not increased the prices. Prices are stable by more utilization, it is going up party. Now on exhibitor revenue, there are two parts - product sales and rentals. Rentals are stable; we do not increase them because we believe that having the exhibitor with us is the most important part of our business. That is how we earn VPF and advertising revenue. For the last 5-6 years, we have not made any change in the rental structure. Now, within product sales there is sale of consumables like lamps and spares and the other is sale of the projectors. Consumables is a consistent business with consistent margins. As far as equipment sale is concerned, that is not our business model. We like to invest in the equipment and perpetually earn rentals and VPF revenue on them. However, in a few quarters there are product sales while in other quarters there is none. All depends on how many new multiplexes are coming up, which like to buy equipment. So, in some quarters there will be sale of equipment primarily led by Middle East. In India, we hardly do anything.

Moderator: The next question is from the line of Ankur Periwal from Axis Capital.

Ankur Periwal: I think you touched upon this earlier as well on the findings from the Nielsen survey. I am just trying to understand this better, the legal challenges that we are facing with the Qube merger were pretty evident 3-4 months back and typically, once you enter into a legal tussle, it takes long for things to settle. So, what restrained us from sharing these findings earlier with advertisers because, if I remember it right, earlier you did mention that the survey will be done on a sample of UFO as well as Qube screens? I presume there will be separate findings for both sets of screens, so why did we let the delay happen?

Kapil Agarwal: It was management's decision to publish the combined numbers because we saw far greater benefit in doing that. So we deferred it because a combination in some form or the other looked imminent. Once NCLT rejected it; we were working on alternative methods. For example, we were planning to buy out the 55.29% shareholders of Qube for cash. That is why we were accumulating cash, despite ICICI Venture dropping out. We looked at doing either a share swap or a merger for the balance shares of Qube. This would be simpler than the complex scheme which was tabled two years ago and rejected by NCLT. For the last three months, we were putting consistent efforts and were very close to doing that but, being price sensitive information not in public domain, we never talked about it. Now, when our stock price dropped substantially, we needed to take a mark down in the sale price but Qube's shareholders were not willing to take that kind of a haircut. So, we called it off and decided to distribute the cash since our combination with Qube has been deferred. It may take a few months before we come back to the negotiation table and we felt it is not wise to hold back the data anymore and started socializing selectively that data with our clients.

Ankur Periwal: So, the prospective benefits of sharing these findings - do you think these are the same as envisaged earlier or would a combined entity be required for the full benefit to come in?

Kapil Agarwal: The combined benefit would certainly have been greater because when you go to a client with an all India solution, it is a different ballgame than going to him with a fractured solution. But we felt that the numbers are now available at least for our network, which will benefit us because there are many clients who do not want to work without numbers. So, we are now attacking those clients who depend on numbers and were not advertising. We hope to bring more new clients to our platform. Post the Qube combination, if at all it happens, the benefit should multiply.

Ankur Periwal: Any thoughts on what kind of advertisement growth are we looking at because as I understand this will be more accretive for Corporate advertisers?

Kapil Agarwal: We expect reasonable growth in Corporate advertising. It all depends on socialization of the data, once that takes off in the next few quarters, we should see good growth in Corporate advertising.

Ankur Periwal: Will receivables on our books be largely for advertisers, is that the right assumption?

Ashish Malushte: A significant portion of the receivables is on account of advertising.

Ankur Periwal: And lease rental VPF will be probably a month or so, in terms of days?

Ashish Malushte: VPF is very short, because it is an advance payment in most cases.

Kapil Agarwal: I will quickly give you a flavor of the three kinds of receivables. So far as lease rentals are concerned, these are coming from exhibitors and in almost every case we have a security deposit from exhibitors - so, with a bit of delay all the rentals come in and we have a cash security deposit. Second is the distributor revenue. Again, in 90% cases except in Hollywood contracts or sub-contracts where there is a credit period, we collect in advance. Now on advertisement revenue, there is a 120 days credit period that the Government and other clients take. After Q4, we see very rapid collections. But, by and large, the major share is advertising debtors, which is about 60%.

Ankur Periwal: The reason I asked this - if I go back in history, receivables were hovering around 85 days to 95 days. But last year, it increased to 113 days and this year increasing further to 118-120 days. Now, is this a new normal that we will be looking at? And since it is largely coming from advertisers, I am trying to connect it with advertisement growth. Is that a new normal or do we think this number can come back to the earlier levels of 90 odd days?

Kapil Agarwal: It all depends on the advertisement growth in the last two quarters. Immediately after close of the year, most of the advertisers clear their dues.

Ashish Malushte: Ankur, you are absolutely right, it is going in line with growth in advertising revenue. So, it is not likely to come back because the composition of revenue is shifting in favor of advertising revenue.

Moderator: The next question is from the line of Neeta Khilnani from B&K Securities.

Neeta Khilnani: For FY19, in-cinema advertisement revenue has grown about 4% whereas volume growth was nearly 7%. Has there been any pressure on yields? And any color on how the Government and Corporate advertisement rates have moved this year? And what is your outlook?

Kapil Agarwal: As you would know, sometime back Government had revised rates by 20%, which has been fully factored in the current quarter's numbers.

Neeta Khilnani: Then why is the full year yield showing a decline of 3%? Volume growth has been about 7% and in-cinema revenue is up 4%, am I missing anything here?

Ashish Malushte: There is one more component, which is the average number of screens. So, if you add that in, then you will be able to get the answer.

Neeta Khilnani: The jump seen in D-Cinema domestic revenues this quarter after several quarters of decline. You mentioned earlier that it is because of the non-sunset screens. Can you quantify that amount? Is this sustainable? What kind of outlook do you have on non-sunset D-Cinema revenue?

Ashish Malushte: What we have guided is the estimate of D-Cinema net revenue which is expected to go out. That is in the range of ₹140-160 Mn and is likely to happen over the next 1-1.5 years.

Neeta Khilnani: After several quarters of decline, net D-Cinema domestic revenue has actually jumped from ₹69 Mn in Q3FY19 to ₹115 Mn in Q4FY19?

Ashish Malushte: So, the way it is going to happen is that annualized revenue for the full year of D-Cinema at a net level would go down by ₹140-160 Mn.

Kapil Agarwal: You are trying to see a pattern. However, what happens in the market - which movies are released, Hollywood, Bollywood, regional movies, how the D-Cinema network gets utilized - has no pattern to it. If there is a big Hollywood movie released, many Hindi movies may get deferred in that quarter and you may see a dip. When no major Hollywood movies are released, then you will see more Bollywood, and then you will see an uptick. So, there is no trend that we can guide the market on.

Neeta Khilnani: Finally, what are the sustainable margins on Caravan, if you give us some color on that?

Kapil Agarwal: This quarter, you can see in VDSPL business, Caravan has contributed 22-23% EBITDA margin. Now it all depends on volumes, Caravan's EBITDA margin in steady state with good utilization should be 35-40%.

Moderator: The next question is from the line of Vaibhav Badjatya from HNI Investments.

Vaibhav Badjatya: If you look at global players in a similar space like National Cine Media, their capital intensity is far lower than UFO and that is primarily because they do not have the lease rental part of our business. So, over time, do you think that our business will also move in that direction or will we always give equipment on lease because otherwise if you look at the numbers of NCM, they are practically working on zero equity base because they just do not need any capital?

Kapil Agarwal: We are in three businesses whereas National Cine Media is only in one business. National Cine Media acquires advertising inventory of various cinema chains like Regal, AMC in the US and in lieu of that it gives them equity. Whatever revenue comes in, is distributed to cinema chains. NCM only acts as a marketing agency and not as a principal. It only aggregates advertising. There is another Company in the US called Cinedigm which invests in the equipment for these chains and gets lease rentals. We are a combination of both, Cinedigm and NCM, without giving any equity to cinema owners. National Cine Media works on 10-15% margin, like any other aggregator of advertising. Our advertising business is at 50% plus margin which should go up eventually as the numbers grow. Our business model is far superior than that of National Cine Media because they are attacking only one part of the business. We are collecting VPF, lease rentals, and also own the advertising in a large number of cinemas where we invest in the equipment.

Vaibhav Badjatya: I was not talking about it just from a margin perspective, but if you look at their ROCE profile it is quite attractive. But, I think with this model we can probably achieve larger scale. Secondly, due to the elections, do you expect that during the June quarter, our revenue will be impacted because Government advertising might be limited for 1-1.5 months and next quarter numbers will be lower?

Kapil Agarwal: So far as the Government advertisement revenue is concerned, there should be a drop in Q1.

Vaibhav Badjatya: But is it not that after 20th of May, they will advertise more and make up for the loss. Do you think there will be an absolute decline in numbers?

Kapil Agarwal: We do not know that yet. In the past, what we have seen is that after the declaration of results there is a process of formation of the Government, allocation of portfolios and transfers of bureaucrats. So, before decision making in the Government starts, it will take away a good part of Q1. So far as Government advertising is concerned, we do expect that there will be some reduction in Q1. However, Q1FY18 was not a very strong quarter for Government advertising and revenue from this segment was only ₹223 Mn in Q1FY18 while Q4FY18 was ₹541 Mn.

Vaibhav Badjatya: Last question is on Caravan - there has been substantial improvement this quarter, was political advertising a big contributor to this improvement?

Kapil Agarwal: This is partly due to political advertisements but the Corporate sector also saw an uptick.

Moderator: The next question is from the line of Nikhil Vaishnav from VD Investments.

Nikhil Vaishnav: Correct me if I am wrong, has ICICI Ventures, which was about to buy the remaining 34% of Qube shares, backed out after the NCLT Mumbai order?

Kapil Agarwal: That is right; we have also made a public disclosure on that. Originally, when we set out to do this merger two years ago, our market capitalization at that time was ~₹11,000 Mn. At that time, we were buying 55.29% shares of the four private equity players of Qube at equity valuation of ₹6,010 Mn for Qube. This translated to a total payout of ₹3,320 Mn to those 55.29% shareholders. Of this ₹3,320 Mn, ₹2,150 Mn was being acquired by ICICI Venture and ₹1,170 Mn by UFO, which shares would have got cancelled. Subsequently, we re-negotiated with them in December last year and brought down that figure from ₹3,320 Mn to ₹2,900 Mn. So, we saved ₹420 Mn there and ICICI Venture was still there. However, post the NCLT order, ICICI Venture decided to exit. We were re-negotiating this figure and were planning to bring it down substantially from ₹2,900 Mn. In the meantime, one and half years had passed and UFO had generated substantial cash, so we thought that entire amount could be bought in by us. So, ICICI Ventures exit really did not matter to us. If the deal happened now, we were in a position to buy out on our own the entire 55.29% equity which would have been very good for our shareholders because the dilution which was happening in favor of ICICI Venture could have been avoided.

Nikhil Vaishnav: Also, just want to understand if D-Cinema is the only technology where Hollywood movies are released?

Kapil Agarwal: Yes.

Nikhil Vaishnav: So, how much revenue have we earned from Avengers Endgame?

Kapil Agarwal: We do not have that number available because that is a post Q4 event, the movie released in the month of April.

Nikhil Vaishnav: What, if the NCLAT finds the same issues and dismisses our petition?

Kapil Agarwal: It does not matter because that deal of merger is off. Once ICICI Ventures withdrew in January, that deal is no more there. The only reason we have gone to NCLAT is because we firmly believe that the observations of NCLT are erroneous. So, the NCLAT decision is not going to affect the deal, we just wanted to satisfy our shareholders and our board and get those remarks expunged.

Moderator: The next question is from the line of Dipan Mehta from Elixir Equities Pvt Ltd.

Dipan Mehta: Just going back to the question which was asked on the sunset clause of D-Cinema, what is the quantum of loss for Q4FY19?

Ashish Malushte: In Q4FY19, because of improved performance the impact of sunset is near zero.

Dipan Mehta: And then you say Ashish that ₹140-160 Mn is your estimated loss from D-Cinema over 12 to 18 months. The way I understand it is that in FY19 you had ₹614 Mn of VPF from D-Cinema. This will come down to ₹480-500 Mn, is that correct?

Ashish Malushte: Slight modification in your understanding, you are looking at the gross level. At a net level, the net VPF revenue is ₹407 Mn for FY19 and likely to reduce by ₹140-160 Mn.

Dipan Mehta: Why is the E-Cinema VPF revenue not moving up? Is it because we have less number of cinema screens? The entertainment industry and box office collections grow at 10-12%, why does E-Cinema remains static?

Kapil Agarwal: Our E-Cinema revenue, it is not growing because the last price hike was in 2015 and the network is fairly stable. So, there is no reason for this to go up except for the release pattern of movies.

Ashish Malushte: In fact, to retain this pricing was a strategic call which we have been communicating to the market for the last 2-3 years.

Dipan Mehta: We have ₹1,398 Mn of investments. Is that mutual funds and excess cash?

Ashish Malushte: That is correct.

Dipan Mehta: And my last question is that what is the stickiness as far as cinema owners is concerned? What prevents them from moving to the competition, is it better service or higher revenue share in advertising? What are the key metrics which a cinema owner would consider for you versus the competitors, what are the leverages that you have over there?

Kapil Agarwal: Number one, we sign long-term agreements, but these are not unlimited period agreements. Obviously, agreements come to an end at some point of time and we do see movement. We are in a highly competitive market and we regularly lose cinemas to our competition. However, we are considered to be the best in terms of after sales service. The competition will take business away from us by agreeing not to charge rentals or foregoing the security deposit. So, these are commercial considerations because of which cinemas do move despite our level of service, which is the finest in the Country. After they move, whenever anything goes wrong with the system, the service does not reach the cinema and it loses 4-5 shows. Then they realize that the financial cost of moving away from UFO is far higher than saving the rental or the deposit. We regularly see this churn to our competitors as well as a similar number of cinemas coming back. The other consideration is advertising revenue share. If we give 25% revenue share, our competition may agree to share 60% of the revenue. However, when they move away they find that the 25% we were giving was far higher than the 50-60% which they get from our competition. We have always maintained that some cinemas will keep moving away and others coming back. That is why the network is stable except some very low-grade screens which are not getting the content, they keep shutting down, but that is again a smaller number.

Moderator: The next question is from the line of Shailesh Kumar from Sunidhi Securities and Finance Ltd.

Shailesh Kumar: Is it fair to assume that if we do not go for inorganic route, we are a fairly stable business and growth is difficult to come by?

Kapil Agarwal: One interpretation could be that. One is inorganic route - in the digital cinema business, we put in efforts to look for combinations and Qube was one such effort. The second growth driver is advertising revenues. Over the last 5-6 years, our advertisement revenue has grown at a CAGR of 19%. That growth could have been accelerated with the merger. However, we also continue working on various other growth opportunities about which we will keep sensitizing the markets from time-to-time as those opportunities mature.

Shailesh Kumar: What kind of topline growth you have been targeting?

Kapil Agarwal: Topline is the least important thing for us. We can increase our topline by increasing sale of equipment. In Q4FY19, revenue has gone up by ₹247 Mn because of sale of equipment in the Middle East. Today, our services business is at 30% plus EBITDA margin but equipment sales have 10-15% margin. We can take topline to ₹7,000 Mn by selling equipment but then margin will reduce. So, we have not been concentrating on the topline growth. Our effort always has been to grow the bottom line.

Shailesh Kumar: Is there something in the pipeline post this Qube deal falling through?

Kapil Agarwal: We keep working on growth opportunities and will keep sensitizing the market at the opportune time as they mature.

Moderator: The next question is from the line of Pritesh Chheda from Emkay Global Financial Services Ltd.

Pritesh Chheda: When I look at your Slide #12 and Slide #19, in Slide #12 I see reduction in E-Cinema and increase in D-Cinema. Why is that happening? And second, there is significant reduction in the screens on your advertising network. If you could just combine these slides and give your comments and are they interlinked by any chance?

Ashish Malushte: Slide #19 gives you the summary view of how the advertising network is built and how the multiplexes have grown. The previous slide that you mentioned covers not only the advertisement business network but is primarily the digital cinema business, also encompassing the screens where we do not have advertisement rights. So, in that sense, these two slides are not complete subsets of each other.

Kapil Agarwal: The general connotation which you may have is that multiplex screens mean D-Cinema and non-multiplex screens mean E-Cinema. That is probably how you are trying to correlate it.

Pritesh Chheda: My correlation is that you are adding D-Cinema screens and I am hoping that those are multiplex screens, but on the other hand there is 200 screens reduction in the advertisement business and why is there screens reduction?

Kapil Agarwal: If it is a multiplex screen it does not mean it is necessarily a D-Cinema screen and if it is a non-multiplex screen it does not mean that it is necessarily a E-Cinema screen. For example, if you go to New Excelsior or many single screens in Mumbai or elsewhere in the Country they are D-Cinema screens because they also run Hollywood movies. There are several cinema chains on our network where a five-screen complex will be there with two D-Cinema screens and three E-Cinema screens. There is no correlation between the number of E-Cinema or D-Cinema screens as well as E-Cinema or D-Cinema VPF. These are two mutually distinct things. That is point number one. Point number two, as we said overall there is a reduction of 200 screens over the past one year. We have always said and even today we have clarified that some low-grade screens either move to the competition or shut down. There is a cost benefit analysis that we do when any screen is going away - at what cost we should retain or revive it. We let them go because we need a more stable network, we need to grow our revenues based on the network that we have.

Pritesh Chheda: This time it is 200 screens, that eats away 5% of your advertisement sales growth. You have advertisement minutes growth and price growth, but there is 4% decline on account of screens reduction.

Kapil Agarwal: Our number of multiplex screens has also grown from 1,194 to 1,266. So, over one year 200 screens might have been lost but there is conversion to higher quality, higher revenue screens which are on the network and that is exactly where we also like to concentrate.

Pritesh Chheda: My other question is on this distributor and multiplex issue. Does our VPF income gets affected in any way incrementally or is there any risk?

Kapil Agarwal: We do not see any risk because we are not even a party to that dispute between the distributors and the multiplexes.

Pritesh Chheda: Your total E-Cinema count has reduced, but I do not see a corresponding reduction in E-Cinema VPF revenues despite no price increase being taken, is there any correlation?

Ashish Malushte: E-Cinema screens have gone down, but we have addressed this point partly. Majority of the screens moving out are low-end screens. So, the impact to our VPF revenues and rental revenues is minimal. Secondly, there is also a yield affect, while you have lost the screen, you would still be able to generate higher annual revenue because of a better yield.

Pritesh Chheda: What is the gross debt and net debt in the balance sheet?

Ashish Malushte: Gross debt is ₹780 Mn, including short-term and long-term, and gross cash is ₹1,969 Mn.

Pritesh Chheda: What would be your advertisement growth rate for in-cinema for FY20. It has not been a good year in FY19, if you could call out the reasons there and what is the growth rate for FY20?

Kapil Agarwal: We will stay away from giving any guidance for FY20. We will review it Q-o-Q and all the information will be public. So far as FY19 is concerned, we would not say that it has not been a good year because Corporate advertisement has seen 15% growth; Caravan has seen 173% growth from ₹89 Mn to ₹241 Mn. Government has seen 4% negative growth, which is very good because there were state elections in the month of November and at that time, 4-6 weeks of business was wiped out due to implementation of the model code of conduct. And then again, there was the general election. Despite these two events, we have still been able to almost maintain advertisement revenue which is good news and a good indication of the future.

Moderator: The next question is from the line of Shalabh Agarwal from Snowball Capital Investment Advisors LLP.

Shalabh Agarwal: You have explained the reasons why some screens move out of UFO's network. The question is what happens to the equipment, are we able to take it back or do we have to write it off? How does that work in terms of projectors and servers that we have installed?

Kapil Agarwal: By and large everything comes back, all our equipment is recovered and deployed elsewhere.

Shalabh Agarwal: If I look at the last annual report, there is a significant disposal from the gross block, more than ₹1,000 Mn. I was wondering if this was somehow related to the equipment that we are not able to procure and if it is not, then can you highlight what is that disposal?

Kapil Agarwal: We have two kinds of business. One is perpetual business, where we invest in the equipment, maintain it, replace it, earn VPF rentals and advertising revenue. However, when D-Cinema was introduced in 2010-11, there were certain chains where based on our agreements, after 5 or 6 years, we were supposed to transfer the equipment back to the chain. There, we did not have any perpetual rentals or advertising rights. We made money and transferred the equipment. So, the largest part of the disposal is the equipment which by agreement got transferred after 5, 6 or 7 years back to the multiplex cinema chains after we made a healthy profit on it. Actually, they also constitute a substantial part of our sunset business which we include in the sunset revenue shortfall.

Shalabh Agarwal: So, these would basically be D-Cinema screens?

Kapil Agarwal: Yes, D-Cinema screens. E-Cinema is never transferred.

Shalabh Agarwal: This process is still happening because depreciation this year remains more than Capex, which is why gross block and net block is coming down Y-o-Y?

Ashish Malushte: Absolutely right.

Shalabh Agarwal: There has been a tussle between distributors and certain cinema chains and UFO is not a party in that. Can you also tell us why we have not been named whereas others have been named?

Kapil Agarwal: The prime reason as we understand from market interactions with various parties is very simple. The distributor or the content owner treats multiplexes as their partners because they get a share of the revenue. So, when the content goes to the multiplex, revenues are shared 50-50 or other ratios depending on first week, second week, third week etc. Distributors contention is that multiplexes are our partners in content, they are sharing revenue, and they are partaking in the success or failure of the film. So, should they impose VPF on top of that? While they treat companies like UFO as third-party vendors, as leasing companies, as service providers who do not have any share in the content. They see us investing money, which is furthering their business, helping them release their movies not only in 3-4 multiplex cinema chains, which collectively have 1,700 screens, but in 4,000 screens, which is an additional 2,000-2,500 screens. If we do not collect VPF, we can’t maintain the equipment and the network will die down, which is counter-productive for the distributors. They release a movie at 4,000 screens and collect the upside by paying a small VPF, which is probably 1-2% of the total collection of the movie. So, it makes good commercial sense.

Shalabh Agarwal: What I want to know is given that you have such a large network that brings commercial benefits to distributors in terms of number of screens on which they can launch a movie, what holds us back from increasing rates. You mentioned that last time you increased rates was in 2015. You also alluded to the fact that if your advertising revenue goes up, you may start giving some discounts on VPF. Can you explain this dichotomy?

Kapil Agarwal: It is purely a commercial decision. We keep optimizing our advertisement footfalls versus the VPF revenues that we make. Every distributor thinks about ₹10,000 or ₹20,000 VPF paid to UFO for particular screens, they think if they should supply content to low grade cinemas where collection is only ₹20,000. The moment we increase VPF, there will be low grade cinemas that may stop receiving content. Once cinemas get content, more footfalls happen, which means more advertising revenue that is more beneficial to us than VPF of ₹200 or ₹400 per show. On the contrary, we are trying to revive screens which are low grade by not charging VPF. Those screens we have already started populating with distributors, here they do not give us fixed VPF but revenue share. It works for us as screens that are otherwise closing down start getting content, more footfalls happen, which helps us enhance advertising business and gives us some VPF revenue because our investment in the equipment is cost anyways.

Shalabh Agarwal: But then it is the same thing that multiplex chains are doing, getting a revenue share from footfalls. Then we go back to the same thing Mr. Screwvala has been challenging.

Kapil Agarwal: We do not. Revenue sharing will still happen between the exhibitor and the distributor. By providing the equipment and giving the distributor an additional 200-400 screens, which otherwise are not releasing his movie, they are partaking a small share of revenue. It is not a charge but a facility to the distributor.

Shalabh Agarwal: So, the way I understand it, VPF from a commercial perspective, there is no risk and you do it because you may get benefited from advertising?

Kapil Agarwal: Exactly. If we see the revival of low grade cinemas by reducing VPF, our benefit from advertising revenue is far higher. We are a media Company and cinema business is the backbone. Our main business is advertising. The moment you got more eyeballs, you are the #1 Company. If we make ₹10,000 Mn in advertisement revenue, even if VPF is zero, it does not really matter. The business plan is evolving, but till the advertisement revenue builds up, we have to make these charges. Eventually, these charges may go down and over a period of time, with substantial uptick in the advertising revenue, may be zero or negligible. I am not making a forward-looking statement; I am just giving a sense of how the model works.

Moderator: The next question is from the line of Vipul Shah from Sumangal Investments.

Vipul Shah: My question is that dividend and special dividend will be burning all the cash. So, hypothetically, if you go look at other inorganic opportunities, how will you fund them?

Kapil Agarwal: As on 31st March, our gross cash is ₹1,969 Mn. The working capital limits are zero utilized. In FY19, cash generation from the operating activity was ₹976 Mn. So, we are generating healthy amount of cash and are highly under-leveraged. First option was merger, inorganic growth by using the cash. Since, that is not happening immediately, normal dividend we have to pay anyway, which is ₹15 per share. We are paying ₹500 Mn in addition. By the time the Qube deal happens in the next few months, operating cash flow generated would be that much anyway. We have been criticized in the past for not distributing cash so we have had the courage of distributing 300% dividend which is a sort of record in today's market. This dividend is not going to compromise our ability to consummate the Qube transaction or other inorganic growth opportunities.

Vipul Shah: You said that Qube is not comfortable to come to the negotiation table at this price. At what price will Qube be willing to come to the negotiation table?

Kapil Agarwal: It is not Qube; it is the four private equity investors in Qube which own 55.29% of its equity. These are Intel, Nomura, CISCO and Street Edge. They invested in Qube 10-12 years ago and want to cash out. Qube's promoters believe in the future growth potential of the combined entity, so they are not cashing out. When we did the deal, our market capitalization was ₹11,000 Mn and we gave them ₹6,010 Mn of value for their equity. Since then, it is a continuous process of negotiation. The price they demanded, we were unable to meet that expectation. Promoters of Qube will do an equity swap; they will get UFO shares in lieu of their Qube shares.

Vipul Shah: But for all practical purposes, the Qube merger is off at least in the foreseeable future, should we assume that?

Kapil Agarwal: It is a continuing process. Currently we don't have a timeline. At this point of time, we have decided to move away from each other because of the expectations mismatch with external private equity shareholders of Qube. We have invested two years on this combination, Qube promoters and UFO promoters are very positive about it. We will come back to you at the appropriate time.

Moderator: The next question is from the line of Ritesh Bakshi from Padmee Capital.

Ritesh Bakshi: Could you shed some light on Nova Cinemaz and the future around it?

Kapil Agarwal: Nova Cinemaz has grown to 44 screens. We are now going back to the drawing board with learnings from the pilot and are currently analyzing how to grow that business more rapidly.

Moderator: The next question is from the line of Urmil Shah from IDBI Capital.

Urmil Shah: With the merger being distant right now, just wanted to understand the capital deployment from a longer term point of view. Before the Qube merger came onboard; it was largely the existing business and Nova Cinemaz. Also on hyper local growth, how should we look at it?

Kapil Agarwal: First of all, capital is intended to be deployed if inorganic growth opportunities including Qube happen. That is the first target. Without hampering the target, we have done capital distribution to the extent we could. Also, as we mentioned earlier, we continue to look at various avenues.

Moderator: The next question is from the line of Anand Bhavnani from Unifi Capital Pvt Ltd.

Anand Bhavnani: On our investments of ₹1,398 Mn, can you give me the breakup in terms of various instruments?

Ashish Malushte: It is entirely invested in liquid mutual funds and debt mutual funds.

Anand Bhavnani: On one hand we have ₹1,398 Mn in liquid mutual funds; on the other hand we have debt of ₹780 Mn. Are you planning to bring down short-term debt by liquidating the mutual funds?

Kapil Agarwal: We practically have no short-term debt. All the debt on the books is to fund equipment. When we buy equipment to install it in the theatres, we establish LC's, which normally get converted into four year debt. With reduced capital intensity, debt is automatically getting reduced and in the immediate future, we have no intention of repaying this debt.

Anand Bhavnani: So, is it fair to say that this investment in liquid funds is primarily intended for M&A opportunities and you want to keep it ring fenced, is my understanding correct?

Kapil Agarwal: Cash available with the Company is not only for M&A opportunities, we have to pay dividends now. Today, our dividend distribution obligation is ₹1,025 Mn.

Moderator: The next question is from the line of Vikas Jain, an Individual Investor.

Vikas Jain: What is the Capex done in FY19?

Kapil Agarwal: In FY19, Capex was ₹401 Mn.

Vikas Jain: And this year?

Kapil Agarwal: Capex is fairly stable, so it should remain in this range unless there is a different direction we would like to give to the current business in the interest of the Company. Last year we had given guidance of ₹600-700 Mn of Capex but our actual Capex is ₹401 Mn.

Vikas Jain: Could you help me get an understanding the breakup of ₹6,119 Mn revenue that we have across our three businesses, in terms of the percentage share? If you can, specifically tell me the revenue that we earned from the advertising vertical?

Ashish Malushte: Out of the total, advertisement revenue share is 39%; the revenue from distributors and digitization is 29%; and the revenue from exhibitors, which includes rental as well as sale of products is 32%.

Vikas Jain: Around ₹2,000 Mn to ₹2,500 Mn revenue comes from the advertisement vertical?

Kapil Agarwal: On a full year basis, out of ₹6,119 Mn, advertisement revenue is ₹2,372 Mn.

Vikas Jain: My next question is on receivables on the balance sheet, which is around ₹2,007 Mn; I understand from the conversation that most of it is outstanding from advertisement revenue.

Kapil Agarwal: We have clarified, 60% of the debtors is from advertisements.

Moderator: Thank you very much. That was the last question. I would now like to hand it back to Mr. Vikram Ramalingam for closing comments.

Vikram Ramalingam: Thank you everyone for attending the call. And special thanks to UFO management. Good day.

Moderator: Thank you very much. On behalf of UFO Moviez India Limited, that concludes the conference. Thank you for joining us. You may now disconnect your lines.

The transcript has been edited for language and grammar; it however may not be a verbatim representation of the call.