OPINION / COLUMNISTS

JARRED HOUSTON: Value during an almost perfect storm of challenges for MultiChoice

Look beyond and there may well be tremendous returns for long-term investors

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13 OCTOBER 2023 - 05:00

by JARRED HOUSTON

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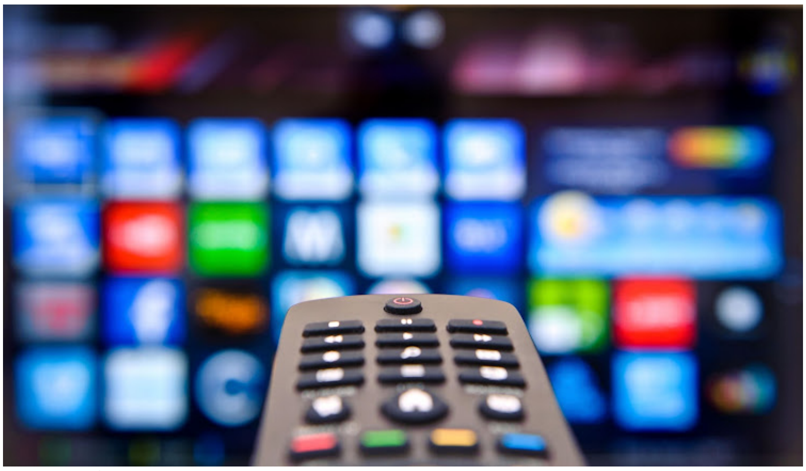
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When one thinks of companies heavily affected by the intensity of load-shedding in 2023, the picture one probably comes up with is that of Astral's forced culling of tens of thousands of chickens or even Pick n Pay spending millions a month on diesel to keep the fridges running. A name less obvious is MultiChoice and its DStv service.

Stage 4 and higher load-shedding became our fate from the early part of 2023 and we regularly had to negotiate the lack of power either from 6pm to 8pm or 8pm to 10pm. Immediate priorities for households were navigating the darkness and putting food on the table, without the use of our usual appliances. Watching television became something we were only able to do around the times of the blackouts.

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Unsurprisingly, 6pm to 8pm tends to be when families are together at home. These are key viewing hours and dominate prime-time programming viewership. Thus, with the inability to make use of your television during these times, the incentive to maintain your DStv subscription started to dwindle. In March MultiChoice put out a profit warning laying bare the harsh effect of a fall in revenue for a largely fixed-cost business. This prompted the share to fall as much as 19% on the day.

Since then, the share has fallen roughly 40% as concerns over load-shedding went on the back burner while others surpassed them: pressure on consumer disposal income due to higher inflation made a satellite TV subscription a luxury that many can no longer afford.

The prevailing weakness in the rand for a company that buys much of its content in dollars provides a real challenge. Then consider the 40% blowout in the currency of Nigeria, its biggest market outside SA. To that one can add a major impairment of the sports betting venture, KingMakers, soon after taking up a stake in the business.

When one further considers that in 2023 the company was coming out of the 2022 Fifa World Cup, a major subscription driver, the picture of a perfect storm forms.

At All Weather Capital, we try to assess a company's normalised earnings power through the cycle when we make a valuation. While it is our opinion that MultiChoice will face challenges for at least the next two years, we also believe the current levels of profitability do not capture the group's long-term growth and cash flow potential.

It's worth considering that this is a business that now has 23.5-million paying subscribers, a library of more than 70,000 hours of locally produced content, some of the best sports broadcasting rights and unparallelled distribution across Africa. The cost to replicate all of this would vastly exceed the company's market cap.

As households equip themselves with solar power, and interest rates potentially start to fall in 2024, we begin to see circling a much higher base in key currencies. This given, it's not hard to see an improvement in the beaten-up current shape of the firm.

Short-term cash flows and, by inference, dividends to shareholders, will no doubt be further hampered by investments in sports betting and a new, larger streaming venture with one of the world's leading players (Comcast's NBCUniversal and Sky).

While there is rightly scepticism over management's ability to execute in these areas, it is clear that these are attractive natural adjacencies to the core business. The investment case has shifted from one of near-term cash flow to that of recovery and long-term growth potential.

When it comes to the value inherent in the group we are further heartened by Canal+ — the pay-TV subsidiary of one of the world's biggest media conglomerates, Vivendi — buying MultiChoice shares.

Vivendi already owns more than 30% of the group and reportedly tried to acquire its Africa operations in 2017, but Naspers, MultiChoice's parent company at the time, rejected the $1bn offer.

A far larger company today, including its SA business and investments outside of terrestrial Pay-TV, MultiChoice now has a market cap of R33.1bn (about $1.75bn).

While any potential deal is likely to be complicated to navigate given the regulatory landscape, it is not hard to see the large synergies that could be extracted if a creative solution is reached between these two companies. Every cloud has a silver lining and if one can look through the current challenges, there may well be tremendous value to be had for long-term investors.

• Houston is an analyst at All Weather Capital

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