Management Discussion and Analysis Report

1. ECONOMIC REVIEW

2011-12 was a challenging year across the global economic and political spectrum: sluggish economic growth, fifth consecutive year of recession in Greece, political instability across the Middle East and North Africa, deepening European crisis and a fragile US recovery. The liquidity infusions by the European Central Bank (ECB) have considerably improved the global financial markets. Nevertheless, an acceptable solution to the euro-zone crisis is still not in sight. The emerging economies are also witnessing slowdown, largely due to the trickledown effect of the global slowdown, and domestic pressures. The World Bank has predicted a modest global GDP growth of 2.5 percent in 2012, increasing to 3 percent in 2013 and 3.3 percent in 2014

The global turbulence has predictably, impacted India's economic performance as well. The domestic economy witnessed 6.5 percent growth in FY 2011-12, the lowest in nine years. Tight monetary control measures, high inflation, increasing fuel cost, growing fiscal deficit, slow infrastructure investments, contracting exports and imports and weakening rupee further arrested growth.

However, the long-term economic prospects appear bright, compared to most countries of the world. The World Bank has marginally raised India's growth forecast for 2012-13 to 6.9 percent, from its January estimate of 6.8 percent.

(Source: World Bank)

2. GLOBAL MEDIA & ENTERTAINMENT INDUSTRY REVIEW

The Media & Entertainment industry comprises the creation, aggregation, and distribution of content, news and information, advertising, and entertainment through various media channels and platforms. The global M&E industry is highly fragmented, with North America dominating the market. Asia Pacific (APAC), Latin America, and the Middle East are anticipated to develop rapidly, with APAC expected to witness the highest growth during the next five years, i.e. 2012–2017. Internet-based entertainment is gaining importance quite rapidly. It is projected to grow in double digits, and account for 10 percent of overall global industry growth in the next six years. Concisely, the market holds significant opportunities and it is expected to reach approximately US$1,289 Billion in 2017 with a CAGR of 5 percent during 2012–2017.

(Source: Global Media and Entertainment Industry 2012–2017: Trend, Profit, and Forecast Analysis by Lucintel Research)

The growth of the industry is expected to be about 13 percent, to reach ₹ 823 Billion in 2012. Going forward, the sector is estimated to grow at a healthy CAGR of 14.9 percent to reach ₹ 1,457 Billion by 2016.

3. INDIAN MEDIA & ENTERTAINMENT INDUSTRY

The recent fiscal has been a vibrant year for the Indian Media & Entertainment (M&E) industry. The industry has progressed considerably leveraging the dynamic consumer preferences towards niche content, digital delivery platforms, evolving business models and changing regulations. The year witnessed robust growth in advertising in the first half, and rather muted in the second. The highly anticipated digital ecosystem showcased its impact in various segments. The film segment also witnessed new means of distribution via digitalisation with regards to Cable & Satellite (C&S) and music.

Backed by a strong consumption especially in Tier II and Tier III cities, continual regional media development and fast growing new media businesses, the Indian M&E industry grew to ₹ 728 Billion in 2011. The growth of the industry is expected to be about 13 percent, to reach ₹ 823 Billion in 2012. Going forward, the sector is estimated to grow at a healthy CAGR of 14.9 percent to reach ₹ 1,457 Billion by 2016.

Television remains the leading medium in the sector. Sectors such as animation, VFX, digital advertising and gaming are growing their share of the market rapidly. Advertising spends across all media witnessed 41 percent growth in 2011, compared to the previous fiscal. Advertising revenues registered a growth of 13 percent in 2011 against 17 percent observed in 2010.

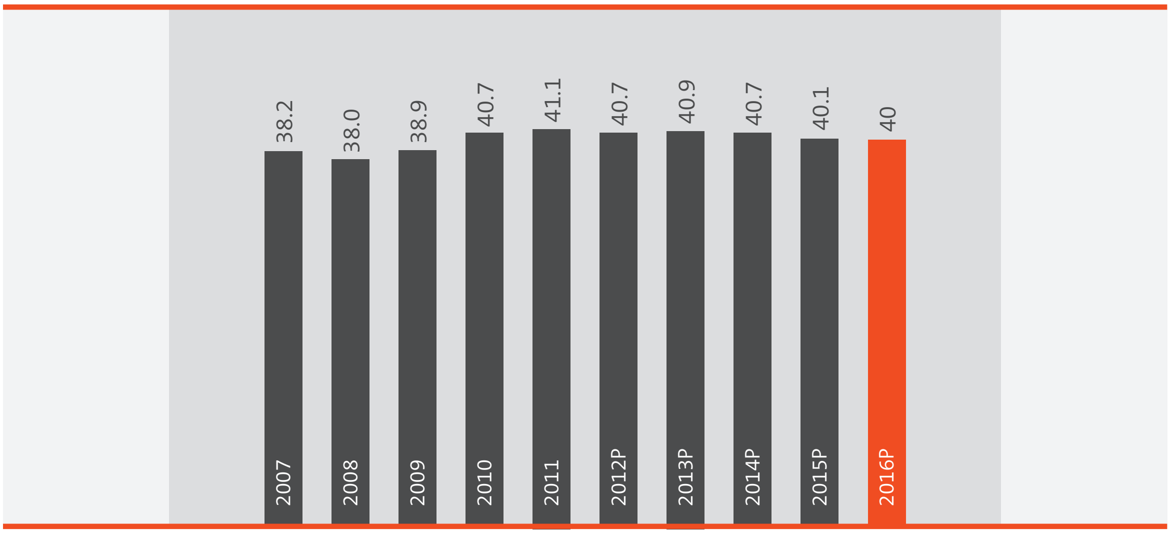
Overall Industry size (₹ Billion)

	2007	2008	2009	2010	2011	Growth in 2011 over 2010	2012P	2013P	2014P	2015P	2016P	CAGR (2011-16)
TV	211.0	241.0	257.0	297.0	329.0	10.8%	380.0	435.0	514.0	618.0	735.0	17.0%
Print	160.0	172.0	175.2	192.9	208.8	8.3%	226.0	246.8	270.0	294.9	323.4	9.0%
Film	92.7	104.4	89.3	83.3	92.9	11.5%	100.0	109.7	121.1	134.5	150.3	10.0%
Radio	7.4	8.4	8.3	10.0	11.5	15.0%	13.0	16.0	20.0	24.0	29.5	21.0%
Music	7.4	7.4	7.8	8.6	9.0	4.7%	10.0	11.3	13.1	15.4	18.2	15.0%
OOH	14.0	16.1	13.7	16.5	17.8	7.6%	19.5	21.5	23.6	26.0	29.0	10.0%
Animation and VFX	14.0	17.5	20.1	23.6	31.0	31.2%	36.3	43.0	51.1	61.0	69.0	17.0%
Gaming	4.0	7.0	8.0	10.0	13.0	30.0%	18.0	23.0	29.0	37.0	46.0	29.0%
Digital Advertising	4.0	6.0	8.0	10.0	15.4	54.0%	19.9	25.8	33.5	43.7	57.0	30.0%
TOTAL	**514.0**	**580.0**	**587.0**	**652.0**	**728.0**	**11.7%**	**823.0**	**932.0**	**1,076.0**	**1,254.0**	**1,457.0**	**14.9%**

* P - Projection

Source – FICCI-KPMG Indian Media and Entertainment Industry Report, 2012

Contribution of Advertising Revenues of Overall Industry Size (%)



* P - Projection

Source – FICCI-KPMG Indian Media and Entertainment Industry Report, 2012

3.1 Key industry trends

3.1.1 Proliferation of new age user devices

The proliferation of various entertainment platforms has made media consumption more personal than ever. Smart phones, tablets, PCs, and gaming devices are gradually influencing content creation and distribution. Multiple media including TV, films, news, radio, music etc are being impacted with this change.

3.1.2 New age consumers

With India's growing young population, there is a greater need for integration and innovation across traditional and new media platforms. The recent introduction of 3G and high bandwidth data networks have enabled consumers to subscribe to customised digital content. Digital formats have provided a platform to deliver content over mobile phones, tablets and other forms of portable computers and devices to meet the demand. The industry perceives changes in media consumption habits and increased inclinations for niche content, and has begun providing additional and greater touch points to engage with audience.

3.1.3 Emergence of regional markets

The regional entertainment industry has been on a sustained growth trajectory primarily on account of increased regional income and consumption. National advertisers are looking at leveraging these markets as prime mediums, and increase their footprint. Local advertisers are also focusing on the regional media realising the benefits of marketing their products. Film studios and funds have already showcased their interest by investing in regional cinema.

3.1.4 Continued dependency on advertising revenue

Advertising revenue is still the main stream of income for the Indian M&E industry as the ARPU for television and average ticket price for films continue to be low, owing to intense competition.

3.1.5 Growth of the Music industry

The Indian music industry achieved revenues of ₹ 9 Billion in 2011, registering 5 percent growth over 2010. The industry witnessed a 19 percent Y-o-Y decline in sales of physical music, which was compensated by significant jump of 24 percent Y-o-Y in digital music consumed. While 2010 was the year of structural shift from physical formats to digital ones, 2011 provided users viable options of music consumption through different digital platforms such as pay per download, unlimited music streaming and subscription based music services.

3.1.6 Regulatory shifts

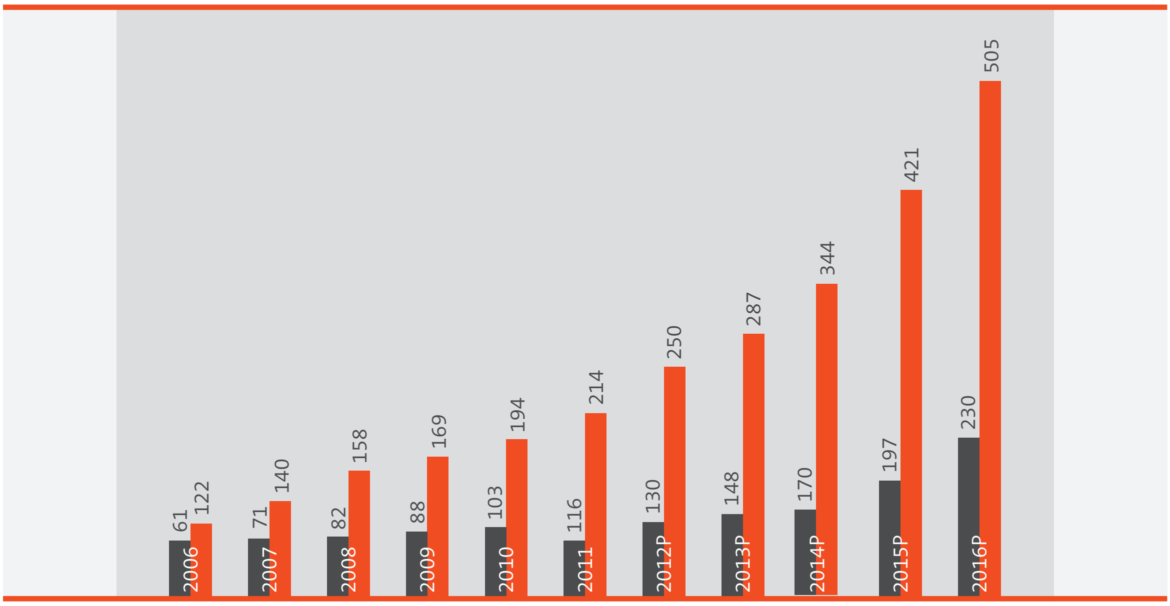
There have been significant changes in the regulatory front in the past few years. The implementation of the recently enacted regulation on digitisation for cable impacts the industry considerably. Implementation of Phase 3 and the roll out of 4G will further affect the industry.

3.2 Indian Television Industry

In terms of revenue, television remains the largest medium for media delivery, representing around 45 percent of the total industry turnover. India continues to be the third largest TV market after USA and China, with 146 Million television households. C&S penetration of television households currently stands at 80 percent of the total households, with DTH driving a significant part of the growth in the last 12 months. In the near horizon, digitisation of all analog cable subscribers will promote the penetration level of digital households. The over-all television industry size was estimated to be ₹ 329 Billion in 2011, and is expected to grow at a CAGR of 17 percent over 2011-16, reaching ₹ 735 Billion in 2016.

The share of subscription to the total industry revenue is expected to increase from 65 percent in 2011 to 69 percent in 2016. The total number of TV channels in India has gone up to 623 in 2011, and a number of channels are anticipating approvals for broadcast. The industry currently witnesses a robust demand for satellite bandwidth with the introduction of HD channels, DTH expansion and new channel launches. This leads to delivering customised content based on a consumer's spending capability in the near future.

TV industry size (₹ in Billion)



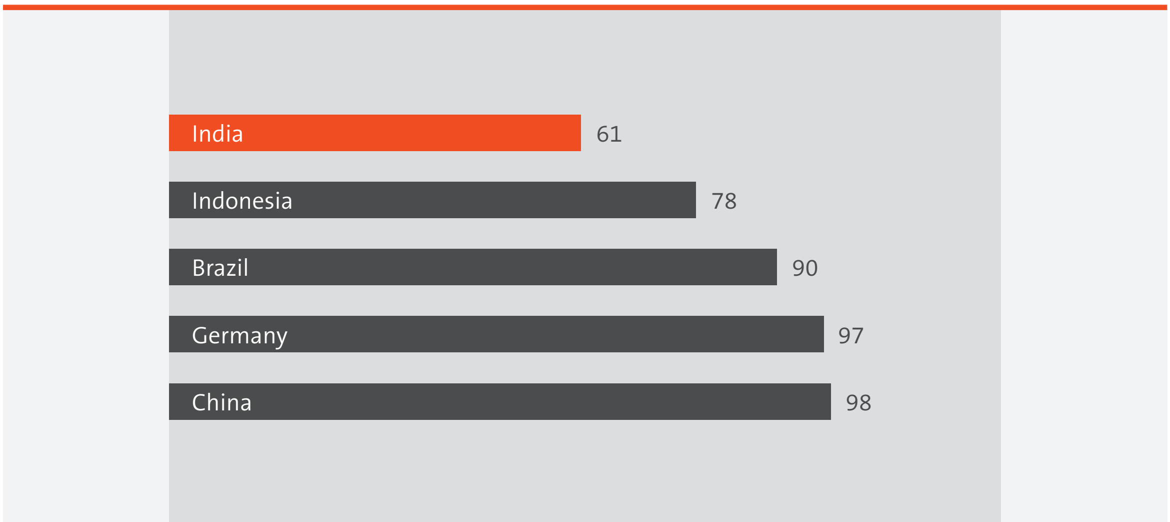
Source – FICCI-KPMG Indian Media and Entertainment Industry Report, 2012

3.2.1 Growth drivers

3.2.1.1 Low television penetration

Compared to other developing countries television penetration is still low in India. Indian TV households were estimated to be around 146 Million in 2011, indicating a TV penetration of approximately 60 percent. The statistics indicate huge growth opportunity. TV penetration in 2016 is estimated to rise by almost 70 percent.

TV penetration in select countries in 2011 (%)



Source – FICCI-KPMG Indian Media and Entertainment Industry Report, 2012

3.2.1.2 Increased television sales

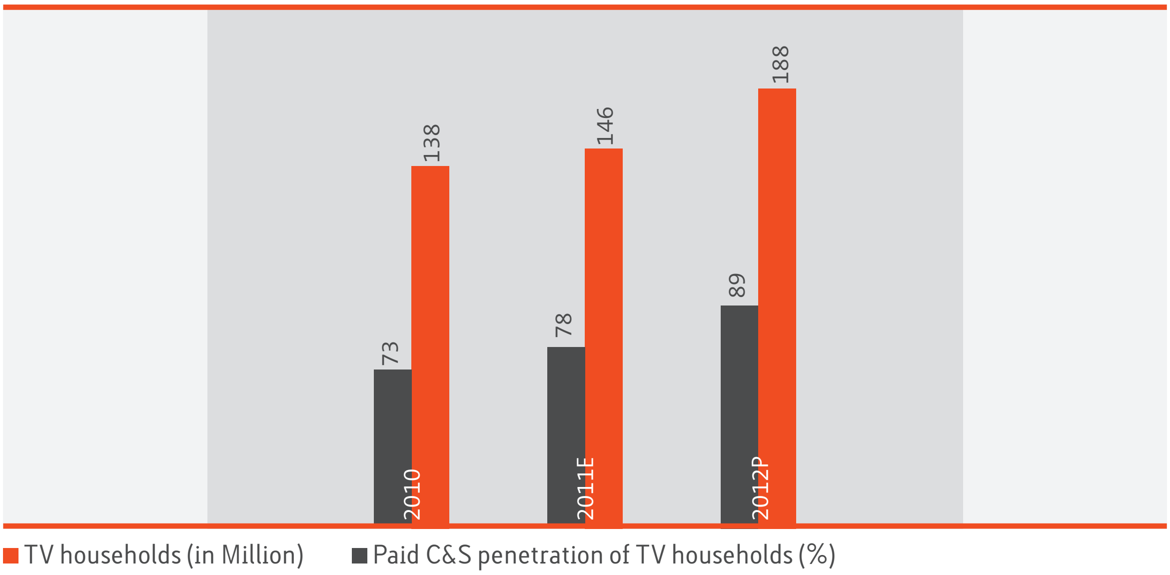
Sales of new TV sets have been on a rise in India. It was estimated to be approximately 17 Million in 2011. Since 2005, India has added 12-16 Million TV sets every year. Owing to rising Indian middle class, growing per capita income and newer television sets with superior technologies, the trend is expected to continue.

3.2.1.3 Increased C&S penetration

During 2011, the number of C&S households has grown by 11 Million to reach 119 Million in India. Of the total TV households, C&S penetration has increased to 81 percent in 2011 from 78 percent in 2010. In the coming years, demand for C&S is expected to be driven by consumer demand for content beyond free to air channels, combined with the relatively low ARPUs in India.

By 2016, the number of C&S households is estimated to reach approximately 176 Million of which paid C&S households is estimated to be 168 Million households, representing a 89 percent of total TV households.

Growth in number of C&S households



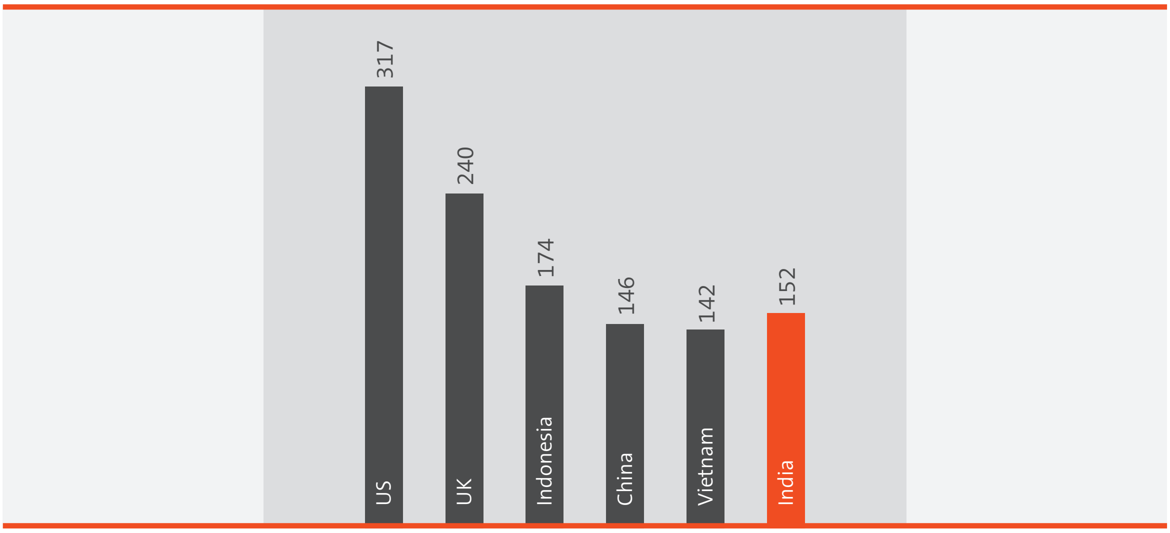
* P - Projection
* E - Estimate

Source – FICCI-KPMG Indian Media and Entertainment Industry Report, 2012

3.2.1.4 Increased TV viewing time

Compared to the developed nations average television viewing time continues to be low in India. Nevertheless, the average television viewing is expected to increase due to various innovations in the sector.

Average TV viewing time in 2011 (Minutes per day)



Source –FICCI-KPMG Indian Media and Entertainment Industry Report, 2012

3.2.1.5 Untapped market in advertising

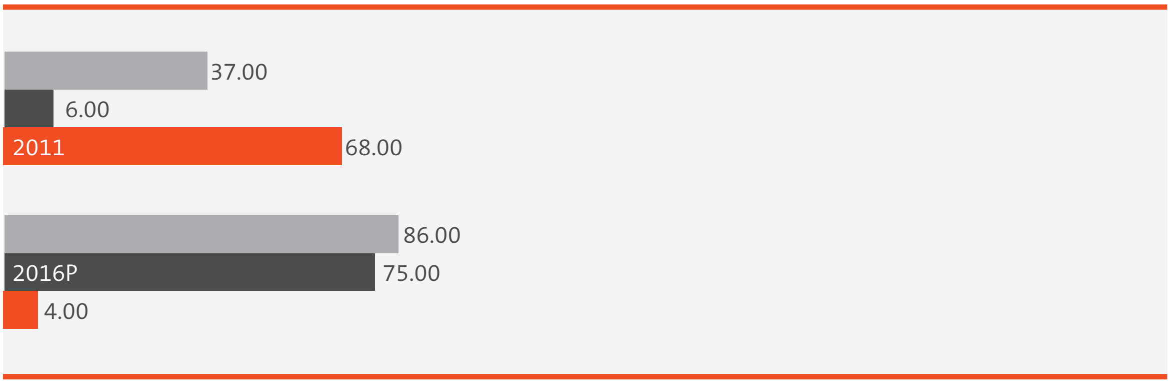
Currently in India, a large number of advertisers are still using only the print platform. However newer and more effective mediums are gaining prominence. As the industry depends primarily on advertisement revenues, emergence of newer platforms provides ample growth prospects.

3.2.1.6 Digitisation opportunities

The Indian cable television industry is transforming to the Digital Addressable System (DAS) for television distribution. Under DAS regime, cable operators would be legally bound to transmit only digital signals. Subscribed channels can be received at the customer's premises only through a set-top-box equipped with a conditional access card, and a Subscriber Management System (SMS). In a nut-shell, each user in the network would be uniquely identifiable to the service provider.

The consumer on account of digital television is expected to gain access to a higher number of TV channels along with customised tariffs, availability of broadband and other value-added-services leading to an enhanced user experience through better viewing quality and consumer service.

Number of digital households in India (in Million)



DTH Digital cable Analogue

Source –FICCI-KPMG Indian Media and Entertainment Industry Report, 2012

3.3 Indian Film Industry

The resurgence of Hindi movies with mass connect backed by improved content quality has benefitted occupancy rates in 2011, which in turn increased domestic box-office collections. The estimated market size of the Indian film industry stood at around ₹ 93 Billion in 2011, registering a growth of 11.5 percent as compared to 2010. Competitive bidding by broadcasters for large budget films resulted in 26 percent growth of Cable and Satellite rights. Ancillary revenues (such as licensing and merchandising, in-cinema advertising and pay per view) which are yet less significant with respect to size and scale, have also displayed strong growth in 2011. The Home video segment was the only exception to the growth trend with most filmmakers ceasing to consider this as a major line-item in their revenue estimations.

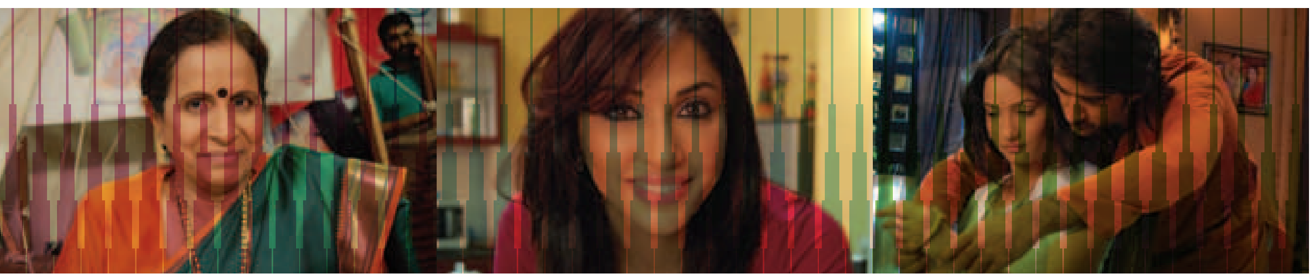
With several upcoming high budget Hindi releases, year 2012 is expected to sustain the growth momentum witnessed in 2011. The Indian film industry is projected to grow at a CAGR of 10.1 percent to touch ₹150 Billion in 2016. The dominance of domestic theatrical revenues in the film industry is expected to sustain. The market share of C&S rights and overseas theatricals revenues are also increasing as strong marketing initiatives for films in the International market may further accelerate the growth of theatrical revenues overseas.

Size of the Indian film industry (₹ Billion)

Film Industry	2007	2008	2009	2010	2011	CAGR (2007-11)	2012P	2013P	2014P	2015P	2016P	CAGR (2011-16)
Domestic Theatrical	71.5	80.2	68.5	62.0	68.8	-1.0%	73.5	80.2	88.0	97.2	108.0	9.4%
Overseas Theatrical	8.7	9.8	6.8	6.6	6.9	-5.5%	7.5	8.3	9.2	10.2	11.5	10.5%
Home Video	3.3	3.8	4.3	2.3	2.0	-12.0%	1.7	1.4	1.2	1.0	0.9	-15.0%
Cable & Satellite Rights	6.2	7.1	6.3	8.3	10.5	14.0%	12.0	13.7	15.6	17.8	20.3	14.2%
Ancillary Revenue Streams	2.9	3.5	3.5	4.1	4.7	12.3%	5.4	6.2	7.2	8.3	9.6	15.4%
TOTAL INDUSTRY SIZE	**92.7**	**104.4**	**89.3**	**83.3**	**92.9**	**0.1%**	**100.0**	**109.7**	**121.1**	**134.5**	**150.3**	**10.1%**

* P - Projection

Source – FICCI-KPMG Indian Media and Entertainment Industry Report, 2012

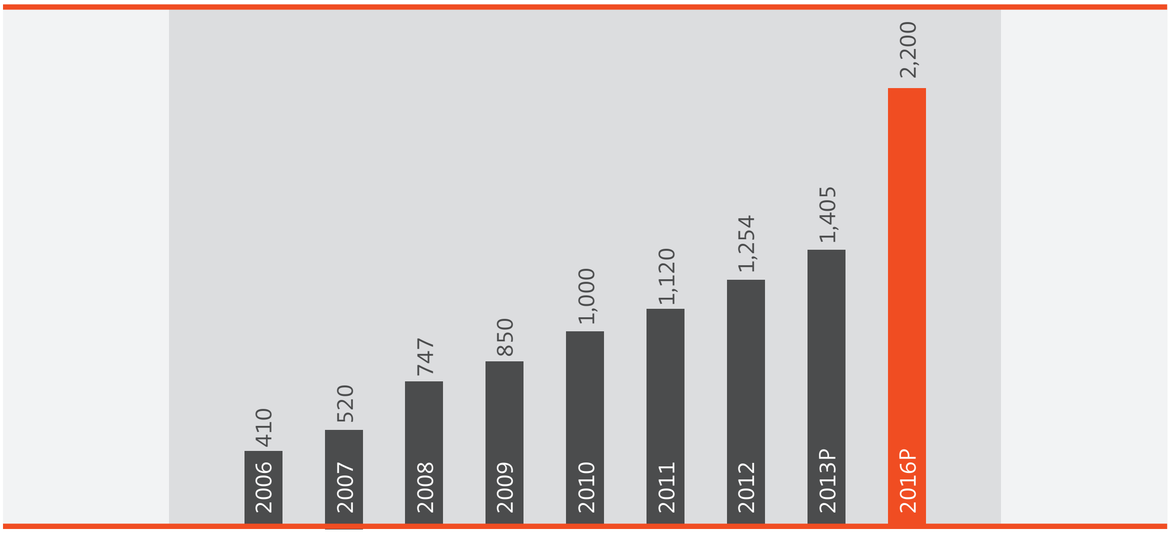


3.3.1 Distribution landscape

Larger film budgets supported by aggressive marketing campaigns and promotional tactics are gaining importance. With growing importance of local presence, there are larger opportunities for producers to unlock the complete potential of a given geography.

In 2011, commercial success ratio of films remains roughly 15 percent to 17 percent. While small budget films continue to struggle for screen space, the number of domestic and international screens for big budget films has more than doubled. Medium budget films have also observed steady growth with regards to domestic screens. The industry expects this number to increase further.

No. of Multiplexes in India



* P - Projection

3.3.2 Growth drivers

3.3.2.1 Growing multiplexes

The growth of multiplex chains continued through 2011. Despite representing less than 15 percent of the total screens in India, multiplex screens in 2011 accounted for a third of the total box office collections. Despite the overall surge in multiplexes across Tier I cities, urban centers are still away from saturation. Moreover, the growing number of multiplexes in Tier I and Tier II cities will further enhance growth. The industry is expected to double the multiplex screens over the next few years to over 2,200 screens in 2016 indicating a CAGR of 20.28 percent.

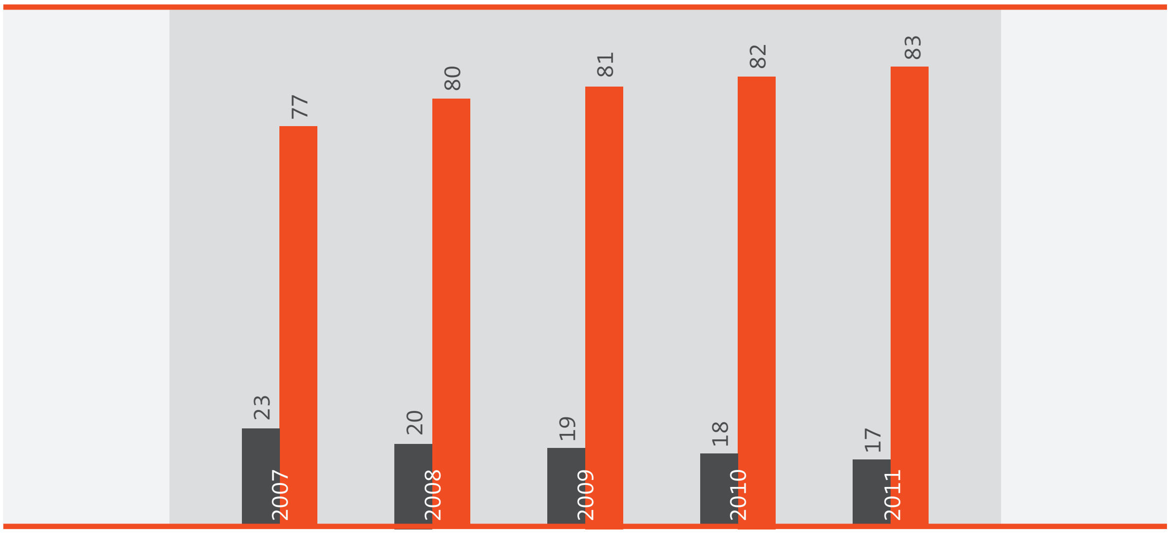
3.3.2.2 Upsurge in film advertising

In past few years, there is a marked improvement in transparency of ticket sales in India. This can be mainly attributed to the superior processes and systems introduced by multiplex chains and the digitisation of theaters and prints. These, in turn, have increased the adoption of cinema advertising in India. The cinema advertising market has grown at a robust 18 percent in 2011 to reach ₹ 140 Crores. Advertising revenue is expected to contribute to 30 percent of total digital cinema revenue this year as compared to 24 percent in the last financial year. Cinema advertising is projected to account approximately 40 percent of revenue for digital cinema providers in the coming years.

3.3.2.3 New opportunities in regional cinema

Regional film industry has come a long way since the past few years. Besides the incremental growth of South Indian cinema, the industry has witnessed growth in Marathi, Bengali and Punjabi cinema. Multiplexes have started experimenting with regional movies in the last few years. Regional movies are also exploring opportunities in the International market. Though the growth of regional films is not uniform across all the languages, there are encouraging signs of growth in the near future.

Certified films by language (%)



Source –FICCI-KPMG Indian Media and Entertainment Industry Report, 2012

3.4 Opportunities of Indian M&E Industry

3.4.1 The HD growth curve

Broadcasters and DTH players have expanded their HD offerings this year due to a rising demand for high end LCD and Plasma TV which are estimated to grow at a healthy CAGR of 22 percent over 2011 to 2015. With rising incomes and changing demography's consumers are looking for a better television viewing experience and are willing to pay a premium to subscribe to HD channels. It is estimated that approximately 7 to 8 percent of new DTH subscribers are opting for HD packages and the trend has gone beyond specific events like sports and movies for HD channels amongst consumers. There are approximately 30 channels available in HD today in GEC, Infotainment and lifestyle apart from movies and sports genres. Growing subscription for HD channels could lead to increase in ARPUs providing a subscription revenue boost to distributors and broadcasters.

3.4.2 Early monetisation

With increased piracy, reduced theatre to TV window and limited screen space at multiplexes, producers are focusing to monetise on a film as early as possible. It works for the distributors as well, since the increased total outlays lead to an urgent need to recover and rotate cash flows. Until a few years ago, 1000+ prints were considered adequate for large budget films. However, in the recent times, the number of domestic prints for large budget films has tripled to 3000+. Industry sources believe that this number will continue to rise, further enhancing the growth opportunities of the film industry.

3.4.3 Growing pre-release cost recovery

Subject to the genre and star-cast of the film, studios are able to recover anywhere between 40-80 percent of their production costs before the film is released. Rights for cable and satellite, music, home video and select merchandising are sold prior to release of the film in theatres. In select cases, even overseas rights are sold upfront. Reduced dependence on box office collections to recover the cost has mitigated the risk associated with the business for production houses and provides an upfront return much before the actual release date which is comforting for production houses.

3.4.4 Rising overseas contribution

While the US, UK and Middle East continue to account for the bulk of overseas revenues, studios continue to explore newer markets like South Korea, Western Europe, Taiwan and Africa for Hindi films which are witnessing rising Indian populations. The contribution of overseas revenue from the total films' revenue is expected to rise to 40 percent from its current levels of 10-15 percent. Growth will be driven by marketing campaign, increased penetration in existing areas apart from newer markets.

Broadcasters and DTH players have expanded their HD offerings this year due to a rising demand for high end LCD and Plasma TV which are estimated to grow at a healthy CAGR of 22 percent over 2011 to 2015.

3.5 Challenges of the Indian M&E industry

3.5. 1 Slowdown of advertising revenues

A slowdown in the global and domestic economy during 2011 has considerably impacted the television broadcasting industry leading to pressure on advertising rates. It resulted in a lower than expected advertising revenues, especially during the second half of the year. The total TV advertising market has increased around 12 percent in 2011, lower than 15 percent of the previous fiscal.

3.5.2 Cannibalisation

Cricket World Cup and IPL (to a lesser extent) almost blacked out a wide four month period from February to May in 2011. Events like these capture the consumers' attention and result in fewer weekends available for film releases. Consequently, only about 40 weekends were available for film releases in 2011 which led to 7-10 films aggressively struggling for screen space.

3.5.3 Unfavorable tax regime

India is a severely under-screened market (12 compared to 31, 81 and 131 in China, Europe and USA respectively). Attempts have been made to improve the situation, however the process is capital and time intensive. Further, the returns on investment cycles are affected by higher real estate prices and stagnant occupancy rates. Also the average ticket prices (ATP) are still beyond the purchasing power of common man coupled with tax multiplicity; increased service tax of 12.6 percent which further affects the scenario.

3.5.4 Lack of quality shooting infrastructure

Despite being a huge film-producing nation, there are only four major film cities in the country (Mumbai, Hyderabad, Noida and Chennai). It results in reduced option available for shooting. Each of the cities faces pressure due to a rapid growth in broadcast and advertising requirements. On a daily basis, there is a demand-supply gap of 10,059 studio floors in Mumbai alone which has the potential for absorbing additional floor space. However, high real estate price has made this option increasingly unviable.

4. COMPANY OVERVIEW

Incorporated in 1994 in Mumbai, Balaji Telefilms Limited is a leading media company of India, engaged in the production of content for the television industry, including television serials, commissioned programmes, and sponsored programmes in Hindi, Tamil, Telugu, Kannada, and Malayalam languages. The Company is also involved in the production and distribution of Hindi feature films.

4.1 Performance overview

- Income from operations stood at ₹ 12,936 Lacs in 2011
- Profit After Tax grown to ₹ 1,071 Lacs in 2011, as compared to the loss of ₹ 340 Lacs in previous fiscal
- The Subsidiary of the Company, Balaji Motion Pictures Limited witnessed a turnover of ₹ 5,845 Lacs, owing to the excellent performance of movies, such as *Ragini MMS, Shor in the City* and *The Dirty Picture.* The turnover registered 40 percent growth, compared to ₹ 4,170 Lacs in 2010.
- Profit After Tax of the subsidiary has increased by 281 percent, reaching ₹ 883 Lacs in 2011 from ₹ 232 Lacs in 2010

4.2 Key concerns

- Growing competition amongst channels – which demands speedy and unique performance
- Shortened show life
- Piracy
- Raising labour and talent cost
- Ambiguous Tax and Regulatory environment

Profit After Tax grown to ₹ 1,071 Lacs in 2011, as compared to the loss of ₹ 340 Lacs in previous fiscal

4.3 Risk management

Risk	Mitigation
Increased competition affecting the bargaining power of the Company with channels.	Over the years, Balaji has established itself as one of the leaders in Hindi GECs and enjoys strong brand recognition with considerable premium. The creative output of the Company ensures a larger show life and automates premium valuation.
Uncertainties in Government policies	The Company thoroughly keeps track of the changing regulations to comply with all the statutory requirements.
Dependence on single channel and specific region may affect the profitability of the Company.	Balaji has a diversified business portfolio including movies, mobile and internet market, apart from the television content. Moreover, it has a strong presence across 5 Hindi GECs and it is diversifying its presence in the regional markets.
Shift in the entertainment preference of the audience may have detrimental effect on the bottom-line.	The talent pool of the Company is creating original concept and contents for television and films to match with changing customer preferences.
Retention of the talent pool is one of the major concerns of the Company.	The brand name of Balaji has always managed to attract and retain superior talent from the industry.

4.4 Future outlook

Over the years, Balaji Telefilms has emerged as one of the key players in Indian M&E industry. To capitalise the future growth opportunities in television and film market, the Company is strategically positioning itself in the market. With increasing demand of creative and niche content in television and movies, there is higher focus on creating original and diverse show content to retain the leadership position. The Company already has a strong presence in Hindi GECs. Further, it is also expanding network on the regional GECs to leverage on the increasing opportunities in regional markets. After huge success of the movie segment in the previous fiscal, the Company continues developing and nurturing talent to generate superior script and film content. Moreover, it has also focused on increasing the distribution capabilities and marketing of the films. All inclusive, the Company is poised to retain its growth and it will further leverage the tremendous opportunities of the M & E industry.

4.5 Internal control system

The Company understands the necessity of a well-defined organisational structure ad strong internal growth. The organisational structure ensures maximum utilisation of resources and safeguards the same from misuse; whereas the Audit Committee ensures statutory and regulatory control and transparency of all financial disclosures. It also has an internal audit team and an independent commercial team, which monitor and enhance operational efficiencies of the Company. All the internal reports are reviewed by the audit Committee and the Board on regular intervals and whenever required, the policies are amended to ensure optimum effectiveness of the Company.

Cautionary statement

Statements in the Management Discussion and Analysis and the annual report describing the Company's objectives, projections, estimates, expectations may be "forward-looking statements" within the meaning of applicable securities laws and regulations in India and other countries. Actual results could defer materially from those expressed or implied. Important factors that could make a difference to the Company's operations include economic conditions affecting the domestic market, in which the Company operates, changes in the Government regulations, tax laws and other statutes and other incidental factors and unforeseen circumstances.

**Source of information: FICCI-KPMG Indian Media and Entertainment Industry Report, 2012*