

Wolves of Paseo

Media and Entertainment Sector
Philippine Stock Exchange (PSE)

ABS-CBN Corporation

Date: 06/11/2019
Ticker: ABS:PM

Current Price:
PHP18.6

Recommendation: Buy
Target Price: PHP31.8

Market Profile

Closing Price (PHP)	18.58
52-Week Range	16.80 – 25.30
Average Volume (PHP'000)	213.5
Shares Outstanding (Millions)	861.97
Market Cap (PHPbn)	15.07
Dividend Yield	2.96%
P/E (ttm)	5.47

Source: MarketWatch

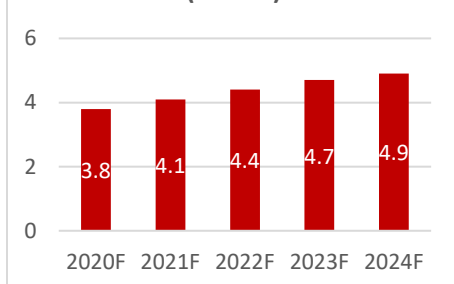
We issue a BUY recommendation for ABS-CBN Corporation (ABS) with a target price of PHP31.8, representing a 71% upside from its closing price of PHP18.6 on 06 November 2019. We arrived at our target price using the Discounted Free Cash Flow to Equity method.

Strong Core Business Anchored on Growing Consumption

Consumer Spending is expected to pick up in the next few years as inflation levels out and labor market strengthens. Furthermore, spending will also be supported by continuously strong inflows coming from remittances.

Outlook towards the labor market and unemployment is positive, with unemployment maintaining its low level. In addition, the higher minimum wage will increase disposable income which will eventually translate to consumption. ABS is well positioned to reap the benefits of this trend as it remains to be the leading media company in the Philippines. It consistently leads the industry based on rating agencies.

Figure 1. Forecasted EPS (in PHP)



Source: Team Estimates

Ratios	2019F	2020F	2021F	2022F	2023F	2024F
Gross Margin	41%	40%	40%	40%	40%	40%
Net Profit Margin	7%	7%	7%	8%	8%	8%
Current Ratio	3.0	3.1	3.2	3.4	3.5	3.6
Debt-to-Equity	0.9	0.8	0.7	0.7	0.6	0.6
Return on Asset	4%	3%	4%	4%	4%	4%
Return on Equity	9%	8%	8%	8%	8%	7%
Earnings per Share	3.8	3.8	4.1	4.4	4.7	4.9

Business Description

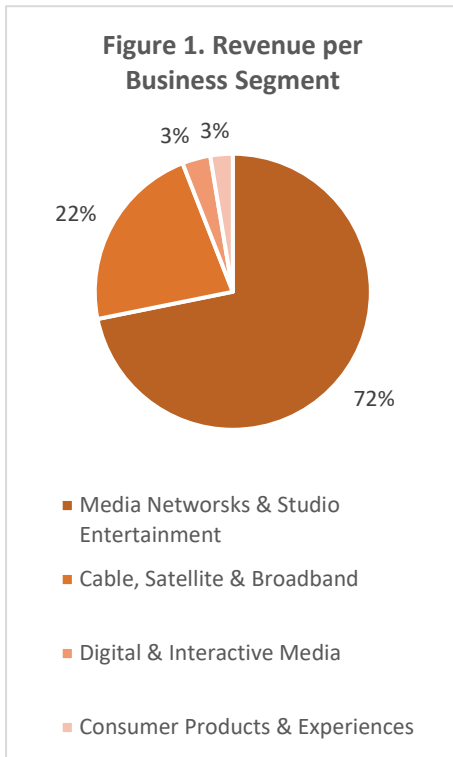
ABS is the Philippines' leading media and entertainment organization. The Company is primarily involved in content creation and production for various media including television, online and over-the-top platforms, cable, satellite, cinema, live events, and radio for domestic and international markets. ABS-CBN also operates various platforms including domestic television and radio networks and worldwide OTT and online platforms. ABS-CBN also has interests in cable, satellite, and broadband systems in the Philippines.

In addition, ABS-CBN has business interests in music and music publishing, consumer products and licensing, multi-media services, magazine and book publishing, production and post-production services, cargo forwarding, TV shopping services, theme park development and management, property management, and food and restaurant services, all of which complement and enhance the Company's strength in content production and distribution.

Maintaining a Strong Core Business

ABS maintains to be the number one network in the Philippines and dominated ratings across all time blocks in 2018. Cable, satellite, and broadband sales continue to grow; ABS-CBN TVplus sold 2.75 million boxes (29% over its annual target), leading to a cumulative total of 6.78 million boxes since its launch 3 years ago. Sky Direct, its Direct-to-Home service, ended the year with 937,000 subscribers and crossed the 1 million subscriber mark in January 2019 – barely 3 years after its launch. ABS-CBN News continued to produce the most-watched news program in the Philippines via TV Patrol, while DZMM held on to the number one spot on AM radio. In FM radio, MOR remained the number one station in Metro Manila and various parts of the country.

Despite the challenges presented by the domestic feature of the film industry, ABS-CBN Films has

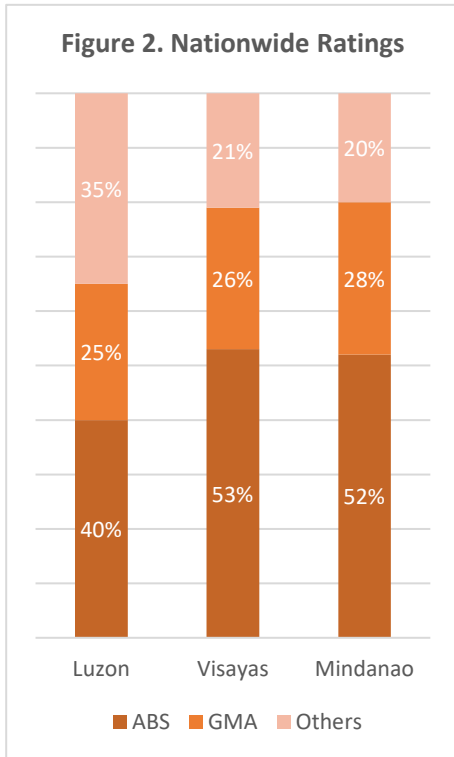


Source: Annual Report

continued to perform well. It holds the all-time Philippine box office record-holder with PHP700 million in local gross receipts and over US\$2 million in international receipts.

Transforming for the Future

Beyond strengthening its core media platforms, ABS ventured into international expansions, digital sales reinvention, and increasing its themed experiences business. Revenues from international syndication grew 30% year-on-year and accounted for 15% of the total revenue in 2018. Digital is ABS' fastest-growing business accounting for nearly a billion pesos in revenues from combined digital advertising revenues representing 13% of the total. In growing the themed experiences business, ABS launched "The Kapamilya Theater"—the first and only 4-dimensional production "ASAP 4D," which immerses the audience in the all-star show as if the performances were happening live. Concerts, mall shows, roadshows, and many other pocket events completed the themed experiences initiatives. These initiatives delivered 53% revenue growth from 2017, 460,000 face-to-face engagements, and close to PHP1.6 billion in revenues.



Source: Annual Report

Other key developments in ABS include the license acquisition from Zeno Media and partnership with Telaria Inks which bring the company's content to other digital platforms. The licensing with Zeno Media provides an opportunity for ABS to have its content and ABS-CBN Radio will be available in both App Store and Google Play Store to be available to the diaspora communities around the world. The Partnership with Telaria, ABS will work with the Telaria's Video Management Platform (VMP) to manage and monetize their OTT video inventory across all screens.

According to ABS reports, the earnings for the first and second quarters of 2019 have garnered higher sales compared to 2018. For the first quarter, the company announced sales were PHP10,358.23

million compared to PHP9,010.37 million and the net income of PHP 856.35 million compared to PHP452.53 million last 2018. For the second quarter, the company announced sales were PHP10,444.03 million compared to PHP 9,925.83 million a year ago and the net income was PHP 695.80 million compared to PHP397.36 million a year ago.

ABS has also announced that it intends to exercise its option for early redemption of its seven year bonds (due February 2021). It also executed a PHP5 billion term loan agreement with UnionBank of the Philippines (PSE:UBP). The loan shall be used to partially finance the Company's capital expenditures and general corporate requirements. This presents that the media & entertainment, telecommunication service still has potential growth especially in the growing digital media which ABS has also been making strategic moves to bring its content to the digital platform.

Corporate Governance

ABS recognizes that to be able to fulfill its mission of being in service of the Filipino, it has to retain the trust of its stakeholders and remain attractive to investors to maintain long term success. In 2019, the Company was the only media network in the country awarded by the Institute of Corporate Directors (ICD) for outstanding corporate governance. We evaluated ABS-CBN's corporate governance practice in terms of the following:

Board: Established programming, audit, risk management, compensation, nomination, succession planning, and corporate governance committees

Sustainability: Formalized a sustainability program in 2018 building from legacy corporate social responsibility programs launched in the 1990s.

Transparency and Disclosures: ABS is fully compliant to SEC's requirements for disclosure on its Integrated Annual Corporate Governance Report. The company also discloses its ESG performance following the Global Reporting Initiative (GRI)

Standards and aligns it to the UN Sustainable Goals for Development (SDG).

Stakeholder Engagement: ABS ensures a mutually beneficial relationship with its stakeholders and respects their rights as provided in the Company's Corporation Code. Customer's welfare, supplier/contractor assessments, and creditor's rights are upheld to the highest possible standards.

Shareholder's Rights: Stockholders, including minority shareholders, have the right to nominate candidates for the Board of Directors. As provided by law, ABS-CBN provides timely and transparent information about the Company to its shareholders and are encouraged to attend annual meetings.

Audit: A designated Chief Audit Executive (CAE) oversee, along with the Board, the internal audit activities of the Company including that outsourced to third parties.

Sustainability

ABS was founded 65 years ago with a mission to serve the Filipino People. As a media organization, it puts a premium on maintaining its responsibility toward its audience, its people, and the society as a whole to create sustainable value through innovative solutions in the delivery of meaningful content. ABS-CBN focuses on seven key areas: Overseas Filipino Welfare, Health and Wellness, Child Welfare, Humanitarian Relief, and Rehabilitation, Education, the Environment, and Livelihood and Employment.

Even before sustainability became a buzzword in the business community, ABS was already championing social responsibility and community welfare through the Lingkod Kapamilya and Bantay Bata 163 programs. Founded in 1997, Bantay Bata 163 is the first and only media-based helpline for children's welfare and victims of domestic violence.

Industry Overview and Competitive Positioning

Global Trends in Entertainment and Media

The global entertainment and media industry is forecasted to expand at a 4.3% compounded annual growth rate from 2018 to 2023 reaching USD2.6 trillion. The increasingly mobile environment augurs well for the industry's income-led by virtual reality (VR), over-the-top (OTT) platforms and internet advertising. VR headset adoption is supported by the 5G network. Meanwhile, by 2023, it is forecasted that more than half of the advertising budget will go to digital advertising.

Philippine Economic Outlook

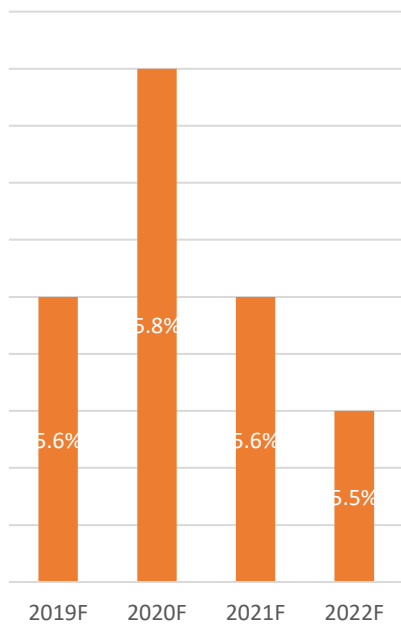
The country's GDP is projected to remain robust expanding at growth rates of between 5.5% to 5.8% from 2019 to 2022. GDP growth is expected to be supported by government spending and household consumption. Private consumption is assumed to continue to grow given the lower inflation, higher real wage, and steady remittances growth.

Philippine Consumer Industry

The benign inflation rate, strong labor market, and steady OFW remittances are expected to boost consumer spending and disposable income in the next few years. Private consumption is expected to grow by 5% in 2020.

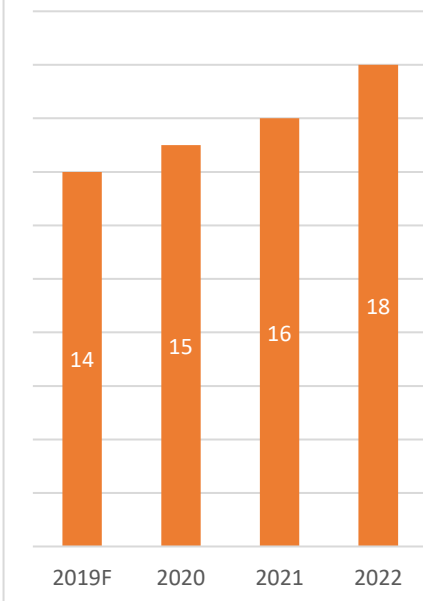
Household spending on recreation and culture averaged at about 5% of total consumption and growing by 3.5% per quarter for the past three years. However, as a result of the growing price sensitivity of Filipinos, consumer spending on non-essential segments are expected to be lower over the medium term.

Figure 3. Forecasted EGDP Growth



Source: Oxford Economics

Figure 4. Household Spending (in PHPbn)



Source: Business Monitor International

Increasing Consumer Base for Free Television (TV) and Digital Media

The consumer base of TV sets and mobile phones is continuously growing. In 2019, over 80% of the 24.88 million households in the Philippines own a color TV set. This number is expected to increase to 86.2% of households in 2024. Similarly, cable TV consumers are also expected to increase.

At present, 90% of households in the Philippines own a mobile phone, while 61.7% own a smartphone. By 2024, 94.4% of households will own a mobile phone, while 82% will own a smartphone. This large consumer base will bode well for ABS's OTT and digital media businesses

Electronics Penetration Rate	2018	2019	2020	2024
Number of Households (in million)	24.4	24.9	25.4	27.4
% of Households with Color TV Set	80.6	81.7	82.6	86.2
% of Households with Cable TV	36.8	37.2	37.7	39.3
% of Households with Mobile Phones	89.8	90.7	91.6	94.4
% of Households with Smartphone	56.2	61.7	66.8	82.0

Source: Euromonitor

Competitive Analysis



Source: Team Estimates

At present, there are 11 commercial free-to-air television stations in Mega Manila with GMA Network Inc. as its major competitor. Other competing stations are ABC 5 and three stations owned and operated by the Philippine government. In terms of radio stations, on the other hand, there are over 21 in Mega Manila. These media networks are primarily competing for advertising and airtime revenues. Globally, ABS also compete with other cable and satellite service providers who cater to Filipino communities abroad. Film and music production also pose a similar competitive environment. Based on Kantar Media Tam, ABS accounted for 44.6% channel share for free-to-air TV in 2018.

GMA Network Inc. is a major player in the industry that launched similar products as ABS. Like ABS, GMA also has its film production studio, Filipino cable

channel, and digital terrestrial set-top box. ABS, however, always has the first-mover advantage in launching new products.

Investment Summary

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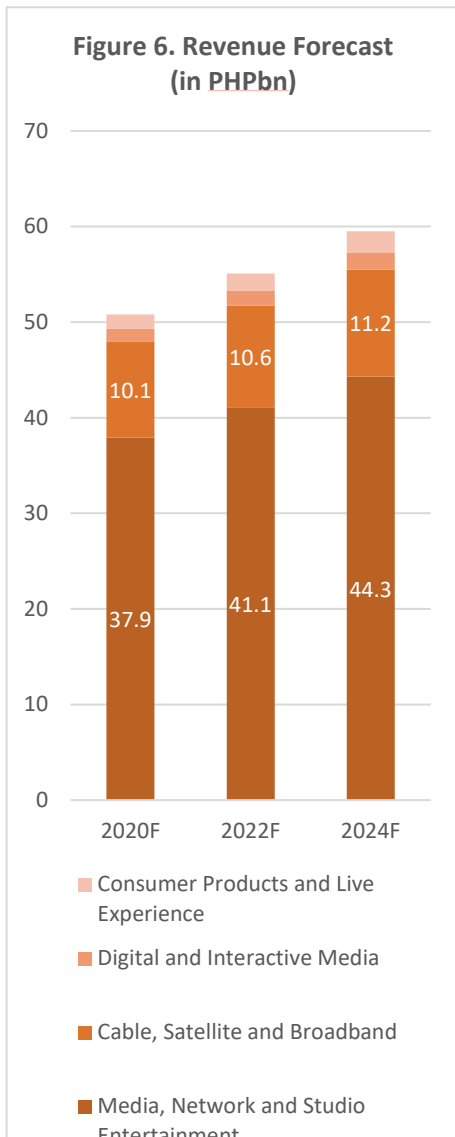
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Foray into Digital Spectrum

In addition to its strong position in the Philippine media industry, it is expanding its foothold in the digital media space. One of the biggest investments of the company is its launch of its own brand of Digital Terrestrial Television (DTT). Launched in 2015, it is continually growing its audience with its aggressive marketing activities. With this broadcasting medium, it is able to monetize proprietary content shown in pay-per-view channels such as Kapamilya Box Office.



Source: Team Estimate, Oxford Economics, Euromonitor

Valuation Assumptions	
Beta	0.70
Equity Risk Premium	8.60%
Risk Free Rate	4.52%
Cost of Equity	10.58%

Source: Team Computation, Risk Premiums NYU Stern, PDex

Also, part of its effort to go digital is increasing its visibility in the web. Through its online content publication, it is able to deepen its connection with its audience. It is able to monetize and market its content through its presence in Youtube and other online media portals such as iWant and TFC.tv.

Aggressive Expansion Across Industries and Geographies

ABS is diversifying its operations through its publication of content outside the country. It is investing in films aimed to be shown in the international stage. It is aiming to sell its content to Africa and Asia through OTT platforms. This segment is one of the fastest growing segments of the company, with 30% YoY growth in 2018. In the same year, it was also able to generate PHP500 million in gross receipts for its movies.

In addition to expansion across other regions, ABS is also beefing up its experience themed portfolio. Come of its most notable investments are: Kidzania Manila and Studio Experience. Experience-based companies turned PHP1.6 billion in revenues in 2018.

Risk Analysis

Possible Investment Risks

Key risks investors must be aware of include Regulatory Risk such as non-renewal of the franchise due to repeated complaints of President Duterte with regards to the network. In case the bill for the renewal is not signed before its expiration (March 20, 2020), ABS will have to shut down its operations in the Philippines. ABS also faces market risks which include unfavorable conditions resulting in lower demand in the Philippines and in abroad. Legal risk includes a pending civil case against Solar Entertainment Inc. and multiple cases that are currently under compromise agreements.

Individual Risk Analysis

Regulatory Risk | Non-renewal of Franchise (RR)

The House of Representatives and/or the Senate of the Philippines can block the franchise renewal of ABS if they will adhere to the wishes of President Duterte which is vocal in stopping the media giant. To mitigate this risk, ABS will need to consult and converse properly with the government and defend their position why should they be renewed. Also, ABS has been partnering with other media providers abroad in case they are stopped in the Philippines.

Based on our analysis, ABS has a high possibility of being renewed because of its strong ties with the Filipino community. Non-renewal of this franchise will result in public outcry since most of ABS' shows are topping the rankings in most television shows categories. ABS holds the highest market share among the television stations in the Philippines.

Market Risk | Decrease in Spending on Advertisements (MR1)

ABS is highly reliant on advertisers for its profits. The high percentage of the Company's operating expenses are fixed, that is why a small decrease in advertising revenue could have a significant impact on the Company's revenue. Even though traditionally increase in advertisement spending are during election season, there is still forecasted growth seen in free television consumers. Based on our analysis, since ABS holds the largest market share, it will be the network of choice for advertisements.

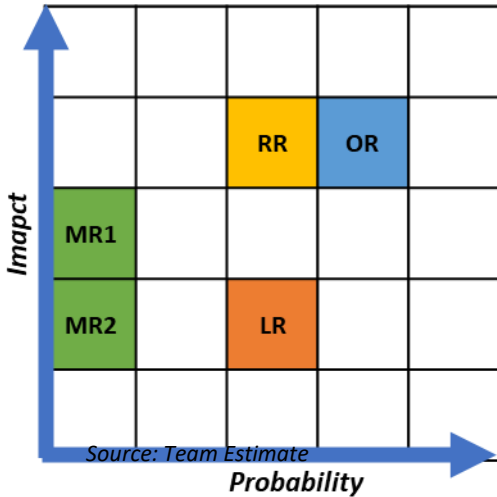
Market Risk | Decrease in Subscribers (MR2)

Aside from the free-to-air television, ABS also provides paid subscriptions as part of their business most notably, SKY Cable and iWant TV. A decrease in subscribers will negatively impact ABS-CBN's financial results and can adversely affect business operations. ABS is competing with other cable and

Risk Factors and Mitigation Strategies	
Risks	Mitigating Factors
Regulatory Risk	
Non-renewal of franchise	Better relationship with the government
Market Risk	
Decrease in spending on advertisements	Large market share
Decrease in subscribers	Original content offering
Legal Risk	
Unfavorable ruling in civil cases	Regular legal assessment activity
Operational Risk	
Downtime caused by fortuitous events	Insurance, recovery mechanism

Source: Team Estimate

digital media providers but has an edge by providing original content that are being enjoyed by Filipinos in the Philippines and abroad. We believe that as long as the Company offers content that is differentiated with another network, it will be likely that they retain or even increase their subscribers.



Legal Risk | Unfavorable Ruling in Civil Cases (LR)

As of December 31, 2018, ABS is involved in 10 civil cases. Despite the fact that in the last 5 years, the Company is not penalized for any claims that for damages in an amount, receiving unfavorable ruling will negatively affect the Company’s image. Nevertheless, the amount if in any case, the Company is required to pay for damages, it will not be substantial as to affect the Company’s financial position.

Operational Risk | Downtime Caused by Fortuitous Events (OR)

Natural calamities can hinder the ability of ABS in providing free television services resulting in major service interruptions. Significant damage in facilities can also result in an increase in unplanned repairs expenses. Albeit, these risks can be mitigated through insurance. Additionally, the Enterprise Risk Management Committee prepared recovery plans in case such events happen.

Annex 1 Income Statement

	2019F	2020F	2021F	2022F	2023F	2024F
Media, Network and Studio Entertainment	36,190	37,891	39,445	41,102	42,746	44,284
Cable, Satellite and Broadband	9,776	10,055	10,337	10,615	10,966	11,237
Digital and Interactive Media	1,151	1,289	1,426	1,562	1,699	1,831
Consumer Products and Live Experience	1,349	1,494	1,655	1,833	2,030	2,248
Eliminations	(4,382)	(5,042)	(5,254)	(5,478)	(5,709)	(5,924)
Total Revenue	44,085	45,687	47,608	49,633	51,731	53,676
Production Costs (Fixed)	(12,787)	(13,388)	(13,937)	(14,523)	(15,103)	(15,647)
Cost of Services (Fixed)	(10,812)	(11,221)	(11,608)	(12,007)	(12,446)	(12,824)
Cost of Sales (Variable)	(2,400)	(2,672)	(2,957)	(3,257)	(3,575)	(3,906)
Gross Profit	18,086	18,407	19,106	19,846	20,606	21,299
General and Administrative Expenses	(12,685)	(13,040)	(13,431)	(13,834)	(14,249)	(14,676)
Finance Costs	(1,285)	(1,285)	(1,285)	(1,285)	(1,285)	(1,285)
Interest Income	395	406	418	431	444	457
Foreign Exchange Gains (Losses)	-	-	-	-	-	-
Equity in Net Losses of Associates and Joing Ventures	-	-	-	-	-	-
Other Income	198	204	210	216	223	229
EBIT	4,710	4,692	5,018	5,374	5,738	6,024
Provision for (Benefit From) Income Tax	-	-	-	-	-	-
Current	-	-	-	-	-	-
Deferred	-	-	-	-	-	-
Income Tax Expense	1,413	1,408	1,505	1,612	1,722	1,807
Net Income	3,297	3,284	3,513	3,762	4,017	4,217
EPS	3.83	3.81	4.08	4.36	4.66	4.89

Annex 2 Balance Sheet

	2019F	2020F	2021F	2022F	2023F	2024F
Current Assets						
Cash and cash equivalents	21,836	25,101	28,487	32,129	36,032	40,122
Short-term investments	5,973	5,973	5,973	5,973	5,973	5,973
Trade and other receivables	10,006	10,369	10,805	11,265	11,741	12,183
Inventories	570	635	703	774	850	929
Program rights and other intangible assets	1,362	1,362	1,362	1,362	1,362	1,362
Other current assets	5,941	5,941	5,941	5,941	5,941	5,941
Total Current Assets	45,689	49,382	53,272	57,444	61,899	66,509
Non-Current Assets	-	-	-	-	-	-
Property and equipment	27,697	27,697	27,697	27,697	27,697	27,697
Goodwill, program rights	12,884	12,884	12,884	12,884	12,884	12,884
FVOCI	271	271	271	271	271	271
Investment Properties	200	200	200	200	200	200
Investments in Associates and JV	440	440	440	440	440	440
Deferred Tax Assets	3,117	3,117	3,117	3,117	3,117	3,117
Other non-current assets	1,764	1,764	1,764	1,764	1,764	1,764
Total Non-Current Assets	46,373	46,373	46,373	46,373	46,373	46,373
Total Assets	92,062	95,755	99,645	103,817	108,272	112,882
Current Liabilities						
Trade and other payables	13,895	14,579	15,232	15,919	16,634	17,304
Contract liabilities	792	792	792	792	792	792
Income tax payable	215	215	215	215	215	215
Obligations for program rights	185	185	185	185	185	185
Total Current Liabilities	15,087	15,772	16,425	17,112	17,826	18,496
Non-Current Liabilities						
Interest-bearing loans and borrowings	32,918	32,642	32,366	32,090	31,814	31,537
Obligations for program rights	473	473	473	473	473	473
Accrued pension obligation and other benefits	4,306	4,306	4,306	4,306	4,306	4,306
Deferred Tax Liability	138	138	138	138	138	138
Convertible note	229	229	229	229	229	229
Other Non-Current Liabilities	462	462	462	462	462	462
Total Non-Current Liabilities	38,527	38,251	37,975	37,699	37,423	37,146
Total Liabilities	53,614	54,023	54,400	54,811	55,249	55,642
Equity						
Common Stock	872	872	872	872	872	872
Preferred	200	200	200	200	200	200
Additional Paid In Capital	4,745	4,745	4,745	4,745	4,745	4,745
Retained Earnings (Loss)	33,196	36,480	39,993	43,755	47,772	51,988
Treasury Stock	- 1,639	-1,639	-1,639	-1,639	- 1,639	- 1,639
Comprehensive Inc. and Other	1,073	1,073	1,073	1,073	1,073	1,073
Total Equity	38,447	41,732	45,245	49,006	53,023	57,240
Total Liabilities and Equity	92,062	95,755	99,645	103,817	108,272	112,882

Annex 2 Discounted Cash Flow

	2019F	2020F	2021F	2022F	2023F	2024F
Cash Flows	1,215,270	3,265,083	3,385,727	3,641,391	3,903,738	4,089,612
Terminal Value						55,866,047
Total	1,215,270	3,265,083	3,385,727	3,641,391	3,903,738	59,955,658
Discounted Cash Flow						
	1,099,393	2,672,116	2,506,649	2,438,874	2,365,284	32,863,470
Enterprise value	27,418,119					
Net debt						
Equity value	27,418,119					
Per share equity value	31.8					