❖ The Global Contrarian ❖

May 26, 2010

Television Broadcasts Limited

(*BUY*)

Price (5/19/10): HKD36.00
52-Wk. Range: HKD28.00– HKD40.85
Shares Outstanding: 438.0 million
Market Cap.: HKD15.8 billion ($2.0 billion)[1]

Ticker[2]: 511 HK / TVBCY
Est. Div.: HKD1.60
Yield: 4.6%

[1]One Hong Kong Dollar (HKD) is equivalent to $0.1282, as of May 19, 2010.
[2]The common shares of Television Broadcasts Limited trade on the Hong Kong Stock Exchange. The ADR's trade over-the-counter in the US.

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Investment Summary

Television Broadcasts Limited (511 HK) is a Hong Kong-based television broadcaster of Cantonese-language programming and the leading broadcaster in that region. The company's programming is licensed in a number of international markets, primarily to serve the Chinese expatriate community, and it currently has a presence in the Guangdong province of Mainland China. Television Broadcasts Limited ("TVB") is the producer of the most popular Chinese-language-based programming in the region, so it would stand to reason that the company could experience significant growth were Mainland China to open its broadcast industry to outside entrants. It does not appear, however, that this growth potential is reflected in TVB's share price. As such, we recommend shares of TVB for purchase based on the fundamentals of its existing business, and we note that TVB shareholders will receive a free option on the company's potential entry into Mainland China, which could be an incredibly valuable opportunity.

TVB was not spared the impact of the broader economic downturn, as revenues and net income declined 10% and 15%, respectively, in 2009. The company has also been experiencing a higher-than-average level of capital expenditures related to the recent acquisition of property for headquarters in Taiwan, the build-out of HDTV production capabilities, and the switch to digital terrestrial technology; however, these expenditures appear to be subsiding. Despite these factors, TVB currently trades at a 6% free cash flow yield based on 2009 results – arguably an attractive yield for a company of TVB's market position, relative stability, and growth prospects. If one looks at the company's historical earnings potential, however, and adjusts the market capitalization for the company's HKD1.8 billion in net cash, this free cash flow yield approaches 9%.

There is abundant reason to believe that TVB will be successful in Mainland China, should it be allowed to enter that market. For example, the company's website, which is one of the most popular in Hong Kong, receives more than half of its visitors from the Mainland. Further, TVB has the highest-rated shows in the one Mainland province in which it is currently allowed to broadcast. With this level of demonstrated popularity within what is, potentially, the largest television and advertising market in the world and one that is as yet underpenetrated, it is hard to believe that TVB is trading at only one multiple turn higher (on a forward EV/EBITDA basis) than the significantly more mature CBS Corp. (NYSE: CBS). Although there are obstacles to entering the Mainland – entry currently requires government approval and partnership with a local network operator – the company is working toward this goal.

It is difficult to say, at such an early stage, just how profitable the Mainland China market could be. However, one of TVB's competitors, Phoenix Satellite (2008 HK), serves as a useful guidepost for the near-term opportunity. Phoenix Satellite derives over 90% of its HKD1.5 billion in revenues from the Mainland, and consensus estimates forecast 27% EBITDA growth in 2011. If one believes TVB could achieve a similar market position – a reasonable assumption, given the popularity of its programming – the company could see EBITDA expand by 30% in the near term, with significant growth prospects going forward.

Company Description

Television Broadcasts Limited ("TVB") is a Hong Kong-based television broadcaster of Cantonese-language programming. Although the company's primary market is Hong Kong, where it is the larger of the region's two broadcasters, TVB also distributes its programming through licensing and satellite subscription agreements to international markets, including Taiwan, the US, Canada, Australia, Europe, Malaysia, Singapore, and Mainland China. Established in 1965 by Sir Run Run Shaw, a centenarian who is considered to be one of Hong Kong's patriarchs, TVB has produced over 80,000 hours of content, which represents one of the largest Cantonese-language media libraries in the world. TVB has been listed on the Hong Kong Stock Exchange since November 1988, with Sir Run Run Shaw owning 32% of the outstanding shares.

TVB generates approximately 60% of its revenue from Hong Kong, with its next largest markets being Taiwan (16% of revenue) and Malaysia/Singapore (10% of revenue) (see Exhibit 1). Total revenues in 2009 declined nearly 10% relative to 2008, as the company's larger Hong Kong and Taiwan markets experienced significant weakness due to the broader economic environment, although this was offset slightly by growth in some of TVB's developing markets, primarily Mainland China and Australia.

Exhibit 1 TVB: 2007-2009 Revenue Breakdown by Geography
(HKD in thousands)

	2007	2008	2009	Growth 2008-2009
Hong Kong	2,689,295	2,660,971	2,366,476	-11.1%
as % of total	*62.2%*	*60.4%*	*59.4%*	
Taiwan	654,339	734,588	627,504	-14.6%
as % of total	*15.1%*	*16.7%*	*15.8%*	
US/Canada	212,721	216,094	217,727	0.8%
as % of total	*4.9%*	*4.9%*	*5.5%*	
Australia	88,442	95,722	98,284	2.7%
as % of total	*2.0%*	*2.2%*	*2.5%*	
Europe	100,694	91,519	82,614	-9.7%
as % of total	*2.3%*	*2.1%*	*2.1%*	
Mainland China	183,786	177,490	183,284	3.3%
as % of total	*4.2%*	*4.0%*	*4.6%*	
Malaysia/Singapore	365,772	399,686	378,668	-5.3%
as % of total	*8.5%*	*9.1%*	*9.5%*	
Other countries	30,760	31,234	28,775	-7.9%
as % of total	*0.7%*	*0.7%*	*0.7%*	
	4,325,809	4,407,304	3,983,332	-9.6%

Source: Company reports.

Revenues derived in Hong Kong (inclusive of revenue from the subscriber business, internet operations, and magazine publishing) have grown relatively slowly at 1% per annum over the last decade, illustrating the relative stability and maturity of that market. TVB's international operations, however, have grown at 4% per annum and now comprise approximately 41% of revenues, up from nearly 34% in 1999, implying that significant growth going forward will likely be derived from TVB's international businesses (see Exhibit 2).

Exhibit 2 TVB: 1999-2009 Revenue Growth by Geography
(HKD in thousands)

	1999	2009	99-09 CAGR
Hong Kong Revenue	2,156,684	2,366,476	0.9%
as % of total	*66.3%*	*59.4%*	
Non- Hong Kong Revenue	1,095,700	1,616,856	4.0%
as % of total	*33.7%*	*40.6%*	
Total	3,252,384	3,983,332	

Source: Company reports.

Hong Kong Television Industry

TVB's programming competes for audiences in Hong Kong with one free-to-air broadcaster, Asia Television Ltd. ("ATV"), and several subscription television companies, which mostly air internationally sourced programs as well as some locally produced shows. While ATV competed with TVB as a duopoly for many decades, the television industry in Hong Kong was opened to competition in 2000 when the government granted subscription television licenses to four domestic companies. Currently, three of these companies provide subscription television services: Hong Kong Cable Television Limited, which is operated by i-CABLE Communications (1097 HK); now TV, which is owned by PCCW (8 HK); and TVB Pay Vision Limited, an associate of TVB, in which TVB owns a 60% economic interest. In aggregate, these three licensees provide Hong Kong with access to over 300 subscription channels, which air mostly internationally acquired content. However, both of TVB's competitors have increasingly invested in the production of local content in an effort to capture market share.

Despite the inflow of domestic and foreign competition since 2000, however, the popularity of TVB's programming has proven resilient. For example, many of the network's top shows routinely earn audience shares of over 70%. Further, throughout 2009, TVB often held all of the top twenty ratings slots in Hong Kong.

This dominance is partly explained by its decades-long history as the region's premier network. Because the broadcasting industry had operated as a duopoly (with TVB the significant market leader), much of the Hong Kong population's access to significant cultural and noteworthy events, from the 1969 moon landing to the yearly airing of the Miss Hong Kong pageant to the Olympics, has been provided by TVB. Moreover, as a producer of television content, TVB is one of Hong Kong's most influential drivers of popular culture.

Hong Kong's role as a regional broadcast hub also gives individuals limited access to foreign-owned channels, which are broadcast via satellite. Hong Kong has a formidable satellite telecommunication and television broadcasting infrastructure that allows multinational companies to uplink their signals to customers all over Asia (currently, satellite television companies operating from Hong Kong serve over 300 million viewers in Asia Pacific). As a result, residents of Hong Kong are able to view a number of these channels for free, and can subscribe to several others. These satellite television companies, however, offer only a fraction of their programming for local viewing, and only 40% of Hong Kong households have access to the rooftop satellite antennas required to receive these services. By comparison, the penetration rate of the two broadcasters is over 98%, and it is over 90% for the domestic subscription businesses.

Increased Competition within Hong Kong

TVB will likely experience increased competitive pressure in Hong Kong going forward, both as a result of the continued development of local programming from subscriber networks and from the potential entry of other free-to-air (FTA) broadcasters. In January 2010, three separate FTA license applications were submitted to Hong Kong regulators in an attempt to enter the free broadcasting market. Two of the three applications were submitted by TVB's competitors in the subscription business, i-CABLE Communications and PCCW, while the other application was submitted by City Telecom Limited (1137 HK), a telecommunications service provider. It is currently unclear whether the government is open to granting these licenses, as none have been granted since 1975. TVB management recently stated that it believed new competitors would not present meaningful challenges given the company's strength in content production.

Of course, it would not be prudent to so readily dismiss the threat of direct competition in the FTA market. There are, however, examples of new competitive entrants in other markets that lend support to the company's claims. For example, TVB's dominant position in the Hong Kong market has characteristics similar to those of the Mexican broadcasting conglomerate, Grupo Televisa (TLEVICPO: MM), in that each is the dominant broadcaster in its own country, and both consistently air the most desirable content and carry the most popular celebrity talent. Grupo Televisa ("Televisa") has been the long-time ratings leader in Mexico, where its networks and local affiliates accounted for a national prime-time audience share of 70% during 2009.

Prior to 1993, Televisa's only competitor was a poorly operated government business with limited production and transmission capabilities. This business was privatized in 1993 and later listed on the Mexican Stock Exchange as TV Azteca (TVAZTCPO: MM), and it has operated as Televisa's main competitor ever since. Additionally, beginning in 1996 (five years prior to Hong Kong's first subscription license), satellite television was introduced in Mexico, providing subscribers with content from international sources, including shows from the US, whose television celebrities are well known in Mexico owing to geographic proximity.

Despite increasing programming options for Mexicans over the last fifteen years, however, Televisas's audience share rating has not been affected in any significant manner. Since 2002, it has maintained a stable prime-time audience share within the 69%-72% range, while increasing television broadcasting revenue at a reasonable compounded annual growth rate (CAGR) of 5% (see Exhibit 3). During the same period, the revenues of its pay television networks and cable segments achieved a CAGR of 22% and 34%, respectively, while Sky, the country's dominant satellite television provider (in which Televisa owns a majority stake), has seen revenues almost triple since 2004. Televisa's non-broadcasting businesses have, in fact, provided Mexican audiences with alternative programming options but have not been detrimental, in terms of ratings or revenues, to the core broadcasting business.

Exhibit 3 Televisa and TV Azteca: Historical Revenue Growth and Audience Share
(Mexican pesos in millions)

		2002-2004			2007-2009			2002-2009
	Line of Business	2002	2003	2004	2007	2008	2009	CAGR
Televisa Revenue by Business Segment								
Television Broadcasting	Nationwide broadcasting	15,354.2	16,185.7	17,102.0	21,213.2	21,460.7	21,561.6	5.0%
Pay Television Networks	Programming for third-party cable TV	665.0	736.0	800.8	1,852.0	2,212.5	2,736.6	22.4%
Sky	Satellite pay TV broadcasting	N/A	N/A	3,636.9	8,402.2	9,162.2	10,005.2	N/A
Cable and Telecom	Cable TV / Data for telecom providers	1,212.1	1,037.7	1,127.9	2,611.6	6,623.4	9,241.8	33.7%
Average Prime Time Audience Share		72.4%	70.1%	68.9%	69.0%	71.2%	69.8%	
TV Azteca Revenue								
Consolidated		7,560.0	7,914.0	8,597.0	9,503.0	9,815.2	9,967.9	4.0%
Average Weekday Prime Time Audience Share		26.3%	26.2%	27.9%	27.2%	23.0%	N/A	

NOTE: Ratings for Televisa include Saturday and Sunday viewership, whereas ratings for TV Azteca do not.

Source: Company reports.

By comparison, TV Azteca achieved only a 4% CAGR in consolidated revenues during the period 2002-2009 and has been unable to increase its audience share. While this may be explained by Televisa's expansion into satellite and cable services, which may have helped defend its total audience share, it could also be argued that Televisa's dominant industry position, and the access to the most popular events and celebrity talent that this affords, has created a significant barrier to meaningful expansion for TV Azteca.

If TVB were to continue developing its programming while leveraging its resources as one of the region's three domestic subscription television providers, it is possible that the company could achieve a stable audience share and broadcasting revenue base in the face of increased competition, similar to the Televisa experience. Indeed, TVB has already demonstrated this resilience, with low but stable revenue growth and increased ratings despite the entry of subscription television providers in 2000. As shown in Exhibit 4, broadcasting revenue is flat since 1999, while prime-time ratings have improved slightly, although the 1.3% CAGR for revenues during the period 1999-2008, which excludes the recessionary environment of 2009, may be more representative of recent growth.

Exhibit 4 TVB: 1999, 2008, and 2009 Broadcasting Revenue and Audience Share
(HKD in thousands)

	1999	2008	2009	99-08 CAGR	99-09 CAGR
Hong Kong Terrestrial TV Broadcasting	2,089,875	2,339,179	2,063,358	1.3%	-0.1%
Average Prime Time Audience Share					
Jade (Cantonese)	71%	85%	86%		
Pearl (English)	76%	75%	75%		

Source: Company reports.

International Operations

TVB's international operations comprise satellite television subscriber services in the US, Canada, Europe, and Australia; program and channel licensing and distribution to cable or satellite operators, primarily in the Guangdong region of China, as well as in Malaysia, Singapore, and Taiwan; the operations of three cable networks in Taiwan, and several Mandarin-language channels in Mainland China, Malaysia, and Singapore.

The most lucrative of the international businesses is the licensing and distribution of TVB's programming in Malaysia, Singapore, Taiwan, and Mainland China. In 2009, this segment achieved profit margins of 72%, despite unfavorable currency exchange rates in Malaysia and Singapore, and contributed 31% of consolidated operating profits while representing only 14% of total revenues (see Exhibit 5). As a result of the high margins associated with this segment, even a small increase in licensing revenue could greatly increase TVB's profitability.

Exhibit 5 TVB: Revenue and Operating Profit Breakdown by Segment
(HKD in thousands)

	2008			2009		
	Rev.	Op. Profit	Margin	Rev.	Op. Profit	Margin
HK terrestrial TV broadcast	2,339,179	639,630	27%	2,063,358	564,718	27%
Program license and dist.	585,001	373,762	64%	547,013	394,444	72%
Overseas satellite pay TV	345,315	61,693	18%	347,436	75,165	22%
Taiwan operations	715,996	164,909	23%	622,998	153,830	25%
Channel operations	329,116	88,947	27%	314,340	94,494	30%
Other	92,697	20,064	22%	88,187	3,702	4%
	4,407,304	1,349,005	31%	3,983,332	1,286,353	32%

Source: Company reports.

The Chinese expatriate community will likely be a continued source of growth for TVB's satellite subscription operations, as we estimate that 23 million individuals outside of Hong Kong have access to TVB's programming (TVB's estimate of 30 million individuals appears to include Hong Kong's population of 7 million) relative to a total overseas Chinese population that is believed to be over 40 million. To the extent that the expatriate community continues to drive demand for Chinese-language programming abroad, TVB's overseas satellite pay television segment, which serves the US, Canada, Europe, and Australia, should experience growth that outpaces growth in its core market. Indeed, before the recession affected 2009 results, this segment achieved a revenue CAGR of almost 19% during the period 2006-2008, while posting a robust CAGR of over 12% when including 2009 (see Exhibit 6).

Exhibit 6 TVB: Historical Rev. and Op. Profit of Overseas Satellite Pay TV Segment
(HKD in thousands)

	2006	2007	2008	2009	06-08 CAGR	06-09 CAGR
Revenue	245,113	280,752	345,315	347,436	18.7%	12.3%
Op. Profit	28,187	59,186	61,693	75,165		
Op. Profit Margin	*11.5%*	*21.1%*	*17.9%*	*21.6%*		

Source: Company reports.

The Opportunity to Enter Mainland China

The most lucrative business opportunity for TVB is a potential expansion into Mainland China, which would provide access to over 1.3 billion Chinese speakers. Although TVB already has a presence on the mainland, its operations are essentially limited to the province of Guangdong, which has a population of approximately 95 million and is situated next to Hong Kong. These operations are conducted under a special arrangement whereby Hong Kong media companies are permitted to distribute a portion of their content to the region under strict regulations. Currently, revenues from this business account for just over 3% of consolidated revenues (shown previously in Exhibit 1).

China has not committed to fully opening its media industry to foreigners, however, and future entry into Mainland China likely hinges on the Chinese government's willingness to do so, and its subsequent approval of the media companies that will be allowed to broadcast within the country. This expectation is similar to what is currently seen in Guangdong, where Hong Kong television companies are required to partner with a local network operator and receive approval from the local government in order to operate in that province.

In order to gain favor with the Chinese government, therefore, Hong Kong media companies, including TVB, have made compromises related to their content, such as self-censorship and coverage of the news that might be considered "pro-government." Further, TVB has entered into several co-production agreements to create dramas in conjunction with Mainland television stations, another effort that could gain TVB favor with the local government.

Should TVB gain access to Mainland China, there is already sufficient reason to believe that its programming will be well received. For example, TVB's website, which has become one of the most popular websites in Hong Kong, receives more than half of its visitors from Mainland China. Further, TVB estimates that it holds the leading audience share out of all the imported programming aired in Guangdong, while other programs, licensed through TVB International for limited rebroadcast throughout Mainland China, have also earned top ratings.

The breadth of the potential market opportunity represented by Mainland China is quite substantial. For example, during 2009, one of the most popular shows in the Mainland was a show called *Happy Girls*, a talent show similar to *American Idol* in the US. In one season, *Happy Girls* received 800 million text message votes from audiences across China, while the 2009 season of *American Idol* received 178 million text message votes in the US. That figure is economically significant, as it is arguably evidence of the fact that there exists an enormous and relatively untapped advertising market in China, which could ultimately become the largest advertising market in the world. Currently, the largest television advertising market is the US and Canada, because those two countries form one very sizeable Anglophone block of 330 million people. By comparison, the Chinese-speaking block in the Mainland is almost four times the size of the US and Canada block, implying that any show that is genuinely popular and available for nationwide distribution in China will likely have an audience several times larger than that enjoyed by the highest-rated shows in the US.

There are very few companies for which there is even a slight possibility of exploiting that situation, because of significant government intervention in the broadcasting market. However, TVB appears to represent one of the government's top contenders to become a foreign media provider, as it could generate immediate public interest, while, at the same time, avoiding dilution of Chinese culture, which Beijing officials fear could occur with an influx of Western media. If TVB is successful in winning support from the government while continuing to deliver popular content, then entry into China could become a very profitable endeavor going forward.

Valuation Analysis

Investors may be surprised to learn that a company with the potential to capitalize on the relatively untapped market within Mainland China is trading at only a slight premium to a significantly more mature peer in the US. Further, one could argue that an investment in TVB is warranted based solely on the merits of its existing business. In this light, TVB's current share price does not appear to reflect any premium associated with the potential growth to be derived from large-scale entry into Mainland China.

The investment worthiness of TVB's existing business is illustrated by its free cash flow generation, especially when one examines its earnings potential in a healthier economy. As shown in Exhibit 7, the company generated a 6% free cash flow yield in 2009, a year that saw significant weakness related to the global economic slowdown. If one considers 2007 to be a year more representative of TVB's earnings potential, TVB is trading at a 7.6% yield based on this free cash flow potential (note that in 2008, expenses increased significantly related to its coverage of the Olympics, and capital expenditures increased dramatically, primarily related to the acquisition of a property for a headquarters in Taiwan).

Exhibit 7 TVB: Free Cash Flow Valuation
(HKD in thousands)

	2005	2006	2007	2008	2009
Cash from Operations	1,292,838	1,369,204	1,403,363	1,330,407	1,192,957
Less: Minority Interest	(7,228)	157	(1,537)	(939)	(312)
Less: Capital Expenditures	(113,092)	(95,439)	(196,961)	(943,168)	(249,304)
Free Cash Flow	**1,172,518**	**1,273,922**	**1,204,865**	**386,300**	**943,341**

Share Price (5/19/10)	36.00
FD Shares Out. ('000s)	438,000
Market Capitalization	15,768,000
2009 Free Cash Flow	943,341
Free Cash Flow Yield	*6.0%*
2007 Free Cash Flow	1,204,865
Free Cash Flow Yield	*7.6%*

Source: Company reports, *The Spin-Off Report* estimates.

Both of these yields are calculated before taking into consideration the company's considerable net cash position of nearly HKD1.8 billion. If one strips out this cash balance from the company's market capitalization, TVB is trading at a free cash flow yield of approximately 8.6% based on 2007 free cash flow. This is a compelling yield when one considers TVB's market position, the relative stability of its revenues, and its potential for future growth, even before taking into account the Mainland China opportunity. Lastly, there is reason to believe that capital expenditures could decline from the levels seen in recent years, as TVB has been investing in the development of DTT broadcasting and HDTV production capabilities, and both initiatives are believed to be near completion.

TVB's ability to grow book value also presents a compelling investment case. As shown in Exhibit 8, the company has grown book value at a compounded annual rate of nearly 10% over the last ten years, despite the recessionary pressures of 2008 and 2009. Further, this has been accomplished both net of a payout ratio that has averaged nearly 70% and without dilution, as total shares outstanding have remained constant at 438 million during this period.

Exhibit 8 TVB: Historical Book Value Growth
(HKD in thousands)

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Net Income	505,682	774,151	589,431	589,918	440,998	719,415	1,180,019	1,188,597	1,263,684	1,055,348	900,444
Dividends	362,613	416,100	416,100	416,100	350,400	438,000	678,900	744,600	788,400	744,600	700,800
Payout Ratio	72%	54%	71%	71%	79%	61%	58%	63%	62%	71%	78%
Shareholders' Equity	2,300,847	2,983,408	3,112,247	3,274,232	3,295,547	3,670,646	4,381,747	4,845,148	5,343,985	5,608,300	5,793,391
Growth - %		30%	4%	5%	1%	11%	19%	11%	10%	5%	3%
CAGR - '99-'09	*9.7%*										

The underpinning of TVB's free cash flow generation and book value growth is the company's very high return on invested capital. In 2009, for example, TVB posted a return on equity of 16% and a return on assets of 13.3%, despite experiencing a 15% decline in profitability. In 2008, the company's return on equity and return on assets was 19.6% and 16.9%, respectively. It is worth noting that TVB's return on assets is higher than most companies' return on equity.

Although these returns are impressive, they significantly understate the earnings potential of the company, as a significant portion of the company's assets are non-productive. As one can see from the company's balance sheet in Exhibit 11, current assets *exclusive* of cash exceeds total liabilities. Further, current assets net of *all* liabilities equal 39% of shareholders' equity. As an example of the profitability of the actual operating business, if the company were to simply pay out all of its cash (which would still leave it with a highly liquid balance sheet) and make the appropriate adjustment to shareholders' equity, the company's return on equity in 2008 would have been 34.2% rather than the previously mentioned 19.6%.

As shown in Exhibit 9, TVB is currently trading at EV/EBITDA multiples of 8.2x and 7.5x the 2010 and 2011 consensus EBITDA forecasts, respectively. While this is within the fairly wide range of other comparable companies, it is interesting to place these comparable multiples in context. For example, TVB trades at only a 14% premium to CBS Corp. based on 2010 EV/EBITDA, despite having a significantly higher return on equity. Consensus growth forecasts looking out to 2011 for both companies are the same, although this does not reflect the longer-term potential of the Mainland China market for TVB, or the fact that TVB's 2009 free cash flow yield relative to enterprise value is approximately 60% higher than that of CBS Corp. (6.7% versus 4.2%). On this basis, one could argue that TVB is the more compelling investment, even before considering TVB's Mainland China opportunity, implying that investors in TVB are receiving a free option on the company's potential entry into this market.

Exhibit 9 Comparable Company Valuations
(HKD in millions, except CBS Corp., which is $ in millions)

	TVB (511 HK)	Phoenix Satellite (2008 HK)	i-Cable Comm. (1097 HK)	CBS Corp. (NYSE: CBS)	PCCW Ltd. (8 HK)
Share Price (5/19/10)	HKD 36.00	HKD 1.81	HKD 1.22	$14.91	HKD 2.27
FD Shares Out. (mn.)	438.0	4,984.6	2,011.5	676.3	6,774.8
Market Capitalization	HKD 15,768	HKD 9,022	HKD 2,454	$10,084	HKD 15,379
Net Debt+Minority Interest	(HKD 1,761)	(HKD 296)	(HKD 437)	$6,098	HKD 26,864
Enterprise Value	HKD 14,007	HKD 8,726	HKD 2,017	$16,182	HKD 42,243
2009 Net Income*	HKD 900	HKD 300	(HKD 41)	$227	HKD 1,795
2009 Shareholders' Equity*	HKD 5,793	HKD 1,831	HKD 2,008	$9,019	(HKD 2,025)
ROE	16%	16%	N/A	3%	N/A
Average, ex. TVB	*9%*				
2010E EBITDA	HKD 1,714	HKD 554	HKD 303	$2,259	HKD 7,072
EV/EBITDA	8.2x	15.8x	6.7x	7.2x	6.0x
Average, ex. TVB	*9.9x*				
2011E EBITDA	HKD 1,859	HKD 706	HKD 439	$2,453	HKD 7,067
EV/EBITDA	7.5x	12.4x	4.6x	6.6x	6.0x
Average, ex. TVB	*7.9x*				
2010E EPS	HKD 2.63	HKD 0.08	(HKD 0.02)	$0.96	HKD 0.22
Price/2010E EPS	13.7x	23.2x	N/A	15.5x	10.2x
Average, ex. TVB	*19.4x*				
2011E EPS	HKD 2.97	HKD 0.10	HKD 0.01	$1.17	HKD 0.25
Price/2011E EPS	12.1x	18.5x	87.1x	12.7x	9.2x
Average, ex. TVB	*39.5x*				

*Excludes minority interest

Source: Company reports, Thomson One, *The Spin-Off Report* estimates.

The upside to TVB's valuation is arguably demonstrated by another comparable, Phoenix Satellite. Despite having comparable returns on equity, Phoenix Satellite ("Phoenix") trades at a significant premium to TVB owing to its higher growth profile (expected EBITDA growth in 2011 is more than three times that of TVB), which is driven by the fact that it is one of the only non-government-related broadcasters available to the Mainland. Further, Phoenix is on good terms with the Chinese government, which holds a significant, indirect ownership stake in the company. If TVB is able to establish as solid a footing in the Mainland China market, Phoenix may serve as an indication of the outsized growth and multiple expansion that TVB could realize.

Phoenix derived over 90% of its HKD1,530 million in 2009 revenues from Mainland China. However, these revenues are not quite as profitable as TVB's existing business. Phoenix earned an EBITDA margin of 32% and a pre-tax margin of 25% in 2009, relative to TVB's results of 40% and 31%, respectively, although Phoenix's efficiency could improve with additional scale.

If one assumes that TVB can achieve a level of market penetration comparable to that of Phoenix, we can begin to assess just how profitable the Mainland China opportunity could be, even in the very early stages of entry into that market. For example, a similar level of revenues would boost TVB's top line by approximately 38% and grow EBITDA by roughly 30%, assuming margins at the level that Phoenix currently achieves. Further, using Phoenix's consensus growth forecast for 2011 as a proxy, TVB would have approximately one-third of its business growing at close to a 30% rate.

Given the demonstrated popularity of TVB's programming, as outlined in the "Company Description" section, it seems reasonable to assume that TVB could gain a presence comparable to that of Phoenix if given the opportunity to operate in Mainland China. Further, given the company's current valuation, it can be argued that investors are paying little, if anything, for this potential. To be sure, there is no shortage of quality companies with normalized free cash flow yields approaching 9% in today's market. However, TVB does appear to be a good value based solely on its existing business, which has the potential to achieve stable earnings from the core broadcasting business and continued growth from its international markets and its subscription business. It is also worth nothing that, when compared to such US companies as CBS Corp., TVB offers a more attractive free cash flow yield relative to enterprise value based on current operations, while providing the added potential for massive growth in the Mainland China market. As such, we recommend shares of TVB for purchase.

Conclusion

TVB is currently trading at 8.2x consensus EBITDA estimates for 2010 and at a free cash flow yield of 6% based on depressed 2009 results. The company has demonstrated significantly higher earnings in a healthier economic environment and is also likely to see a lower level of capital expenditures going forward, as a number of recent investment projects appear to be coming to a close. Further, the company's net cash position of HKD1.8 billion gives it significant financial flexibility and, with a return on equity of 16%, the capital to fund profitable growth given adequate investment opportunities. If one looks to TVB's historical earnings potential, the company's normalized free cash flow yield approaches 9%, thus making TVB shares a compelling investment opportunity when one considers the company's market position, its relative stability, and its potential for growth in its existing markets.

This growth potential, however, does not speak to the massive opportunity represented by possible entry into Mainland China where the company's content has demonstrated significant popularity. Although the Mainland China market is still in the early stages of development, it is a source of significant earnings and growth for its few existing participants and could provide TVB with as much as a 30% boost in EBITDA in a relatively short period of time. One could argue that this growth opportunity is not reflected in TVB's current valuation and, as such, an investment in TVB shares appears to carry a free option on its potential entry into Mainland China.

To be sure, entry into the Mainland has its obstacles, including government approval to broadcast in the region and the likely need to find a local partner. The demand exists for TVB's content, however, and, given the company's apparent willingness to self-censor, the likelihood of future entry into Mainland China cannot be dismissed. Again, considering that investors are receiving this potentially lucrative option for free, shares of TVB are recommended for purchase.

Exhibit 10 TVB: Consolidated Income Statement
(HKD in thousands, except per-share amounts)

	2006	2007	2008	2009
Turnover				
Ad income, net of agency deductions	2,681,120	2,691,325	2,755,575	2,399,781
Licensing income	815,500	824,692	821,382	796,611
Subscription income	422,625	454,497	475,717	464,948
Others	328,441	405,785	402,012	372,160
Less: withholding tax	(46,500)	(50,490)	(47,382)	(50,168)
	4,201,186	4,325,809	4,407,304	3,983,332
Cost of sales	(1,778,433)	(1,763,971)	(2,025,045)	(1,780,942)
Gross profit	2,422,753	2,561,838	2,382,259	2,202,390
Other revenues				
Interest income	58,080	89,165	56,868	11,665
Other rental income	15,816	14,795	13,547	27,688
	73,896	103,960	70,415	39,353
Selling, distribution, and transmission costs	(451,064)	(453,001)	(507,396)	(455,506)
General and administrative expenses	(504,427)	(569,801)	(569,764)	(504,590)
Other gains/(losses), net	57,670	26,529	(18,928)	9,204
Gain on disposal of equity interest in associate		140,000		
Impairment on trade receivables from associate		(135,000)		
Finance costs	(98)		(7,581)	(4,498)
Share of losses of associates	(163,109)	(124,982)	(63,174)	(64,971)
Profit before income tax	1,435,621	1,549,543	1,285,831	1,221,382
Income tax expense	(247,181)	(284,322)	(229,544)	(320,626)
Profit for the year	1,188,440	1,265,221	1,056,287	900,756
Profit attributable to:				
Equity holders of TVB	1,188,597	1,263,684	1,055,348	900,444
Minority interest	(157)	1,537	939	312
	1,188,440	1,265,221	1,056,287	900,756
Shares in issue (in millions)	438,000	438,000	438,000	438,000
EPS (basic and diluted)	2.71	2.89	2.41	2.06

Source: Company reports.

Exhibit 11 TVB: Consolidated Balance Sheet
(HKD in thousands)

	2008	2009
ASSETS		
Current assets		
Programmes and film rights	412,219	366,133
Stocks	12,952	13,056
Trade and other receivables, prepayments, and deposits	1,095,718	1,152,715
Tax recoverable	1,716	2,802
Pledged bank deposits	5,158	7,002
Bank deposits maturing after three months	130,422	194,179
Cash and cash equivalents	1,963,094	1,893,586
	3,621,279	3,629,473
Non-current assets		
Property, plant and equipment	2,322,872	2,345,621
Leasehold land	208,922	203,466
Goodwill	161,145	163,248
Interests in jointly controlled entity	-	7,500
Interests in associates	375,674	675,830
Available-for-sale financial assets	3	3
Deferred income tax assets	16,925	17,995
Prepayment	35,182	-
	3,120,723	3,413,663
Total assets	6,742,002	7,043,136
LIABILITIES		
Current liabilities		
Trade and other payables and accruals	593,810	640,153
Current income tax liabilities	61,598	164,131
Borrowings	22,367	22,778
	677,775	827,062
Non-current liabilities		
Borrowings	296,357	279,030
Deferred income tax liabilities	124,394	111,713
Retirement benefit obligations	9,563	6,706
	430,314	397,449
Total liabilities	1,108,089	1,224,511
EQUITY		
Equity attributable to equity holders		
Share capital	21,900	21,900
Other reserves	696,886	723,094
Retained earnings		
Proposed final dividend	613,200	591,300
Others	4,276,314	4,457,097
	5,608,300	5,793,391
Minority interest	25,613	25,234
Total equity	5,633,913	5,818,625
Total equity and liabilities	6,742,002	7,043,136

Source: Company reports.