Ten Network Holdings 15/05/2018 **FAT-AUS-873**

TEN Spec. **HIGH** **S**

Taken Off the Air

Note to Members: As of 24 November 2017, all shares in TEN were transferred to CBS International Television Australia for A$209.7 million in consideration following TEN's trading halt and subsequent administration.

As contrarian investors, we have picked our fair share of turnaround stories over the years, many of which have met with success. This has certainly not been the case with Ten Network Holdings, with the company continuing to be hampered in recent years by increasing programming costs amidst an unfavourable advertising environment due to the rise of Google and Facebook as well as online streaming. In the end this was too large a cross to bear financially.

Having gone through the financial wringer the company's largest supporters called it quits. This then led to an acquisition by a bigger network with the shares subsequently delisted. We accept that Ten Network has been a thoroughly disappointing recommendation, and we are now moving on from the stock and ceasing coverage.

A Forensic Autopsy: Tracing the steps

Initially, back in 2014 (FAT-AUS-676), we saw that the company, much like the rest of the media industry in Australia (and globally), faced structural headwinds from an increasingly fragmented advertising market, thanks to the rise of digital advertisers like Google and Facebook.

This was also worsened by the fact that advertiser bookings were increasingly short term oriented making it harder for networks to lock in better deals. This made it difficult for networks to deliver decent returns on capital and to reinvest profits for better shows and infrastructure.

<u>This wasn't a real issue for Ten Network since it has always punched above its weight with a low cost, high profit model</u> **and benefitted from having a larger share of the market (>20%)**. The company at the time also saw the nadir of the advertising cycle and just passed its low point in earnings, highlighting what at the time seemed **a compelling cyclical turnaround case**.

In light of that background, we also saw potential for the company as an acquisition target as at the time (in 2014), the media industry was back on the up and saw an increase in Merger & Acquisition (M&A) activity. There were also increasing talks in the grapevine of a major US network looking to explore 'options' which extended beyond programming deals. Britain's ITV was also said to have been in talks about a 'strategic investment'.

As such, these factors led to our High Risk Buy recommendation.

However, befitting its High Risk rating, the journey to the present was fractious to say the least. A worsening broader advertising market, with more and more advertising dollars running to digital, caused networks to seek quite expensive solutions to counter the digital threat and bring back ratings.

We understood fully that TV companies live or die on their ratings and we believed that Ten had what it took to turn things around. One of Ten Network's solutions was to get licenses for new shows from big US TV networks. There have been quite a few successes with "The Bachelor' and "I'm A Celebrity Get Me Out of Here!" however there were shows that flopped as well such as the heavily promoted "Biggest Loser".

The issues didn't end there as some output contracts with Fox and CBS for shows like "Homeland" and "Madam Secretary" didn't deliver the ratings needed to drag in advertisers and ended up as loss makers. The company's last publicly released financial report showcases the impact of these with significantly high Television Expenses exceeding Revenues brought in:

STATEMENT OF COMPREHENSIVE INCOME

Income statement for the half year ended 28 February 2017

Group Results ($m)	1H FY17	1H FY16	Fav / (Unf)
Television Revenue	341.4	334.2	2.1%
Television Expenses	(343.8)	(324.1)	(6.1%)
Television EBITDA	**(2.4)**	**10.1**	
Depreciation & Amortisation	(5.6)	(6.9)	18.0%
EBIT	**(8.1)**	**3.3**	
Net Interest Expense	(9.1)	(9.3)	1.9%
(LOSS)/PROFIT BEFORE TAX & SIGNIFICANT ITEMS	**(17.2)**	**(6.0)**	**(186.2%)**
Significant Items	(214.6)	23.3	-
(LOSS)/PROFIT BEFORE TAX	**(231.7)**	**17.3**	
Income Tax (Expense)/Benefit	(0.1)	(2.1)	93.2%
(LOSS)/PROFIT AFTER TAX	**(231.9)**	**15.2**	
Non-Controlling Interest	(0.3)	(1.8)	82.6%
NET (LOSS)/PROFIT AFTER TAX ATTRIBUTABLE TO MEMBERS	**(232.2)**	**13.4**	
Underlying Net (Loss) / Profit After Tax Attributable to Members	*(17.6)*	*(9.9)*	*(78.1%)*

Source: 24 April 2017 Company Presentation

However, there was a light at the end of the tunnel with prospects of a **Media Reform** being increasingly likely. Historically, old media regulations from the early 90s allowed media companies to own just **one form of media** (TV, newspapers, radio) in the same market which led to Rupert Murdoch taking control of over 70% of the newspaper market.

At the time, the likelihood of a Media Reform was becoming increasingly apparent as calls for a more level playing field in Australia were resounding. This, in our view, was a significant catalyst to support the inherent value in the stock.

The only clincher was for the company to buy enough time to realise its valuation. This would need enough financial backing, which at the time, the company did have that in the form of a $250 million guarantee from billionaire shareholders Lachlan Murdoch, Bruce Gordon and James Packer.

BALANCE SHEET

Balance sheet as at 28 February 2017

Group Balance Sheet ($m)	Feb-17	Aug-16	Feb-16
Cash and Cash Equivalents	15.3	14.8	15.8
Receivables	83.1	104.7	83.7
Program Rights and Inventories	187.0	156.8	230.5
Intangibles	132.0	346.5	481.7
Property, Plant and Equipment	42.6	42.2	39.7
Other Assets	14.1	15.7	25.0
Current Liabilities	(285.0)	(168.6)	(223.9)
Borrowings (Non-Current)	-	(90.2)	(51.5)
Other Non-Current Liabilities	(36.6)	(39.0)	(47.4)
TOTAL EQUITY	**152.6**	**382.8**	**553.6**

Source: 24 April 2017 Company Presentation

However, the $232.2 million net loss sustained by Ten in the 1H17 ultimately resulted in its financial backers pulling the plug. The company then had no choice but to move into voluntary administration in 14 June 2017 (FAT-AUS-827) and has since been suspended from official quotation.

The company provided commentary in a filing noting that “this decision follows correspondence received from Illyria and Birketu over the weekend which left the directors with no choice but to appoint administrators.”

Despite the end of its time as a listed entity, we didn’t believe it was the end of the road for the company considering its inherent value, even in the context of recent structural changes within the broader media landscape (i.e. the proliferation of online and digital media that has resulted in a marked fragmentation of media content and with it media advertising).

Another supporting factor was that, despite withdrawal of its guaranteed loan, the two key shareholders (i.e. Lachlan Murdoch [Illyria] and Bruce Gordon [Birketu], who collectively owned 22.7% percent of the shares at the time) announced their intention to aid in recapitalising and restructuring the business.

This was followed with a positive titbit in late August was an announcement by the Australian Competition and Consumer Commission would not oppose an acquisition by the large shareholders, Birketu and Illyria.

However, in 28 August 2017, Murdoch and Gordon’s rescue bid were ultimately rejected by creditors in a vote as CBS swooped in when it guaranteed funding of circa A$142.7 million to refinance the loans. This also included a A$30 million working capital facility.

This act led to a binding agreement to purchase Ten Network to bring it into the CBS fold and in 16 November 2017, CBS completed the acquisition of Ten Network for A$209.7 million. This was after the NSW Supreme Court gave the deal the green light.

Image Credit: John Shakespeare

For shareholders who have been left stranded, the outcome though has not been a happy one, with unsurprising opposition to the deal, and murmurings of a class action. The level of debt present underpinned the high risk nature of this recommendation, and ultimately the decision by the company backers to call time sealed Ten's fate.

Delisted - TEN NETWORK HOLDINGS LTD - TEN (ASX) - 1 Month CandleStick Chart - AUD

Summary

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Having gone through the financial wringer the company's largest supporters called it quits. This then led to an acquisition by a bigger network with the shares subsequently delisted. We accept that Ten Network has been a thoroughly disappointing recommendation, and we are now moving on from the stock. **We will no longer be covering TEN or its reincarnation under CBS going forward.**

Foster Wheeler, Anglo American, Archipelago Resources, Arian Silver Corp, Aviva, Avocet Mining, Bank of China, Barratt Developments, BMW, Berkeley Energy, BG Group, BOLSAS Y MERCADOS ESPANOLES,SOCIEDAD, Bovis Homes, BP, Braemar Shipping Group, British American Tobacco, BT Group, Cairn Energy, Centamin Egypt, China Life Insurance, China Mobile, China Overseas, China Taiping, China Vanke, Country Garden, Daejan Holdings, Development Securities, Dragon, Enquest, Esure, Euronext, FedEx, Fresnillo, Ibiden, Infosys, Glaxosmithkline, Glencore International, Goldbridges Global Resources, Google (Alphabet), Grainger, Gulf Keystone Petroleum, Highland Gold Mining, HSBC,ICICI Bank, Ironveld, iShares Physical Metals, J Sainsbury, JKX Oil & Gas, John Wood Group, Kazakhmys, Legal & General, Lloyds, Low and Bonar, Market Vectors Junior Gold Miners, Market Vectors Oil Services, Market Vectors Vietnam, Marstons, Medusa Mining, Mitchells & Butlers, Mitsubishi Tokyo Financial, Mitsubishi UFJ, National Grid, Nippon Telegraph and Telephone, Panasonic, Paragon Group of Companies, Petra Diamonds, Petrofac, Petropavlovsk, PICC Property & Casualty, PPHE Hotel Group, Randgold Resources, Rank Group, Reckitt Benckiser, Royal Dutch Shell, Solgold, Sony Corporation, Standard Chartered, STV Group, Sylvania Platinum, Tata Motors, Tencent, Tertiary Minerals, Teva Pharamaceutical, Toyota Motor, Tullow Oil, Unilever, Vedanta Resources, Vodafone, Walt Disney, Zillow.

Snapshot TEN

Ten Network Holdings

Ten Network Holdings Limited operates commercial television stations through five capital cities in Australia know as the Ten Network. The Company broadcasts and produces television shows, movies, news and sporting events. The Company also provides outdoor advertising services.

Market Capitalisation: