

CME

Buy

Shares punished too much on sector de-rating

01/07/2008

Previously: US\$116

Bloomberg: CETV US/CETV CP

Price: US\$87.3

12-mth target: US\$125

- CME closed the acquisition of a 30% stake in Studio 1+1, which gives it the highly needed complete control over the decision-making process.
- We raise our SOTP TP by 8% and maintain our BUY rating. We view the current weakness in the share price as BUYing opportunity.

CME increased its stake in Studio 1+1 Group to 90%. CME completed the acquisition of a 30% equity stake in Studio 1+1 Group in Ukraine from local partners for a total consideration of US\$220m. The company has a call option for the remaining 10% stake, which it can execute at the price of US\$94-109m. Renewed licence for Studio 1+1 already reflects the new ownership structure.

Hands free to do the reset. The transaction gives CME full discretion over important issues (eg, recruitment, programming and investments decisions, advertising sales strategy or development of thematic channels). The reset of the Ukrainian operations will likely be a time-consuming process, the effects of which should make a difference to the company's income statement starting from 2009 rather than 2008. Political and macro instability continue to provide a challenging environment in Ukraine, but we remain confident that the TV ad spend should grow by 30% this year in Ukraine. We understand CME plans to give guidance for Ukrainian operations sometime in 3Q08, most likely in September. We currently expect Ukraine to report 2008F and 2009F segment EBITDA of US\$31m and US\$60m, respectively, and to reach segment EBITDA margin of 40% in 2012F.

BUY maintained. We recommend using the current weakness in the share price to purchase CME shares. We believe the fall in CME shares is unjustified and related to global sentiment, the de-rating of the media segment in the region and not to CME's fundamentals. The stock is trading at a 2009F EV/EBITDA of 11.7x vs 9.9x for TVN and 10.9x for CTC Media. We expect the share price to be driven by: (1) continued strong earnings delivery; (2) guidance for Ukraine to be announced most likely in September and (3) the restructuring of Ukrainian operations, which makes the CME story compelling to us in the long term.

Forecasts and ratios

Year to Dec	2004	2005	2006	2007	2008F	2009F	2010F
Revenue (US\$m)	182	401	603	840	1,100	1,218	1,347
EBITDA (US\$m)	26	80	185	264	367	428	469
Net income (US\$m)	19	42	20	89	186	244	280
EPS (US\$)	0.55	1.19	0.50	2.12	4.41	5.76	6.61
PER (x)	158.7	73.4	174.6	41.2	19.8	15.1	13.2
EV/EBITDA (x)	90.6	46.8	21.0	15.7	11.7	9.6	8.2
P/BV (x)	11.9	5.4	3.6	2.6	2.3	2.0	1.7
ROE (%)	5.5	8.6	3.0	7.3	12.5	14.2	14.0

Source: Company data, ING estimates

12-month forecast returns (%)	
Share price	43.7
Dividend	0.0
12m f'cst total return	43.7

Key ratios		
	2008F	2009F
EBITDA margin (%)	33.4	35.1
Operating margin (%)	26.5	29.1
Net debt/equity (%)	38.2	23.4
DPS (US\$)	0.0	0.0
Dividend yield (%)	0.0	0.0

Quarterly data		
(US\$m)	4Q07	1Q08F
Revenue	301.0	223.5
Segment EBITDA	128.6	74.7
EBIT	97.8	44.7
Net income	73.0	14.9

Share data	
No. of shares (m)	42.3
Daily t/o (US\$m)	40.0
Free float (%)	82.1
Mkt cap (US\$m)	3,830

Share price performance



Source: Reuters

CME has taken steps to improve sell-out ratios in low season quarters this year. The company used incentives for advertisers to migrate some of the TV ad spend from 2Q08 to 1Q08 and the incentive for the advertiser was a visibly lower cost-per-point (CPP) in 1Q compared to 2Q. In the high sell-out 2Q the rating of the commercial break (on the basis of which we understand CME sells a majority of its inventory) could be up to 30% lower than the rating of the broadcast because the breaks have maximum length. By moving sold rating points to 1Q CME hopes to achieve more spread out rankings of the breaks and maximise its effective average prices in individual markets. Management expects to increase the effective price as measured by CPP metrics by more than 50% in Romania and more than 20% in the Czech Republic.

We increased our profits estimates for CME following the release of 1Q08 results, stronger advertising revenue in Czech Republic due to the successful efforts to increase sell-out ratios in 1Q08, higher estimates for non-advertising revenue in a number of markets as well as following revisions in assumptions on FX rates, particularly for Czech koruna and Romanian lei. We increase our 2008F EBITDA and net profit estimates by 7% and 8%, respectively and 2009F EBITDA and net profit estimates by 7% and 8%, respectively.

Fig 1 Revision in segment EBITDA estimates by country

US\$m	2008F EBITDA			2009F EBITDA		
	Old	New	% change	Old	New	% change
Czech Republic	176	200	14	182	210	16
Romania	126	128	1	140	143	2
Ukraine	31	31	1	60	60	(1)
Slovakia	53	53	0	56	56	(1)
Slovenia	28	28	1	27	30	9
Croatia	0	0	N/A	11	11	3
Group segment EBITDA	414	440	6	476	510	7

Source: ING estimates

Fig 2 Revision in estimates

US\$m	2008F		% change	2009F		% change
	Old	New		Old	New	
Revenue	1047	1,100	5	1152	1218	6
EBITDA	344	367	7	398	428	7
EBIT	271	291	7	329	355	8
Net profit from continuing operations	172	186	8	225	244	8
Diluted EPS, US\$	4.07	4.41	8	5.31	5.76	9

Source: ING estimates

Following the upward revision in our earnings estimates, we increase our sum-of-the-parts based target price for CME by 8% to US\$125. CME shares declined 18% in the last month driven by an earlier sector de-rating and the overall weakness of the US equity market. The shares trade at a respective lower-than-historical 13% and 6% premium to average 2008F EV/EBITDA and PER multiples to the average for TVN and CTC Media. We expect that premium to widen as management should be able to turn around Ukrainian operations successfully as it did with its Czech and Slovak acquisitions in the past. Ukraine is only an upside for CME. The Ukrainian market is already the largest of all CME markets as measured by the value of TV ad spend, but it was the second smallest for CME by segment EBITDA contribution last year.

Fig 3 SOTP valuation of CME based on DCF models on country basis

Country	Station	EV	Implied 2008F EV/EBITDA (x)*	Economic stake	Proportionate EV
Czech Republic	TV Nova	2,161	10.8	100	2,161
Slovakia	Markiza	682	12.9	100	682
Ukraine	1+1	988	31.5	90	889
Romania	Pro TV Group	1,370	10.7	95	1,301
Slovenia	POP TV	207	7.3	100	207
Croatia	Nova TV	199	9.9	100	199
Total enterprise value					5,439
Net debt					747.6
Equity value					4,692
# of shares, m					42.3
Fair value, US\$					111
Target price, US\$					125
* 2009F EV/EBITDA for Croatia					

Source: Company data, ING estimates

Fig 4 Media valuations

	Country	Rec	Current price	Target price	Tot rtn (%)	Mkt cap (US\$m)	EV/EBITDA (x)			PER (x)			
							2008F	2009F	2010F	2008F	2009F	2010F	
RBC	Russia	Buy	US\$	9.00	12.3	36.1	1,071	9.2	6.1	4.2	16.7	11.0	8.5
Rambler Media	Russia	Hold	US\$	27.0	45.3	68.0	408	10.1	7.2	5.2	13.8	10.3	8.2
CTC Media	Russia	Hold	US\$	25.4	30.9	21.8	3,855	10.9	8.2	6.4	22.6	17.8	14.7
CCI	Poland	Hold	PLN	23.9	27.8	16.3	572	10.1	8.4	7.5	17.6	13.9	12.5
TVN	Poland	Buy	PLN	17	24.8	48.7	2,805	9.9	8.6	7.6	15.0	12.3	9.8
Agora	Poland	Buy	PLN	33.5	57.6	76.4	869	6.9	5.7	4.6	14.6	11.8	9.6
Average								9.5	7.4	5.9	16.7	12.9	10.5
Average TV								10.4	8.4	7.0	18.8	15.1	12.2
CME	Czech Republic	Buy	US\$	87.3	125	43.7	3,694	11.7	9.6	8.2	19.8	15.1	13.2
<i>Premium/(discount)</i>								23.1	30.8	39.0	18.6	17.8	25.4
<i>Premium/(discount)</i>								12.8	14.6	17.8	5.5	0.5	8.1
<i>to average for TV</i>													

Source: ING estimates

Risk factors

CME derived 90% of its revenue in 2007 from TV advertising; we expect the revenue mix to remain highly geared to TV advertising in the future. We have assumed certain growth rates for TV ad spend in individual markets and certain market shares for CME stations. Specifically, we assume CME would capture 50% TV ad market share in Romania, 60% in the long term and even higher in the medium term in the Czech Republic. Our estimates and target price would change materially should CME stations fail to achieve these targets.

We have incorporated a significant element of expansion in the segment EBITDA margin in the Ukraine from 17% in 2007 to 49% in 2015F. Competition in this market is fierce and stronger for CME than in the Czech Republic or Slovakia and we believe the success of CME's stations will depend on the right choices of programming, advertising sales strategy and co-ordination of multi-channel rollout, among other issues. While CME has an impressive track record of restructuring broadcasters after taking full control the challenge in Ukraine is greater. Our estimates and target price would change materially should CME's Ukrainian stations miss our margin estimates.

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