

May 2018 Strategic case study examination

Pre-seen material



*FINANCIAL ANALYSIS*  
*BY*

*R. SHYAM PRASAD*

# *R. Shyam Prasad*

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- ❖ Member of CIMA from 2013
- ❖ Member of ACCA from 2014
- ❖ Postgraduate with MBA Finance
- ❖ Teaching CIMA & ACCA for last 5 years
- ❖ Studying is my hobby. Cleared CFA level 1, ICWAI Inter.
- ❖ Interested in Solving Case studies,
- ❖ Passionate in teaching Financial Management, Management Accounting, Strategic Management.
- ❖ Currently involved Edu start up “**Wowacademics**”

# Financial Analysis

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RATIO, COMMONSIZE STATEMENT, COMPARATIVE STATEMENT

Comparative Analysis of CW & HV										
		Couchweb		HomeVideo						
Performance analysis in private sector orgs		2018	2017	2018	2017	Comments				
Shareholders ratio										
	Earnings per share (EPS)	0.4	0.3	0.3	0.4	Comparatively better than HomeVideo				
	<b>Note: Nominal or face value of share is assumed to be M\$1</b>									
	Price Earnings (PE) ratio	467.9	374.5	Share price information not given		Very high. Due to high expectation on future growth.				
						This is due to assumption of Face value				
	Dividend per share (DPS)	No information is given		No information is given						



The following information has been extracted from Couchweb's financial statements for the year ended 30 April 2018

**Couchweb**  
**Consolidated statement of profit or loss**  
**For the year ended 30 April 2018**

	<b>2018</b>	<b>2017</b>
	<b>M\$m</b>	<b>M\$m</b>
Revenue	13,226.0	10,823.8
Cost of sales	(9,192.1)	(7,446.4)
Gross profit	4,033.9	3,377.4
Research and development expense	(1,069.5)	(854.2)
Other operating expenses	(1,880.2)	(1,630.0)
Operating profit	1,084.2	893.2
Finance costs	(184.0)	(170.0)
Profit before tax	900.2	723.2
Income tax expense	(215.8)	(195.9)
Profit for year	684.4	527.3

**One hit series can give M\$ 400 - 600 mn Gross profit.**  
**Approximately:**  
So this 2018 Gp is culmination of  $4000 / 600 = 7$  Hit series

Couchweb  
Consolidated statement of financial position  
As at 30 April 2018

	2018 M\$m	2017 M\$m
<b>Non-current assets</b>		
Content	9,463.5	7,972.4
Other intangible assets	520.1	342.6
Property, plant and equipment	378.2	296.3
	<u>10,361.8</u>	<u>8,611.3</u>
<b>Current assets</b>		
Content	4,652.7	3,812.8
Cash and cash equivalents	1,942.6	1,533.5
	<u>6,595.3</u>	<u>5,346.3</u>
<b>Total assets</b>	<u><u>16,957.1</u></u>	<u><u>13,957.6</u></u>
<b>Equity</b>		
Share capital and share premium	1,830.0	1,580.0
Retained earnings	1,813.3	1,426.7
	<u>3,643.3</u>	<u>3,006.7</u>
<b>Non-current liabilities</b>		
Loans	5,321.0	4,470.0
Non-current content	3,245.4	2,348.3
Deferred tax	245.6	232.1
	<u>8,812.0</u>	<u>7,050.4</u>
<b>Current liabilities</b>		
Content	4,283.1	3,711.0
Current tax	218.7	189.5
	<u>4,501.8</u>	<u>3,900.5</u>
	<u><u>16,957.1</u></u>	<u><u>13,957.6</u></u>

In line with industry practice, Couchweb shows the cost of creating or licensing content as an asset, amortised over the useful life of those rights. Content that is expected to be amortised within 12 months is shown under current assets and content that is expected to be amortised beyond 12 months is shown as non-current.

The unpaid costs associated with acquiring content are recorded as liabilities, either current or non-current depending on whether payment is due within 12 months or beyond.

Comparative Analysis of CW & HV									
		Couchweb		HomeVideo					
Performance analysis in private sector org:		2018	2017	2018	2017	Comments			
<b>Profitability ratio</b>									
	Capital Employed	12455.3	10057.1	10083.7	6704.8				
	ROCE	8.7	8.9	7.0	12.4	ROCE is low, As Company seems to be buying/Creating more content thereby increasing Capital employed			
	Operating Profit ratio	8.2	8.3	7.4	9.7	Operating profit is low, because of ???			
	Gross Profit ratio	30.5	31.2	27.9	27.9	Gross Profit ratio is healthy.			



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Performance analysis in private sector orgs		2018	2017	2018	2017	Comments			
<b>Liquidity ratio</b>									
	Current ratio	1.5	1.4	2.0	2.0	Current ratio is slightly lower than HomeVideo			
	Quick or Acid test ratio	8.9	8.1	11.8	7.6	CouchWeb has high cash & cash equivalents compared to Tax payable			
	Without content								
	With Content	0.43	0.39						
	Inventory turnover ratio	Not applicable		Not applicable					
	Receivables turnover ratio	No information is given		No information is given					
	Payables turnover ratio	No information is given		No information is given					
	<b>Note: Customers payment in advance is not shown in the balance sheet explicitly</b>								
	Working capital turnover	6.3	7.5	3.5	3.5	CouchWeb uses its working capital better than HomeVideo			



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Comparative Analysis of CW & HV									
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Performance analysis in private sector org:		2018	2017	2018	2017	Comments			
Capital Structure Ratio									
	Capital Gearing ratio	2.4	2.3	2.6	1.7	Gearing of 2.4 in 2018 is very high & aggressive.			
	Interest coverage ratio	5.9	5.3	4.0	8.3	Interest coverage ratio of 6X indicates that Finance cost can be paid easily.			
	Income tax Expense	24	27	24	27				



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**Table indicating Operating profit on Serial**

<b>Page 9</b>							
<b>First TV Programme</b>							<b>million</b>
Revenue		40 million viewers x m\$12 x 3 months / 3 device					480
Cost of production		m\$ 6.8 mn x 13 episodes					88.4
<b>Operating profit per serial</b>							<b>391.6</b>
<b>2nd &amp; 8th TV Programme</b>							
Revenue		60 million viewers x m\$12 x 3 months / 3 device					720
Cost of production		m\$ 8.2 mn x 13 episodes					106.6
<b>Operating profit per serial</b>							<b>613.4</b>

## Own productions

In 2012, Couchweb conducted a survey of subscribers' viewing habits and discovered that it was becoming increasingly common for them to watch the whole of a new season of a programme over a weekend or over two or three consecutive evenings. The survey, backed up with data gathered from the website, also indicated the factors that attracted viewers. Couchweb realised that it could use this information to commission TV programmes that would attract large viewing figures.

Couchweb started to commission its first TV programme, a crime serial called 'Tumbling Down', aiming for a target audience of 40 million viewers. For the first season of 13 episodes, Couchweb hired a freelance creative director and production team and gave them a budget of M\$6.8 million per episode.

Production took eight months and the resulting programme was so popular with viewers that a second season was commissioned, with a budget of M\$8.2 million per episode. Even with this increased budget, the programme is relatively cheap to produce in comparison to other popular shows. It relies on good writing and excellent acting to develop story lines rather than special effects and other expensive elements.

Tumbling Down is now in its eighth season, with viewing figures averaging 60 million per season. All eight seasons still attract healthy viewing figures both from new subscribers and from those who enjoyed it enough to watch it again.

Tumbling Down remains one of Couchweb's most popular programmes, although it has proven to be the first of many successful programmes and even movies. 'The Politics Game' is presently Couchweb's most popular TV programme, attracting higher viewing figures than many of the more expensive programmes purchased from the major studios.

### Viewer Habits

- So customers will not pay 12 monthly subscription fee. Rather they will pay fewer monthly payments and binge watch serials.
- This causes less & unpredictable income

Viewers 40mn to 60mn viewers.



**Table indicating Cash raised & spent on Content creation**

**Issued Equity Share for M\$250 mn**

Either retained earnings is used for content production or Dividend seems to be declared in 2017.

				Opening reserve	1,426.70		
				2018 Profit	684.4		
<b>Issued loans for M\$850 mn</b>				<b>Decrease in RE</b>	<b>-297.80</b>		
<b>Unpaid content for M\$900 mn</b>				Closing Reserve	1,813.30		
New Content NCA =			1,491.10				
New Content CA =			839.90				
<b>Total cash spent on New Content</b>			<b>2,331.00</b>				
Equity =			250.00				
Debt =			851.00				
Non-current liability content =			897.10				
Current liability content =			572.10				
Decrease in reserve =			297.8				
<b>Total cash raised for New Content</b>			<b>2,868.00</b>				

# Key Findings - Ratio Analysis

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- ❖ 25% Increased Spending in R&D YoY
- ❖ Profit increased (30% YoY) faster than the revenue (22% YoY)
- ❖ M\$ 1491 mn of New Content created in 2018 which is 4X the PAT
- ❖ 51% Increased Spending in Other intangible assets for 2018
- ❖ In 2018 Content Asset alone is  $NCA + CA = 56 + 27 = 83\%$  of Total Asset.
- ❖ In 2018 Content Unpaid is  $CL + NCL = 19 + 25 = 44\%$  of Total liability

# Key Findings - Ratio Analysis

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- ❖ Company has used M\$300 mn from Retained earnings
- ❖ Aggressive Content creation
- ❖ Currently each serial gives an Revenue of M\$ 720 mn, cost of creation is M\$106 mn & operating profit of M\$613 mn
- ❖ Inshort if successful an serial can give 6X return or 600%
- ❖ ROCE is low, because of Company seems to be buying/Creating more content thereby increasing Capital employed
- ❖ Gearing of 2.4 in 2018 is very high & aggressive.
- ❖ Interest coverage ratio of 6X indicates that Finance cost can be paid easily.

# Reach me @

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Thank you

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