Zee Entertainment Enterprises Ltd

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Equity Research Desk

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Event update

Proposed merger between Sony Pictures Networks India and ZEEL

Recounting the series of events:

Subhash Chandra Goenka after gaining success in media business ventured into infrastructure, finance, education, cruise lines, among other enterprises. It was an audacious expansion but most of the companies drowned in a flood of debt. The total debt taken by the group was close to rupees 13,000 crores to fund its other businesses as well. What created a mess is that most of his stocks were pledged as collateral against loans availed by the group companies. In 2019 there was a claim on Essel group in relation to a huge deposit post demonetization (SFIO investigated Nityank Infrapower). Post this the share price plunged 33% intraday pulling down the market value by Rs 14,000 crores. He admitted that he had made some incorrect bids in Essel Infra and the acquisition of Videocon D2H was a mistake. Selling his shares at the beaten-down price was the only option. A clutch of institutional investors bailed out the promoters of ZEEL by buying a stake. The ownership of the promoter group reduced from 41.62% to 3.99% currently.

Shareholder activism to re-jig boardroom:

On September 11, Zee Entertainment's largest shareholders, Invesco Developing Markets Fund and OFI Global China Fund holding 17.88% together, called for the removal of the company's MD and CEO Punit Goenka (son of Subhash Chandra Goenka) as well as two of the company's long serving independent directors, Ashok Kurien and Manish Chokhani. The latter two have resigned prior to the AGM. Further, institutional investors have also suggested inducting six new names into the board. While the existing management had taken steps to improve corporate governance & disclosure practices, given that the promoter shareholding was just 4% odd, a rejig was expected. A spokesperson for US-based Invesco said the fund has been an investor in Zee for more than a decade and has "initiated this action to strengthen board governance at the company".
The two institutional investors have called for an extraordinary general meeting (EGM) to seek shareholders' views on the board reshuffle.

Sony Pictures Networks India comes to the rescue of Zee Entertainment:

Zee Entertainment Enterprises (ZEEL) on 22nd September announced that its board of directors at a meeting held on 21st September, unanimously provided an in-principle approval for the merger with Sony Pictures Networks India (SPNI). SPNI will infuse $1.575 billion as growth capital. However, with the proposed infusion of growth capital into SPNI, the resultant merger ratio is expected to result in 47.07% of the merged entity to be held by ZEEL shareholders and the balance 52.93% of the merged entity to be held by SPNI shareholders. The merged entity will be a publicly listed company in India. The promoters will be allowed to increase their shareholding from 3.99% upto 20% over a period of time as per the applicable law. The combined entity will own 75 TV channels, two video streaming services (ZEE5 and Sony LIV), two film studios (Zee Studios and Sony Pictures Films India) and a digital content studio (Studio NXT), making it one of the largest entertainment networks in India. The merged entity will approximately have 27% market share in the television network business. The final transaction will be subject to completion of customary due diligence, required corporate, regulatory and third party approvals including the votes of Zee's shareholders.

Outlook:

Decision by Zee enterprises to merge with Sony Pictures is in the best interest of all the stakeholders. The merged entity will have strong viewership as Sony is doing well in GEC (general entertainment) whereas Zee has a strong position in the regional categories. The merged entity will also be strong in the OTT space given the merged entity has a powerful library of movies and other content. Merged entity will also have balance sheet strength as Sony has committed to invest additional USD 1.575 bn. While the details of share swap ratio are awaited, we believe this event is a turning point for Zee shareholders. All the concerns relating to related party transactions, corporate governance etc should recede with this proposed merger. The stock has reacted positively to the news with a 25% jump. We believe long term investors can accumulate the stock even at current prices as we see strong rerating happening in the coming years.

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