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The Big Leap to a formal economy

Volume 2.2



Volume 1



Ground Reality
Jewelry

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Contents

Shift likely to remain gradual	3
The large Indian jewelry industry.....	4
Organized market share has been gradually rising.....	9
GST & demonetization–will it change industry dynamics?	11
Companies	17
Titan: India's leading player in branded jewelry.....	18
PC Jeweller: 2nd largest listed jewelry retailer in India	20
TBZ: A 150-year old brand.....	22

The Big Leap



Shift likely to remain gradual

Pace can intensify with stringent cash transaction norms

- India is on a structural path towards a formal economy, (please refer to our inaugural issue of “The Big Leap” series) prodded by a string of government initiatives such as demonetization, GST, and Aadhar-linking. While these are steps in the right direction, we believe the shift will be prompt for some sectors, gradual for others, and might remain challenging for a few.
- In this edition, we focus on the ~INR3t Indian Jewelry industry, where we believe the shift will be gradual. A fragmented industry, it is dominated by the unorganized segment (estimated at INR1.2t; 70% of domestic jewelry sales), and changes in administrative procedures under the GST regime using technology are unlikely to accelerate the shift towards organized players.
- Yet, a material reduction in the threshold for cash purchases without identity proof could be the catalyst, and would benefit large organized players like Titan, P C Jewellers, Malabar Gold & Diamonds, Kalyan Jewellers, and Joyalukkas among others.

Significant opportunity to formalize the sector

- Gems and jewelry have historically been a preferred mode of accumulating illicit wealth in India. Given the high faith in family jewelers (usually unorganized) that have been offering competitive pricing and their expertise in traditional jewelry over generations, the sector has come to be dominated by the unorganized trade, estimated at ~INR1.2t (70% of overall domestic industry revenue).
- However, with rising urbanization, change in government policies & consumer preferences, and emergence of strong brands, there has been a steady increase in the market share of organized players from 10% in 2000 to 30% in 2016.

Administrative policy changes under GST unlikely to formalize jewelry trade

- The Indian government is taking initiatives to shift trade in favor of the formal economy. GST, with its new administrative procedures and technology, is yet another step to formalize the trade. This presents an opportunity to investors to take advantage by investing in sectors likely to benefit.
- However, we believe that with a small B2C supply chain, the Jewelry sector can continue to operate end-to-end in the parallel economy. Changes in the administrative procedures and technology platform are unlikely to alter the trajectory of shift of trade towards the formal economy.

Significant reduction in cash transaction limit needed to drive the shift

- We believe that revealing of the identity of the buyer will be the key to check the investment of illicit wealth in the sector. A significant reduction in the threshold limit for cash purchases (without identification proof) could be a key catalyst to accelerate the shift toward formal trade.

Big Leap Report – Volume 2.1



The large Indian jewelry industry

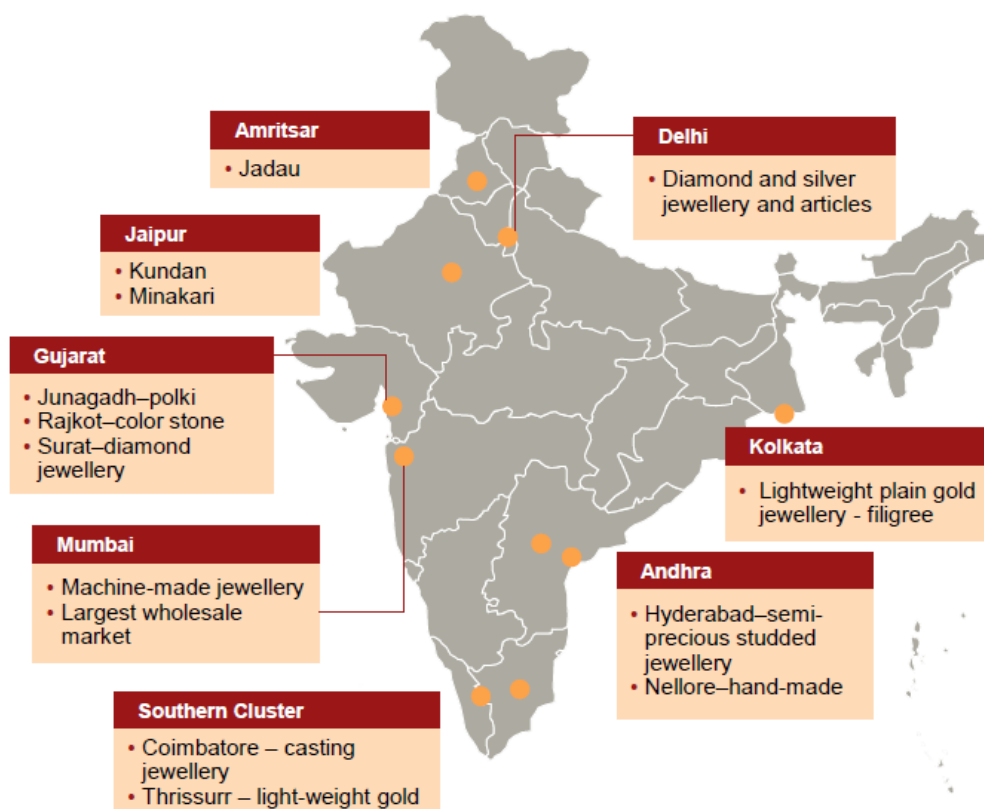
- India's INR3t Gems and Jewelry industry is one of the largest in the world, and caters to both exports (~44%) and domestic demand (~56%).
- However, the sector has been import-dependent due to limited mines in India for key inputs – gold, diamonds, and other precious/semi-precious stones.
- The industry is fragmented, with more than 0.5m players, and is largely dominated by small and mid-size retailers. However, over the last two decades, regional and national-level players have been gaining share.

Indian Gems & Jewelry industry – one of the largest in the world

- The Indian Gems and Jewelry (G&J) industry, estimated at ~INR3t, is one of the largest in the world, with a 29% share in global jewelry consumption.
- The industry is highly fragmented, with more than 0.5m gems and jewelry players across the country. It provides employment to nearly 2.5m people.
- The cultural diversity of India has led to a large variety of customer preferences across the country. To cater to the regional preferences, many jewelry manufacturing hubs have developed in India.

Indian Gems and Jewelry industry, at ~INR3t, is one of the largest in the world, with ~29% share in global jewelry consumption

Exhibit 1: Major jewelry manufacturing hubs in India

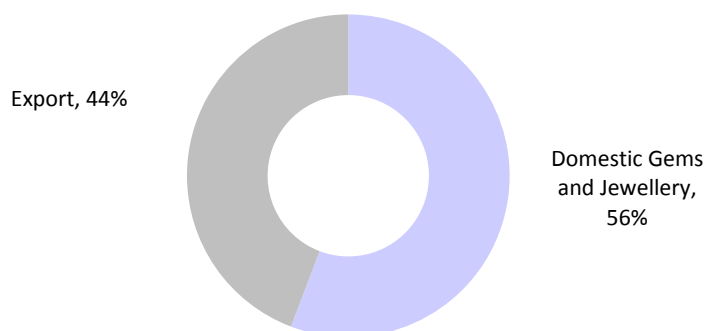


Source: A. T. Kearney analysis, MOSL

Industry revenues – a blend of domestic consumption and exports

- The Indian Gems and Jewelry (G&J) industry caters to both domestic and export demand. While exports constitute 44% of the overall industry revenue, domestic consumption constitutes a larger part of the revenue pie at ~56%.

Exhibit 2: Exports account for a huge chunk of the industry



*for 2013

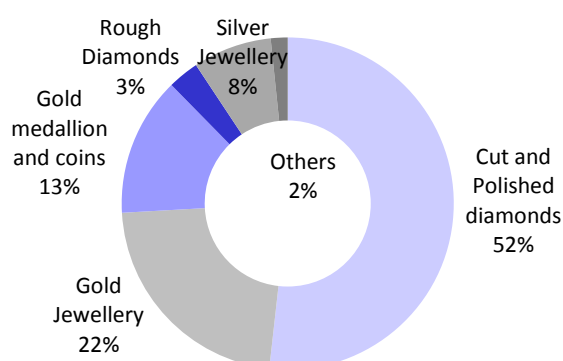
Source: FICCI, MOSL

Jewelry – a big contributor to forex earnings

G&J industry contributes 10-12% of the country's total exports trade

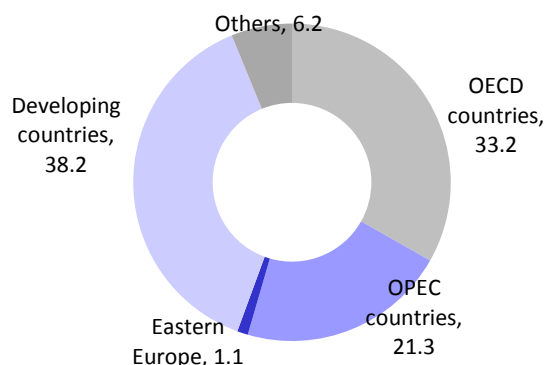
- The Indian G&J sector is a big forex earner for India and currently contributes 10-12% of total exports. Since 2004, it has earned over USD369b (INR19,024b) of foreign exchange.
- G&J export revenue is estimated at ~USD40b, of which ~55% is from cut and polished / rough diamonds and the balance from jewelry / coins and medallions.
- The Indian diamond industry has grown from its small origins in the 50s. India has established itself as the world's largest manufacturing center of cut and polished diamonds, contributing 60% of the world's supply in terms of value, 85% in terms of volume, and 92% in terms of pieces.
- India is one of the largest gold jewelry exporters in the world. In FY16, Indian gold jewelry shipments came to ~USD9b, with around half delivered to India's largest jewelry export destination, the UAE.

Exhibit 3: Diamond contributes > 50% of G&J exports



Source: World gold council, MOSL

Exhibit 4: Significant exports to developing countries (%)



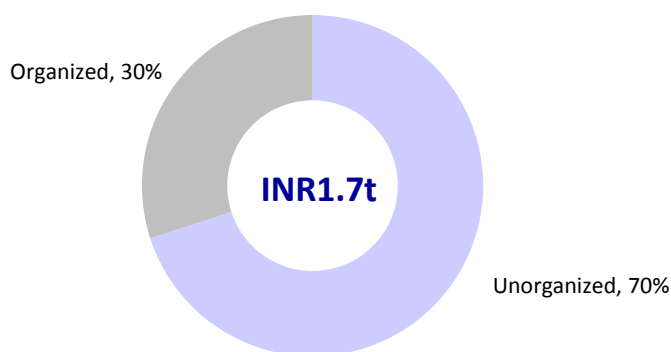
Source: Industry, MOSL

India has a large domestic gems and jewelry market

- The domestic G&J market is estimated at ~INR1.7t and is highly fragmented. The industry is dominated by standalone jewelers and medium-size retailers.
- However, over the last 15 years, large regional and national-level retailers have been taking market share from standalone jewelers and mid-size retailers.

Exhibit 5: Unorganized players dominate domestic Jewelry market

The domestic gems and jewelry market is ~INR1.7t, of which ~70% is unorganized

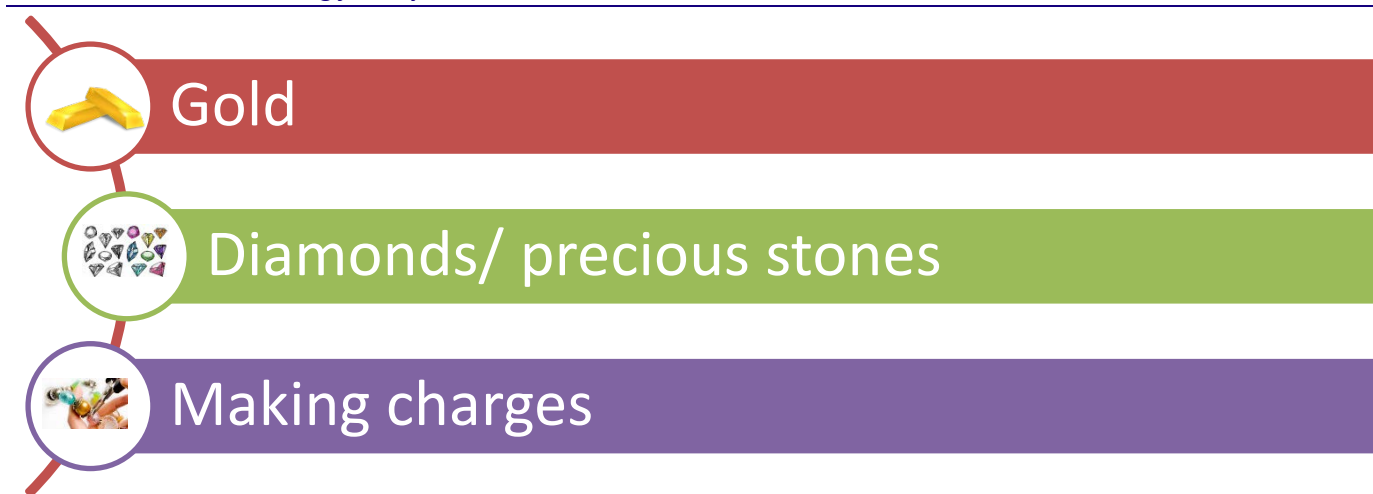


Source: World gold council, MOSL

Industry remains heavily dependent on imported raw materials

- There are three primary inputs for making jewelry – gold, diamonds/precious stones, and labor.

Exhibit 6: Elements in making jewelry



Source: MOSL

- Currently, India has very little captive supply of gold, diamonds, and other precious / semi-precious stones. Hence, it remains import dependent.

I. GOLD

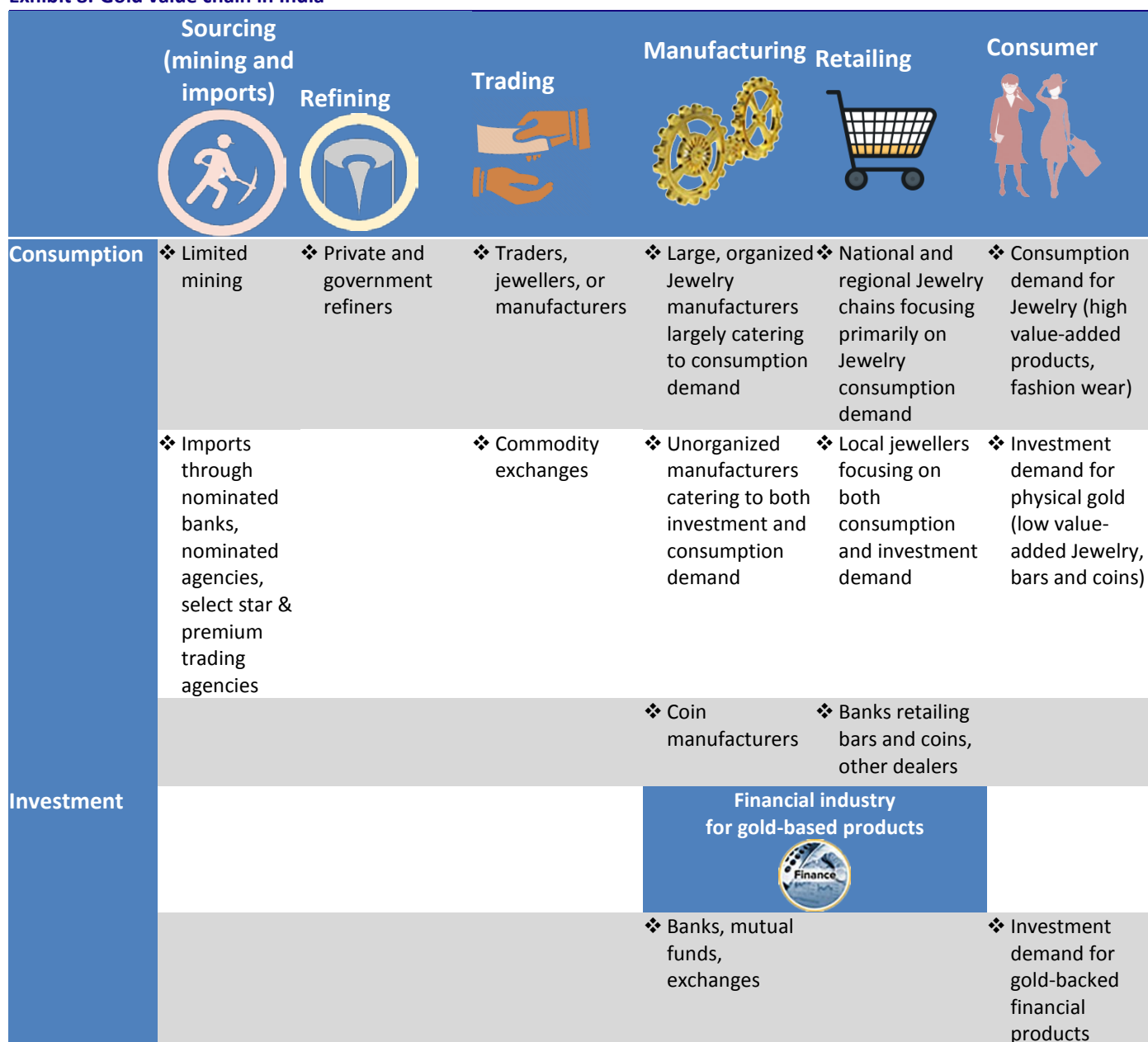
- Gold is a primary raw material for manufacturing jewelry. Gold and jewelry are used both for consumption and investment.
- In FY16, India imported ~675.5 tons of gold. Only nominated banks, nominated agencies or bullion banks, and select star and premier trading houses and export oriented units (EOUs) can import gold under the current regulations.
- Hence, most gold is imported through a handful of bodies and is largely organized and consolidated among a few players.

Gold demand is primarily met through imports, which are largely organized and consolidated among few players

Exhibit 7: Who can import gold in India

Banks		Trading houses/agencies	
Axis Bank	Kotak Mahindra Bank Ltd	Metals and Minerals Trading Corporation Ltd (MMTC)	Council (G&J EPC)
Bank of Baroda	Karur Vysya Bank Ltd	Handicraft and Handloom Export Corporation (HHEC)	EOU and SEZ gems and Jewelry units, for their own consumption
Bank of India	Oriental Bank of Commerce	State Trading Corporation (STC)	Premier Trading Houses
Bank of Nova Scotia	PNB	Project and Equipment Corporation of India Ltd (PEC)	Star Trading Houses (only for the gems and Jewelry sector)
Corporation Bank	South Indian Bank Ltd	STCL Ltd	
Federal Bank Ltd	State Bank of Hyderabad	MSTC Ltd	
HDFC Bank Ltd	State Bank of India	Diamond India Limited (DIL)	
ICICI Bank Ltd	Union Bank of India	Gems & Jewelry Export Promotion	
Indian Overseas Bank	Yes Bank Ltd		
IndusInd Bank Ltd	The Ratnakar Bank Limited		

Source: World Gold Council, MOSL

Exhibit 8: Gold value chain in India

Source: A. T. Kearney analysis

Besides official imports, smuggling and recycling are the other major sources

- Besides official imports, smuggling and recycling are the other major sources of meeting the gold requirement.

Diamonds are also imported into India; however, they are imported as roughs and then processed in India

II. Diamonds and precious stones

- India does not have any significant mines for diamonds and other precious/semi-precious stones. It imports rough diamonds in bulk from trading hubs like Belgium, Israel, UAE and Hong Kong among others.
- Rough stones are sourced from DTC holders via the official channel.
- India is one of the largest cutting and polishing centers in the world. 14 out of every 15 diamonds set in jewelry worldwide are processed in India.
- Surat, Navsari, Bhavnagar and Amreli are the diamond manufacturing/processing hubs whereas Mumbai is the diamond trading hub. India is the world leader in diamonds, both in quantity and value terms.

Organized market share has been gradually rising

- The domestic Jewelry industry is largely unorganized. Unorganized players account for ~70% share of the market. This is because (a) jewelry is a preferred mode of keeping illicit wealth, and (b) small/mid-size family jewelers enjoy high trust, and offer competitive pricing and expertise in traditional jewelry.
- However, over the last 15 years, rising urbanization, change in government policies and consumer preferences, and growing faith in large brands have helped organized players to gain market share from ~10% to ~30%.

A fragmented market dominated by unorganized players

- The retail jewelry market in India has for long remained highly fragmented and dominated by unorganized players.
- In FY00, ~90% of India's gold retailers were "unorganized" – small, standalone retailers, often family jewelers. Unorganized retailers still dominate the market, but the share of organized retailers has trebled to 30%.
- We believe that the unorganized segment has remained large due to (a) gold and jewelry being a preferred mode of keeping illicit wealth, (b) historical government policies restricting gold holdings (repealed since 1990); however, psychological effect remains, (c) high difference in making charges of organized and unorganized players, (d) high trust on small/mid-size family jewelers, and (d) higher demand for traditional jewelry, where unorganized players have expertise and decades of experience.

Unorganized players continue to dominate domestic jewelry industry; however, their market share has declined from 90% to 70% in the last 15 years

Exhibit 9: Organized market share very small...

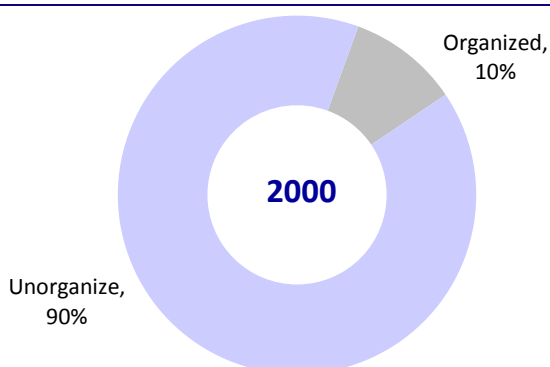
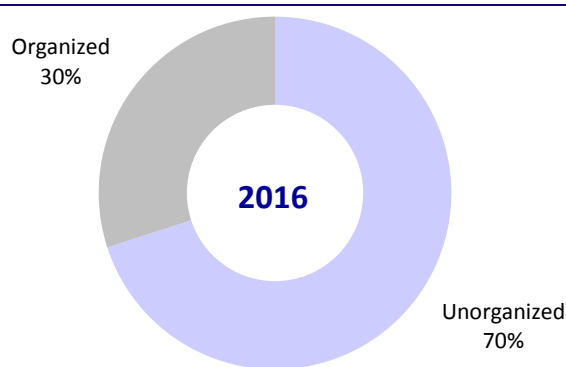


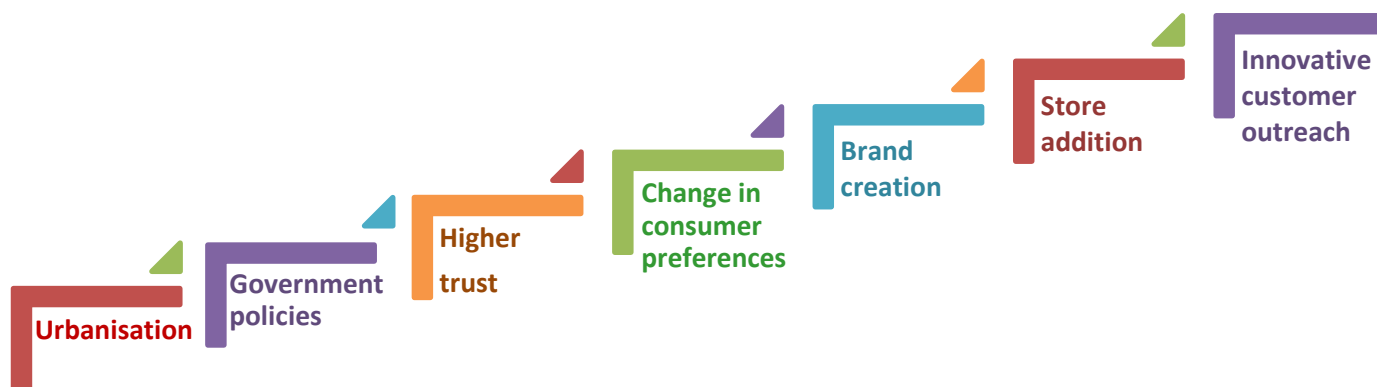
Exhibit 10: ... but gradually rising over the years



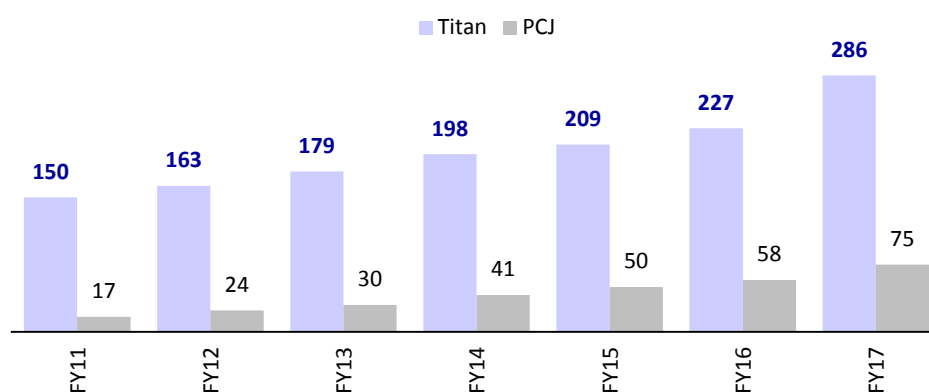
Source: Industry, MOSL

Organized players gradually gaining market share

- Over the last 15 years, organized players have gradually been gaining share. The shift of trade is primarily due to growing urbanization, change in consumer preferences and government policies, increase in reach of organized players, and growing faith in large brands.
- Proactive measures by organized players like introduction of sophisticated advertising and sales campaigns, effective inventory management systems, innovative customer outreach and building of domestic and international brands are also aiding the shift in favor of the organized segment.

Exhibit 11: Reasons for shift in trade to organized segment over the years

Source: MOSL

Exhibit 12: Store additions rising over the years (Nos)

Source: Company, MOSL

Exhibit 13: Significant presence of regional/national bands (FY16)

Company	Stores	Cities/Towns
Titan	227	120
PC Jewelers	58	48
Shubh Retail	80	NA
Malabar Gold and Diamond	80	69
Kalyan	68	59
Joyalukkas	58	53

Source: World gold council, MOSL

GST & demonetization—will it change industry dynamics?

- The Indian government has taken various initiatives (such as demonetization and GST) to shift trade to the formal economy.
- Our discussions with jewelry industry participants indicate that the administrative procedural changes under the GST regime are unlikely to lead to a material acceleration in the shift towards organized trade.
- However, materially reducing the cash transaction limit and making it mandatory to furnish identity proof for high-value jewelry purchases could accelerate the shift.

GST and demonetization – big drivers of shift towards formal economy

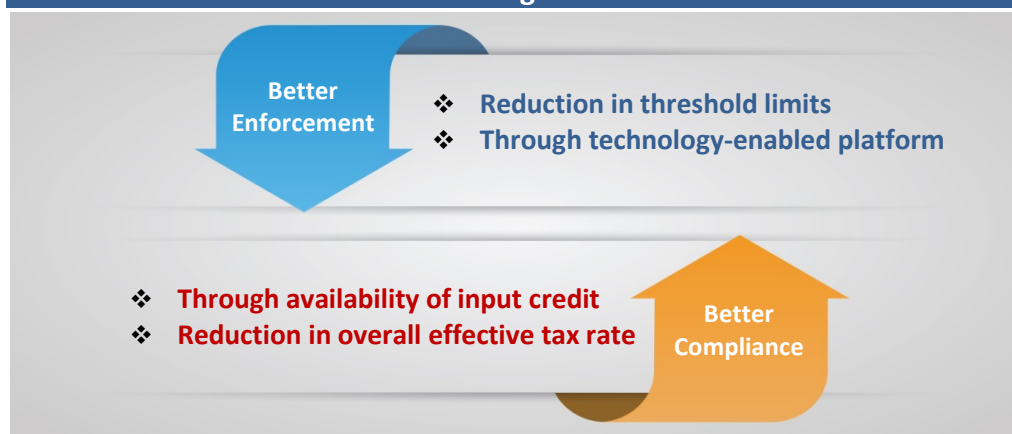
- India is set to see a shift in favor of the organized (formal) segment, with the government taking a number of initiatives to curb the shadow economy.
- Demonetization of high-value currency notes has created fear among unorganized players, as transactions in this space were mostly cash-based and unaccounted. Even in the recent budget announcements, cash transactions of INR0.2m or more have been prohibited.
- Also, with GST implementation nearing reality, the organized segment is well poised to confront the high presence of unorganized (informal) players.
- The impending shift could present attractive investment opportunities. Yet, our discussions with experts and sector participants highlight that the shift will be prompt for some sectors, gradual for others, and challenging for a few.

With GST at the backdrop, our discussions with experts and sector participants highlight that the shift to formal trade will be prompt for some sectors, gradual for others and challenging for a few.

Will the drivers be effective for the Jewelry industry too?

- As discussed in our previous report ([click here to access](#)), to analyze the pace of the shift (to organized) for each sector, one has to carefully consider the administrative/procedural changes and the tax rates under GST.
- We believe the following measures can potentially accelerate the shift toward formal trade: (a) reducing threshold limit for exemption from indirect taxes, (b) tracking flow of GST credit in the entire value chain by using technology platforms, (c) ensuring availability of seamless input credit, and (d) reducing overall effective tax rates.

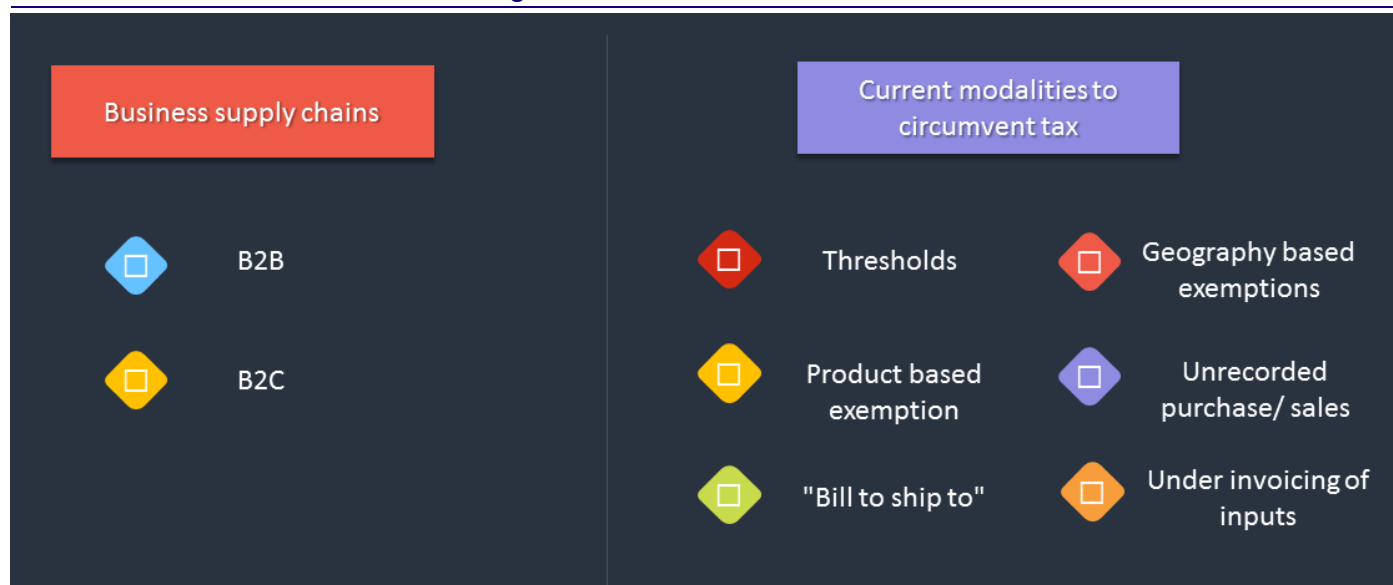
Measures that could lead to shift to organized trade



Source: MOSL

- To estimate the pace of shift to formal economy for each sector, one needs to look at: (a) the supply chain the sector works with, (b) operational nuances of players in the unorganized segment, and (c) how government initiatives will change the way in which unorganized segment players operate.

Exhibit 14: Critical determinants of shift to organized trade



Source: MOSL

Short B2C supply chain may continue to be unorganized under GST

- To determine the probability of shift in trade from unorganized to organized, it is imperative to understand the supply chain in which the entity operates. We note that any break in the organized chain leads to the beginning of unorganized trade. We believe that in the GST regime, a conversion to organized in the B2B chain will be relatively easy as compared with the B2C chain.
- We believe the shift to organized trade in short B2C chains (where manufacturers/service providers source raw materials/inputs from the unorganized market, and continue supplying in unorganized manner throughout the supply chain) will be difficult.
- This is primarily due to the fact that only businesses can register on the GST network and claim the benefit of input credit. End-consumers will not have any direct benefits for being part of the organized chain. Also, most consumers are indifferent to choosing between organized and unorganized players; the focus is more on pricing.
- Also, in the Jewelry industry, we believe it is demand for 'unorganized goods' that drives supply. The customer is habituated to parking illicit wealth in gems and jewelry. Since the customer demand is for jewelry in exchange for cash, business participants looking to generate extra revenue offer suitable solutions to meet this demand.

Smuggling, managing input output ratio, and 'bill to ship to' mechanism are key facilitators to run the unorganized trade

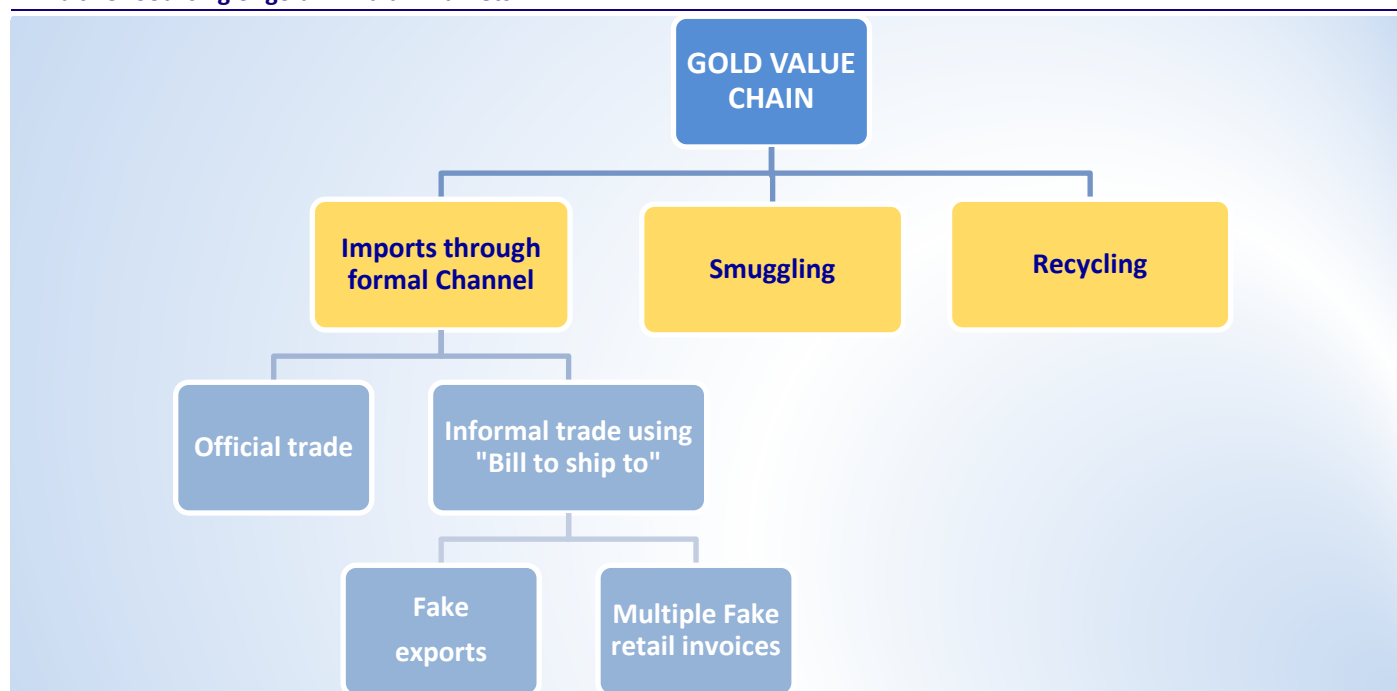
Modalities of circumventing taxes in Gems and Jewelry industry

- Our discussions with various sector participants suggest that the Jewelry industry stems from two primary industries: (1) Gold, and (2) Diamonds and other Precious Stones.
- To understand how unorganized trade happens in Jewelry, let us understand how this industry sources raw materials from these two primary industries.

Gold finds its way into unorganized trade in multiple ways

- India has very limited captive production of gold, and hence, is primarily dependent on imports.
- We note that besides formal imports, smuggling and recycling of old gold are the other two primary sources of meeting the country's demand.
- While most of the smuggled and recycled gold continues to be part of the unorganized trade, our discussions with trade participants suggest that even some portion of the formally imported gold finds its way to the unorganized jewelry trade.

Exhibit 15: Sourcing of gold in Indian markets



Source: MOSL

Smuggling accounts for 15-20% of gold demand

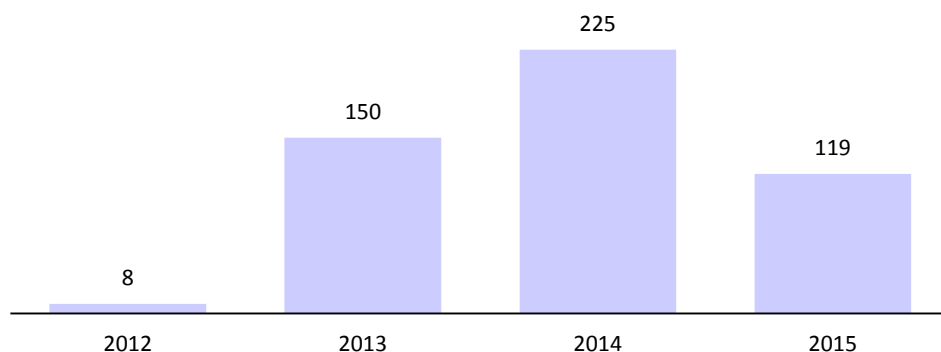
- According to the World Gold Council, ~119 tonnes (total demand: 668 tonnes) of gold is smuggled into India annually. Of this, 65–75% comes in by air, 20-25% by sea, and 5-10% by land.
- Bullion import regulations encourage unofficial flows into India. The Gold Control Act created a lively market in smuggled gold, but its repeal in 1990 saw unofficial imports collapse.
- In 2013, to control ballooning gold imports, the government gradually increased import duty, which eventually reached 10%. This was followed by the 80:20 rule, which is repealed now. These measures created significant market distortions,

Gold smuggling increased significantly post 2013 on increase in customs duty to 10%

resulting in a surge in domestic gold premiums. It became very profitable to smuggle gold into India.

- Most of the gold flown into India comes from the Middle East, notably the UAE, and is carried out by low income workers returning home. In exchange for their services, they receive carrier fees and a sponsored air ticket. Smuggling via land or sea routes occurs through porous borders with neighbors.
- In the first half of 2016, in response to the 1% manufacturing excise duty, smuggling activity from Thailand also increased.

Exhibit 16: Smuggling increased as government hiked customs duty in 2013 (Tonnes)



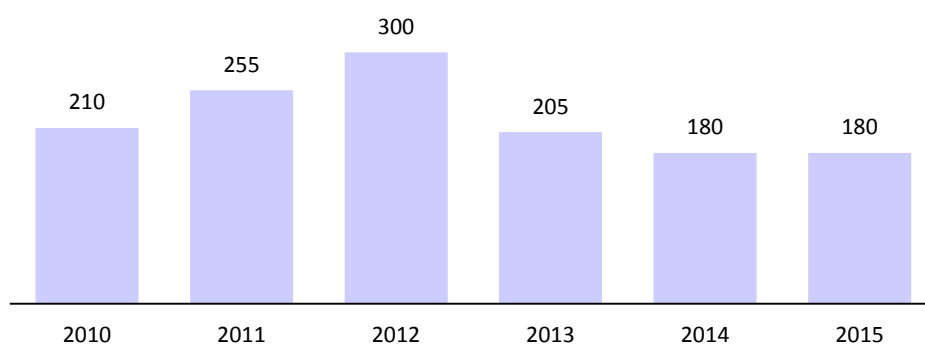
Source: World gold council

Gold demand is sourced through recycling

- Recycling is an important source of supply for jewelers. Recycled gold plays an important role in India's gold supply, fulfilling Indian jewelry fabrication needs since 1990. Recycling is generally done from gold sourced from:
 - **Gold exchanged for jewelry:** In price-sensitive markets, consumers often exchange their gold jewelry, bars or coins for new pieces of gold jewelry. The only cost to them is the making charge. This mechanism provides a significant flow of gold into the jewelry industry.
 - **Gold sold for cash:** Gold is often sold by households to raise cash. In such cases, jewelers generally deduct 2-5% of the value.

Gold recycling remains one of the facilitators of unorganized trade

Exhibit 17: Gold recycling over the years (tonnes)



Source: World Gold Council, MOSL

Formal gold imports also enter the informal jewelry supply chain

- Our discussions with the trade channel highlight that even some of the formally imported gold finds its way into the informal chain. This primarily happens in what is called “bill to ship to” mechanism – the physical delivery of the goods is made to someone else and the goods are billed to a third party. This happens in two ways:

Fake exports

- One of the mechanisms prevalent in the industry is what is popularly known as paper exports. Bills are generated to show exports of gold / jewelry. However, the physical goods are sold in the domestic informal channel.
- The use of this mechanism has reduced considerably.

Multiple domestic retail invoices

- Gold imported formally also finds its way into the informal economy, as buying gold is a popular means of parking illicit wealth.
- It is mandatory to obtain the buyer’s PAN details for transactions above INR0.2m. To circumvent this, sellers make multiple invoices for amounts less than INR0.2m while the physical gold is sold in bulk.
- This gold is often used for jewelry manufacturing in the informal chain. While there is no material tax saving in doing this from the gold perspective, it helps in (a) deployment of illicit wealth, and (b) there is no taxation on the value addition (making charges and value of diamonds/other gemstones used).

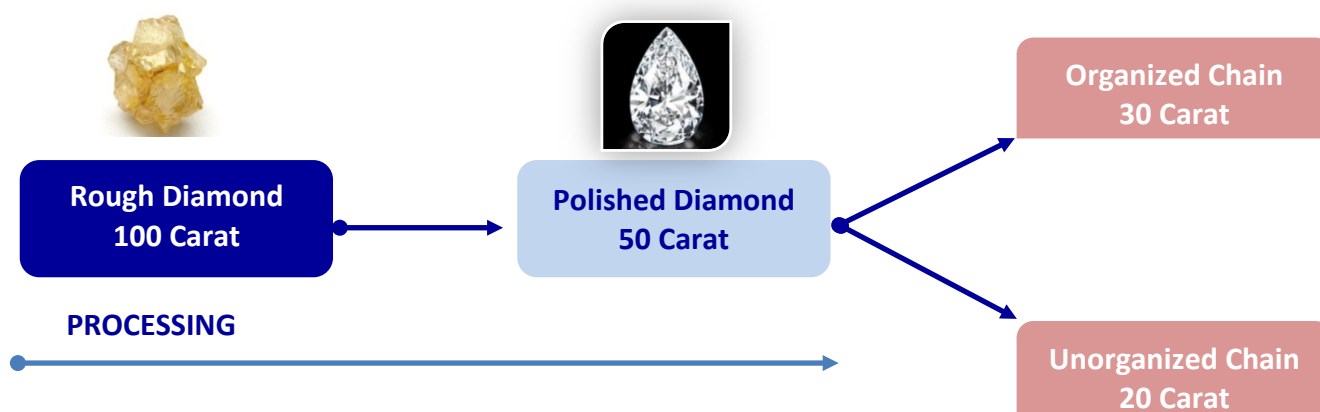
Diamonds and gemstones – input-output ratio difficult to measure

- India imports rough diamonds and other gemstones. These are further processed to form cut and polished diamonds/gemstones.
- There is a huge variation in the input-output ratio in conversion of rough stones to the final cut-and-polished product. It ranges from 30% to 50% of the input.
- The output depends on the skill of the worker and quality of the rough stone, leaving a lot of scope for manipulation of inventory. Also, the pricing of diamonds and stones is a matter of judgment and very difficult to estimate.
- This variation in output along with the difficulty in estimating price gives the manufacturer a huge opportunity to officially show low output and sell the rest in the informal economy.

“Bill to ship to” mechanism is a popular way to source gold from formal trade to unorganized jewelry trade

Non-standardized input-output ratio in processing diamonds facilitates supplies to unorganized trade

Exhibit 18: Input-output ratio adjusted to manage inventory



Source: MOSL

All participants in the jewelry value chain can end-to-end remain outside the technology platform and continue to trade in an unorganized manner

Escape from administrative and technology platform likely

- Under GST, the government intends to employ technology to track end-to-end credit flow in the value chain. Bilateral validation of invoices, online integration of data and big data analytics will go a long way in addressing the loopholes in tax administration.
- The IT portal can capture data even if at least one participant in the value chain sells goods through the organized chain (and hence, is a part of the GSTN).
- However, in industries like Gems and Jewelry (G&J), it is possible for all participants in the value chain to stay outside the formal trade, and thus, escape from data capture by the technology platform.
- We note that the G&J industry has a small B2C supply chain, where raw material (gold, diamonds and other gemstones) is sourced by the jewelry manufacturers and the end products are sold to the retail consumers via family jewelers.
- In our view, the unorganized players can continue to get key raw materials used for manufacturing of jewelry in the following manner:
 - **Gold** is available through smuggling, recycling and 'bill to ship to' mechanism.
 - **Diamond and other gemstones:** These can be made available by managing the input-output ratio at the end diamond/gemstone processing units (engaged in cutting and polishing of roughs).

Higher GST rates further disincentive to shift to formal trade

- GST rates on gems and jewelry have been increased to 3% v/s the current effective tax rate of 2-2.2%. We believe that increase in the effective tax rates applicable to the formal industry (will be passed on, though) will only act as a slight disincentive for the participants to become part of the formal chain.
- Also, we note that the price differential between an organized and an unorganized player is high at 20-25%. This is primarily on account of higher making charges and higher prices of diamonds levied by the organized players; also, the unorganized players engage in under-carting of gold and diamonds to reduce their pricing.
- Though the finishing of jewelry is apparently better for organized players, we believe that the price differential and acceptance of cash by unorganized players are enough to drive consumers towards unorganized players.

Mandatory buyer identification could accelerate shift to formal segment

- Purchasing gold and jewelry is a preferred mode of investing illicit wealth.
- While the government is taking multiple steps to propel the shift of trade from unorganized to organized, the retail buyer may not get identified under GST (since individual customers do not require a GSTN registration).
- We believe that if the government is able to create a mechanism by which the buyer in each transaction is identified, the shift towards a formal economy would be accelerated. This can be achieved by significantly reducing the cash transaction limit (currently INR0.2m) above which obtaining the buyer's PAN card/identity card is mandatory.
- We believe this will cut down a significant proportion of gold trade which originates in the formal import channel but later enters the unorganized trade.

Significant reduction in the cash transaction limit without identity proof can lead to a significant shift of trade to formal economy

Companies

BSE Sensex: 31,805

S&P CNX: 9,816

July 2017

Titan

PC Jeweller

TBZ





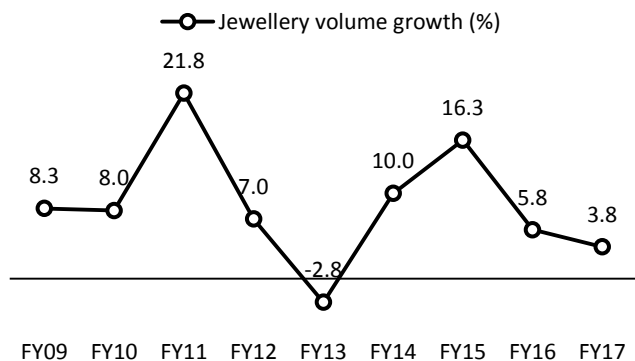
Titan: India's leading player in branded jewelry

- The Titan Company is India's leading player in Branded Jewelry, Watches, and Eyewear. The company was formed in 1984 as a joint venture between the Tata Group and Tamil Nadu Industrial Development Corporation.
- It has pioneered the Branded Jewelry concept in India and has created a sizable leadership presence in both Jewelry and Watches, leveraging its Tata brand equity. Competition exists in both segments, but Titan has continued to lead.
- In Jewelry, Titan innovated its offerings and created specific sub-brands for the youth and working women. It introduced Light-Weight Jewelry for fashion-conscious consumers. The company was growing strongly in Adornment Jewelry. However, market slowdown due to weak consumer sentiment and regulatory issues in the Golden Harvest Scheme (used to account for 30% of sales at peak) necessitated an entry into Wedding Jewelry. Wedding Jewelry (INR1.5t) is a much bigger market than Adornment Jewelry (INR0.5t).
- In Watches, Titan has created a portfolio that straddles price points and aspirations. This has helped it to retain consumers across cycles of premiumization and down-trading.
- To de-risk its long-term business from cyclical associated with the Jewelry business, Titan is targeting emerging lifestyle categories with significant unorganized presence – Eyewear, Fragrance, Helmets, Sarees.
- Titan's financials have shown significant transformation in the 2000-13, with improvement in balance sheet leverage, consistent free cash generation, best-in-class RoE despite aggressive retail space expansion, and healthy earnings growth. However, slowdown in discretionary consumption coupled with regulatory challenges has adversely impacted financials in FY14-16.

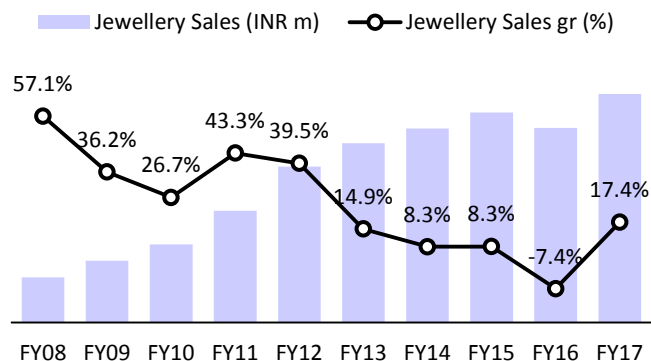
Exhibit 19: Titan (INR m): Financials snapshot

Titan	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17
Sales	30,540	39,110	47,791	65,331	88,484	101,233	109,274	119,134	112,779	129,789
YoY Change (%)	43.0	28.1	22.2	36.7	35.4	14.4	7.9	9.0	-5.3	15.1
9YR CAGR (%)										17.4
EBIT	2,237	2,669	3,480	6,378	8,842	10,572	10,970	11,296	8,968	10,450
Margin (%)	7.3	6.8	7.3	9.8	10.0	10.4	10.0	9.5	8.0	8.1
9YR CAGR (%)										18.7
PAT	1,476	1,639	2,513	4,331	6,014	7,254	7,349	8,163	6,894	6,973
YoY Change (%)	47.8	11.1	53.3	72.4	38.8	20.6	1.3	11.1	-15.5	1.1
9YR CAGR (%)										18.8
ROE	37.7	32.7	39.0	49.0	48.2	42.3	32.7	29.1	21.0	18.0
ROCE	36.2	38.7	45.5	65.3	66.1	59.4	40.3	33.8	25.7	28.4
D/E	0.6	0.4	0.2	0.1	0.0	0.0	0.2	0.2	0.0	0.0
Capital Employed	6,557	7,244	8,049	11,492	15,261	20,350	34,036	32,741	37,120	42,324
Cash Flow - FCO	1,077	1,652	3,416	10,533	1,626	5,530	-5,547	5,026	5,803	17,509
Cash Flow - FCF	561	987	2,990	9,890	164	3,880	-7,659	2,956	3,273	14,524
Trailing P/E	1.7	22.1	34.0	40.8	35.2	32.8	33.1	44.9	46.3	NA

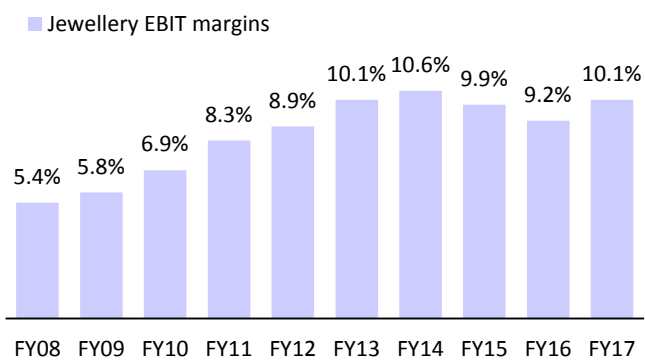
Source: Capital line, MOSL

Exhibit 20: Jewelry volume growth suffered in last couple of years due to demand challenges

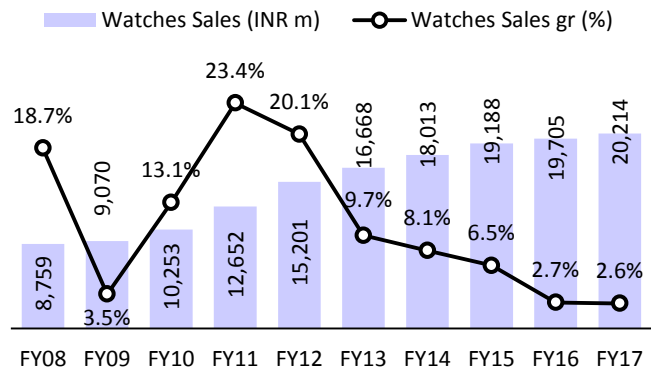
Source: Company, MOSL

Exhibit 21: Company aiming for 2.5x growth in Jewelry by 2022

Source: Company, MOSL

Exhibit 22: Growth might come at the expense of margins, as it will be primarily driven by the lower-margin Wedding Jewelry segment

Source: Company, MOSL

Exhibit 23: Watches segment has been adversely impacted by changing consumer preference

Source: Company, MOSL



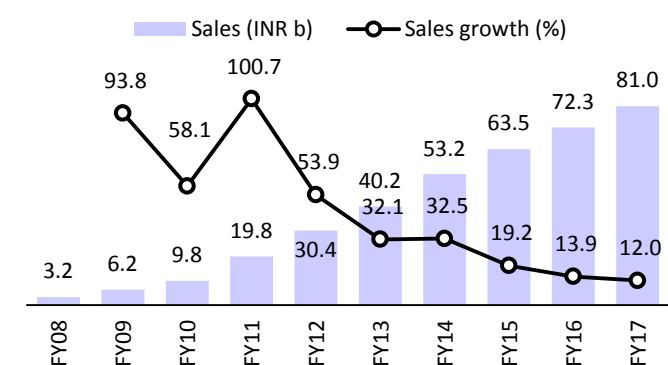
PC Jeweller: 2nd largest listed jewelry retailer in India

- PCJL is the second-largest listed Jewelry Retailer in India. It manufactures, retails and exports Jewelry. It began operations in 2005, with one showroom in Karol Bagh (New Delhi), and now has 71 showrooms (60 own large format + 7 own small format + 4 franchisee), with operational retail space of ~380ksf. PCJL has strong presence in the metros and tier-I cities, with large format stores focused on Wedding Jewelry.
- Having created a favorable brand image as a wedding jewelry player in the metros and tier-I cities, PCJL now aims to tap newer micro markets with small format (limited capital) and franchisee (asset-light model) stores with an area of 1-2ksf. It aims to open 10 franchisee stores and 15 own stores in FY18.
- It is expanding its portfolio by introducing different ranges of Jewelry like *Flexia* and *Azva*. PCJL aims to take *Azva* to 50 retailers by FY18 (25 currently). High-end Diamond Jewelry is currently not available in many store chains; PCJL's will leverage *Azva* brand to target customers of high-end Diamond Jewelry. Besides *Flexia* (Detachable Jewelry) and *Azva*, it has collections such as *Shakuntalam* and *Inayat*. PCJL is also in the process of launching Smart Jewelry in FY18.
- While PCJL outsources 30-35% of its production, it has four manufacturing facilities to support its retail footprint. It has already expanded its manufacturing capacity by 29% to 107ksf and is looking to add further capacity over next two years, with an investment of ~INR3b through internal accruals.
- PCJL is also targeting reduction in overall inventory through technology and digitization, whereby designs available at any of its stores can be seen sitting at one store. It has invested INR0.1b in developing virtual reality technology, which is currently on trial run; the management believes it could be a big hit.
- In exports (~35% of total sales), PCJL is exploring newer markets and is looking at starting B2C (retail) sales of its *Azva* and *Flexia* range of products in the US, UK, and South East Asian and Gulf countries.

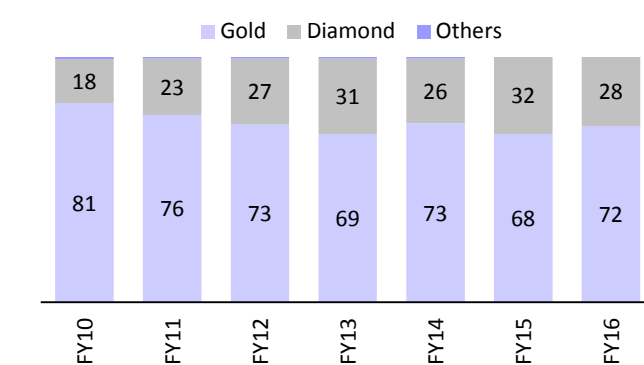
Exhibit 24: PC Jeweller (INR m): Financials snapshot

PC Jeweller	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17
Sales	3,213	6,227	9,849	19,771	30,419	40,184	53,248	63,613	73,302	84,744
YoY Change (%)	-	93.8	58.2	100.7	53.9	32.1	32.5	19.5	15.2	15.6
9YR CAGR (%)										43.8
EBIT	239	555	1,148	2,127	3,419	4,924	6,227	7,664	7,576	7,355
Margin (%)	7.5	8.9	11.7	10.8	11.2	12.3	11.7	12.0	10.3	8.7
9YR CAGR (%)										46.3
PAT	130	310	665	1,449	2,309	2,910	3,563	3,784	3,997	4,210
YoY Change (%)	-	138.9	114.5	118.0	59.4	26.0	22.4	6.2	5.6	5.3
9YR CAGR (%)										47.2
ROE	26.4	30.5	45.1	60.7	30.1	35.7	28.9	28.6	25.4	14.6
ROCE	36.5	68.8	64.3	60.7	41.6	29.9	23.2	20.6	18.5	22.5
D/E	1.6	3.0	1.5	0.5	1.0	0.4	0.4	0.5	0.4	0.2
Capital Employed	906	2,731	2,358	4,655	11,343	16,231	26,882	26,753	33,011	40,436
Cash Flow - FCO	4	-1,419	1,701	-293	-3,366	5,200	-7,859	3,327	156	NA
Cash Flow - FCF	-43	-1,467	1,529	-434	-3,863	4,965	-8,139	3,039	121	NA
Trailing P/E						7.1	5.0	15.5	16.9	NA

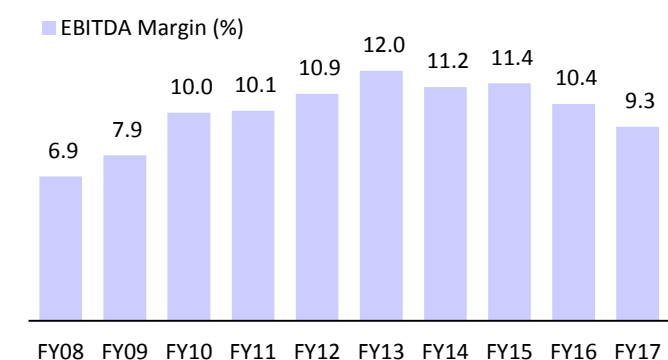
Source: Capital line, MOSL

Exhibit 25: Sales have grown at 22% CAGR since IPO (FY12-17)...

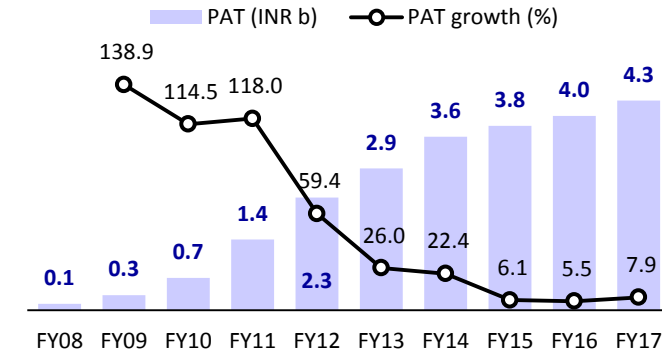
Source: Company, MOSL

Exhibit 26: ...with salience of diamond increasing year by year

Source: Company, MOSL

Exhibit 27: EBITDA margin declining lately

Source: Company, MOSL

Exhibit 28: Adjusted PAT has grown at 13% CAGR over FY12-17

Source: Company, MOSL



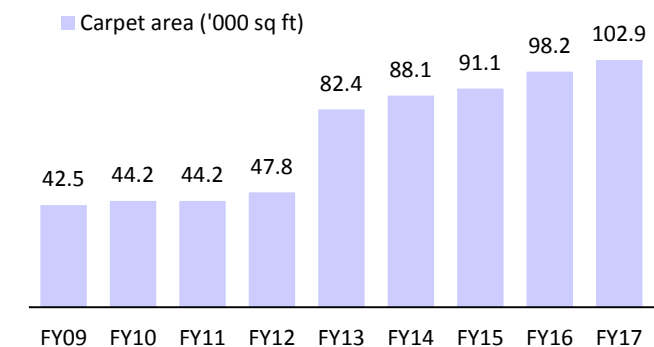
TBZ: A 150-year old brand

- TBZL, a 150-year old brand, is transforming itself into a national Jewelry Retailer, with 33 showrooms in 26 cities across 11 states and a carpet area of 108,948sf.
- TBZL mainly sells Gold and Diamond Jewelry. Wedding and related Jewelry contributes ~65% of its revenue.
- TBZL has its own manufacturing facility in Mumbai, with an annual Gold Refining capacity of >4,000kg, Gold Jewelry Components capacity of 4,500kg, and Diamond Jewelry capacity of >100,000cts. Most of the production is done in-house and a small portion is procured from recognized vendors and suppliers.
- In addition to Jewelry designs from different parts of India, TBZL also offers a wide range of Jewelry from Italy and Turkey.
- Of the 33 showrooms it operates, 28 are large format stores, with a carpet area of over 2,000sf, while five are small format stores, with an area of 1,000-2,000sf.
- TBZL has set up strong systems and processes, with oracle inventory management and a team of 43 designers (including 21 CAD), to maintain its competitive edge.

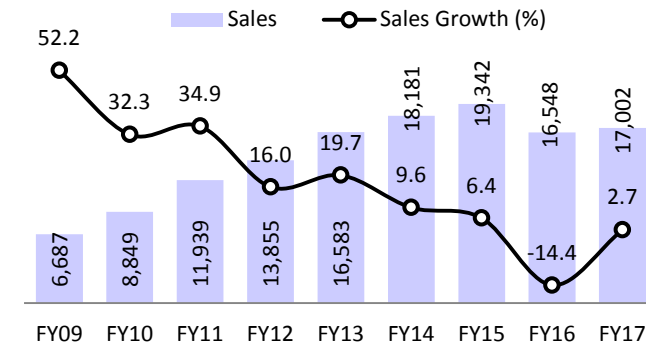
Exhibit 29: TBZ (INR m): Financials snapshot

TBZ	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17
Sales	4,394	6,687	8,849	11,939	13,855	16,583	18,243	19,342	16,548	17,002
YoY Change (%)		52.2	32.3	34.9	16.0	19.7	10.0	6.0	-14.4	2.7
9YR CAGR (%)										16.2
EBIT	222	293	444	849	1,197	1,486	1,344	946	355	605
Margin (%)	5.1	4.4	5.0	7.1	8.6	9.0	7.4	4.9	2.1	3.6
9YR CAGR (%)										11.8
PAT	75	104	169	392	572	845	550	243	-275	147
YoY Change (%)		39.1	62.2	131.6	46.1	47.5	-34.9	-55.8	-213.2	-153.5
9YR CAGR (%)										NA
ROE	408.3	78.8	24.7	44.6	42.8	29.6	12.8	4.0	-6.1	3.3
ROCE	184.7	36.2	59.0	43.2	34.7	24.6	14.5	8.2	3.3	6.0
D/E	0.2	0.2	0.1	1.2	1.6	1.1	1.2	1.3	1.4	1.2
Capital Employed	82	661	752	3,175	3,719	8,359	10,217	10,596	10,960	9,983
Cash Flow - FCO	-83	-529	95	285	385	-3,026	-302	148	141	NA
Cash Flow - FCF	-206	-750	-6	184	316	-3,485	-490	22	45	NA
Trailing P/E						18.7	16.7	43.5	0.0	NA

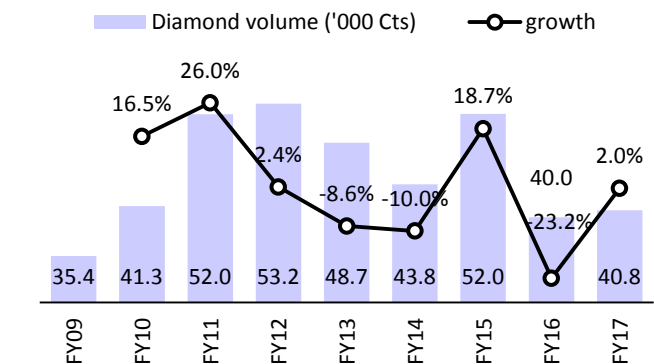
Source: Capital line, MOSL

Exhibit 30: Targeting area of 150,000sf over the near term

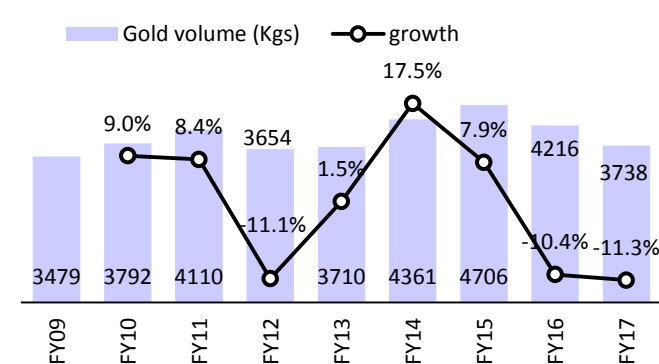
Source: Company, MOSL

Exhibit 31: Sales have slowed in the last few years, like peers

Source: Company, MOSL

Exhibit 32: Diamond forms 22% of total sales (FY17)...

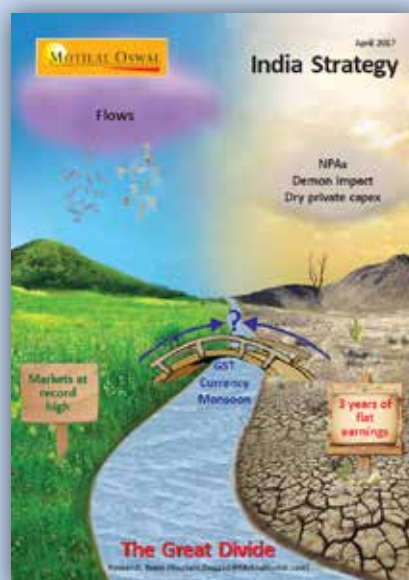
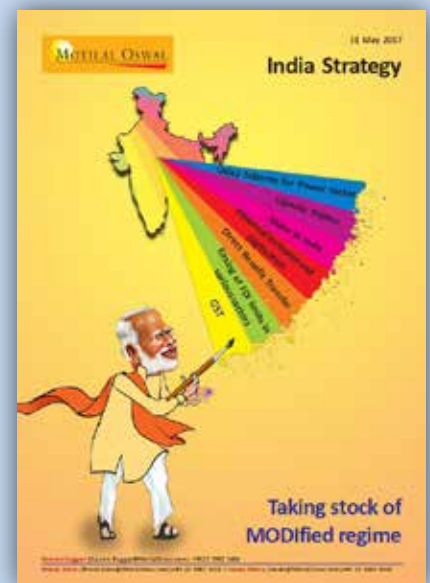
Source: Company, MOSL

Exhibit 33: ...while Gold forms 76%

Source: Company, MOSL

NOTES

THEMATIC/STRATEGY RESEARCH GALLERY



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