

Titan Company

BSE SENSEX
36,134

S&P CNX
10,870

CMP: INR926

TP: INR1,105 (+19%)

Buy



Stock Info

Bloomberg	TTAN IN
Equity Shares (m)	888
M.Cap.(INRb)/(USD\$b)	822.4 / 11.7
52-Week Range (INR)	1006 / 732
1, 6, 12 Rel. Per (%)	3/0/5
12M Avg Val (INR M)	2521
Free float (%)	47.1

Financials Snapshot (INR b)

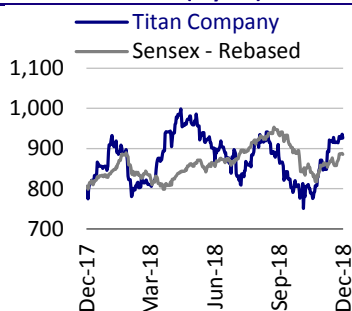
Y/E Mar	2018	2019E	2020E
Sales	161.2	191.3	229.3
EBITDA	16.4	20.3	25.6
Adj. PAT	11.2	13.8	17.5
Adj. EPS (INR)	12.6	15.5	19.7
EPS Gr. (%)	39.9	22.7	27.3
BV/Sh.(INR)	57.3	57.2	66.1
RoE (%)	24.0	27.1	32.0
RoCE (%)	24.7	27.7	32.7
P/E (x)	73.6	59.9	47.1
P/BV (x)	16.2	16.2	14.1

Shareholding pattern (%)

As On	Sep-18	Jun-18	Sep-17
Promoter	52.9	52.9	52.9
DII	7.8	6.6	5.6
FII	19.5	20.5	21.7
Others	19.8	20.0	19.8

FII Includes depository receipts

Stock Performance (1-year)



Wedding season demand healthy

Own initiatives strengthening the reforms-led tailwinds

We recently met Titan Company's (TTAN) management to take a stock of the company's underlying story and the efforts that it is undertaking to grow amid a favorable operating environment for organized players. Key takeaways.

- In an encouraging sign, wedding season demand is scaling up well for TTAN. This should uplift management confidence as it had guided for healthy growth (25-30%) for 3QFY19 but refrained from commenting on the fourth quarter performance. In our view, if consumers continue flocking to its stores in the wedding season, Jewelry sales growth of 25% for the full year is achievable (note that TTAN had guided for Jewelry sales growth of 25% at the start of the year but lowered it to ~20% later).
- SSSG is likely to contribute 75-80% of Jewelry sales growth, which is even higher than the impressive 60% that it was reporting earlier. This, in turn, would have extremely positive implications on Jewelry EBIT margin.
- Sustained growth in the Watches segment (where visibility is high for the near term, but somewhat unclear for the longer term) can prove beneficial, as EBIT margin in this segment is 300-400bp higher than that in Jewelry.
- Jewelry business growth prospects remain robust, and now Watches and even Eyewear segments have raised their hands to contribute to growth. We believe that premium valuations are fully deserved for a business that has perhaps the best revenue growth potential in the large cap FMCG/retail space (20% CAGR in Jewelry business over the next five years) and also operating leverage-led margins support. We maintain our Buy rating on the stock with a target price of INR1,105, based on 47x Dec'20 EPS (~10% premium to three-year average P/E).

Jewelry: Taking initiatives for more glitter

- Six factors are driving growth in Jewelry segment: (1) high-value studded jewelry growth, (2) increase in the share of wedding jewelry, (3) gold exchange, (4) golden harvest, (5) efforts to grow in cities where it is weak and (6) the target to increase the number of stores from 267 stores in 150 towns now to 400 stores in 250 towns in the next few years. Management believes that all of these measures have started yielding results and contributing nearly two thirds of 20-25% growth that it is recording in Jewelry. Tightening of measures to stop illegal trade over the past few years, GST implementation, and credit squeeze faced by other players due to various scams have also helped but to a smaller extent, according to management.
- In FY18, the gold exchange scheme contributed 40% of Jewelry sales, while the gold harvest scheme accounted for 18%. Growth targets for studded jewelry are also being met.
- The company aims to focus more on wedding jewelry now, setting a target to increase its contribution to 50% of Jewelry sales from 30% now. Wedding jewelry segment has turned more attractive now as stricter compliance norms is taking away the edge that unorganized players had earlier. Design element is also becoming important for buyers.

➤ **Reasons why wedding jewelry was not a focus area earlier?**

- a) Tanishq was design and purity focused, and thus, products were sold at a significant premium
- b) Involved large deals, where bargains were sought
- c) Low compliance among peers; they could thus offer discounts
- d) Involved plain gold, and thus, relatively low margins

■ **Other points on Jewelry business**

- Average ticket size in Jewelry has increased to INR80,000 from INR65,000 a few years ago.
- Management recently guided for 25-30% growth in 3QFY19 but was reluctant to call out strong growth for 4QFY19. However, TTAN can achieve 25% growth in Jewelry this year, especially if wedding demand sustains (we are assuming 18% growth in our forecasts).
- SSSG is likely to contribute 75-80% of Jewelry sales (as against 60% stated earlier). This should significantly benefit segmental EBIT margin.
- The focus on *Mia* and *Caratlane* brands stems from the increasing trend toward lower-value accessories among women.
- Jewelry stores are classified into: (1) L1 stores: Operated and owned by the company, inventory on the books of the company and opex borne by the company. (2) L2 stores: Operated and owned by management agent, inventory on the books of the company and opex borne by management agent and (3) L3 stores: Store operated and owned by the franchisee, inventory on the books of the franchisee and opex too borne by the franchisee. Each of them has an equal one third share in overall store count. Investment for a 3,000sq.ft store is INR120m and average store size is 6,000 sq. ft. Stores are expected to become profitable in three years.
- For the calculation of SSSG, retail sales of stores are calculated by taking the stores present in the base quarter as well.
- For the company's Jewelry business, plain gold jewelry above 75gm is treated as wedding jewelry.
- Gold procurement: 50% of inventory is gold on exchange, 40% is gold on lease and the balance 10% is bought at the spot rate. Cost of gold on lease is 2%.

Watches: Time is good, but sustenance is key

- Reasons for Watches segment resurgence (management unclear as to whether it will sustain):
- a) The company can be offering better products, designs and variants at good price points (INR2,000-4,000).
- b) TTAN earlier had stayed away from online channel because of discounting and to avoid potential harm to the brand. However, it is now able to sell without offering discounts. The company now derives 10% of revenues from the online channel, primarily in the last 15 months. Profitability is good for both TTAN and online retailers.
- c) Share of gifting was smaller earlier. However, the company now has good products; it is also doing well on advertising.
- d) Smart watches now contribute 10% of sales.

- *Titan* brand has the highest gross margin in Watches compared to the other brands of the company. *Titan* is the biggest, followed by *Fastrack* and *Sonata*.
- *Fastrack* fitness tracker is gaining good traction.
- Management believes that there is a need to get smarter, e.g. analog watches with connectivity. The company is no. 2 in wearables already.

Eyewear: New strategy of lower ASP working well

- The changed strategy of moving from higher ASP to lower ASP is working well.
- E-commerce now contributes 10% of Eyewear sales.
- *Fastrack* segment now accounts for 15% of Eyewear.
- 85% of lenses are manufactured by *Titan* itself. It is also investing in lens labs (5-6 now) that are closer to customers.

Other key points

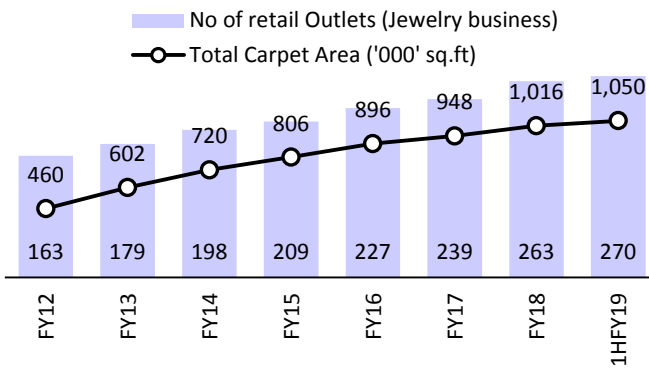
- There is increasing confidence among various business teams of the company because of performance delivery.
- Agility, adaptability and innovation have picked up sharply over the past 30 months.
- Cost escalations are likely – staff costs increasing by 10%, rentals by 5% and other expenses by 4-5%. Thus, any fall in SSSG below 10% might hurt margins.
- *Skinn* is now an INR1b brand.

Exhibit 1: Recent promotional activity



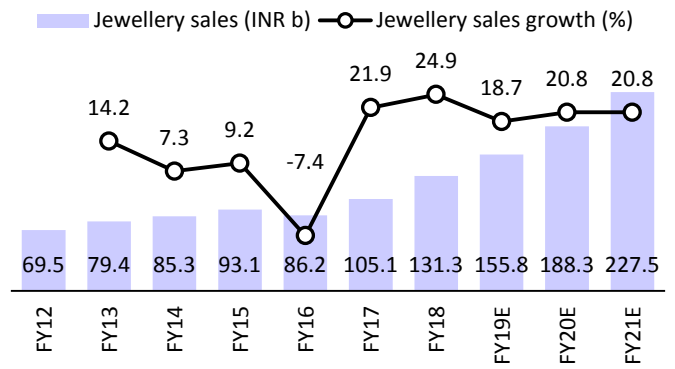
Source: Company, MOSL

Exhibit 2: Jewelry store expansion to stay strong



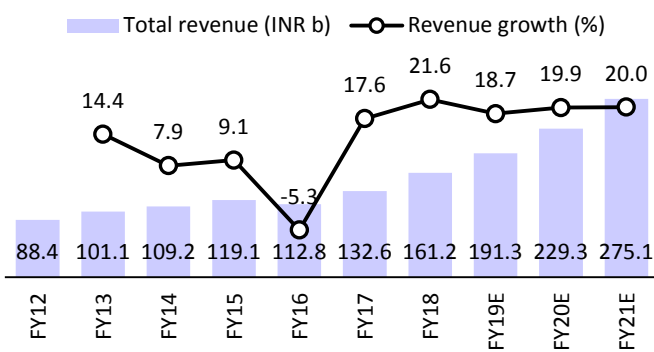
Source: Company, MOSL

Exhibit 3: Expect Jewelry sales CAGR of 20% over FY18-21



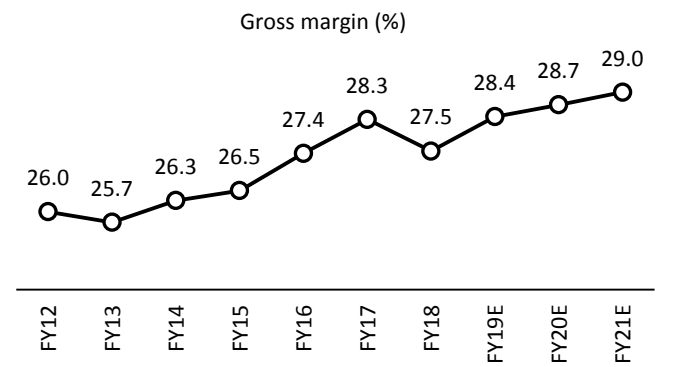
Source: Company, MOSL

Exhibit 4: Expect overall sales CAGR (FY18-21) of ~19.5%



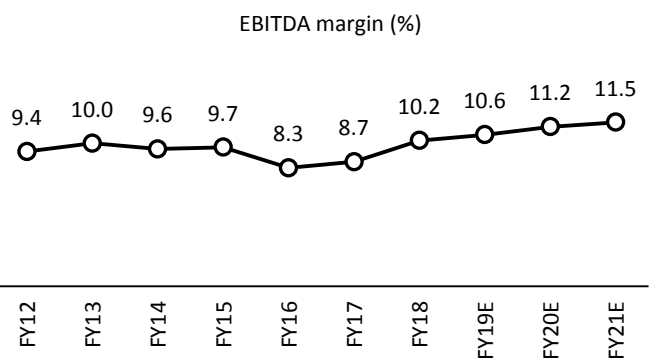
Source: Company, MOSL

Exhibit 5: Gross margin to expand 150bp over FY18-21



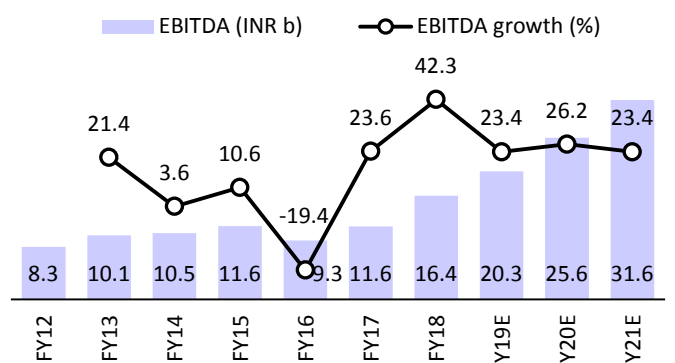
Source: Company, MOSL

Exhibit 6: EBITDA margins to expand 130bp YoY over FY18-21



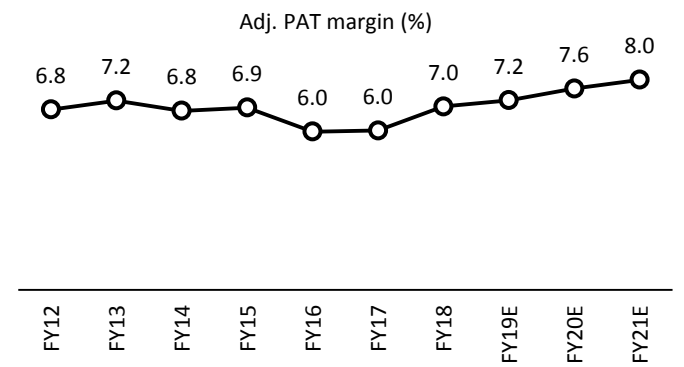
Source: Company, MOSL

Exhibit 7: Expect EBITDA CAGR of 24.3% over FY18-21



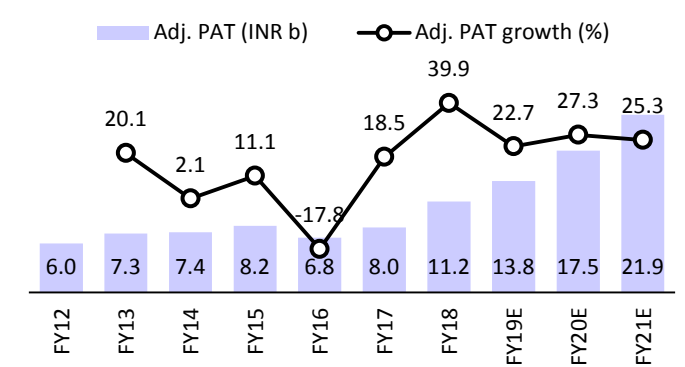
Source: Company, MOSL

Exhibit 8: Adj. PAT margins to reach 8% by FY21



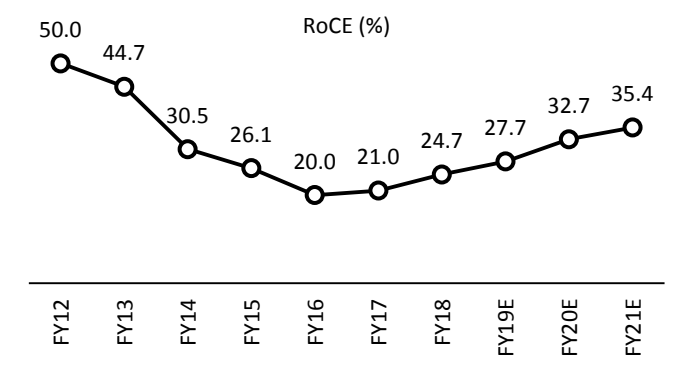
Source: Company, MOSL

Exhibit 9: Expect adj. PAT CAGR of 25.1% over FY18-21



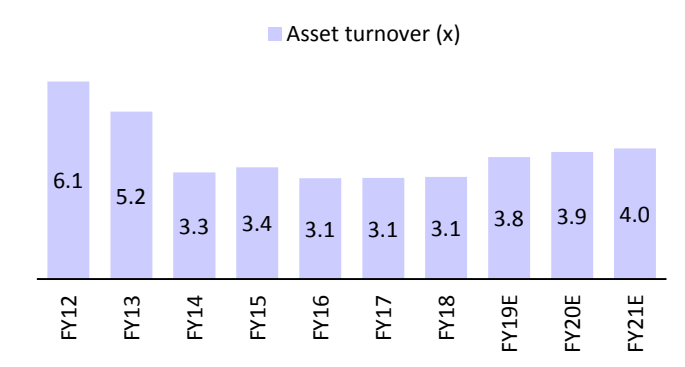
Source: Company, MOSL

Exhibit 10: Return on capital employed to improve to ~35% by FY21...



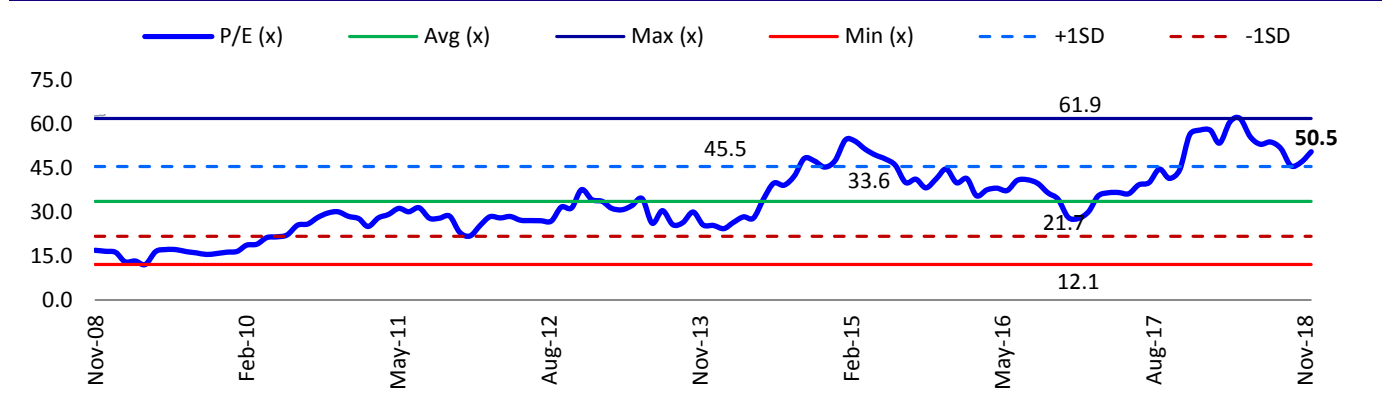
Source: Company, MOSL

Exhibit 11: ...with improvement in asset turns



Source: Company, MOSL

Exhibit 12: P/E (x)



Source: Company, MOSL

Financials and valuations

Income Statement							(INR M)
Y/E March	2015	2016	2017	2018	2019E	2020E	2021E
Net Sales	119,095	112,759	132,608	161,198	191,264	229,330	275,136
Change (%)	9.1	-5.3	17.6	21.6	18.7	19.9	20.0
Gross Profit	31,562	30,949	37,534	44,336	54,269	65,758	79,774
Margin (%)	26.5	27.4	28.3	27.5	28.4	28.7	29.0
Other expenditure	19,962	21,601	25,979	27,889	33,976	40,152	48,178
EBITDA	11,599	9,347	11,555	16,447	20,293	25,606	31,596
Change (%)	10.6	-19.4	23.6	42.3	23.4	26.2	23.4
Margin (%)	9.7	8.3	8.7	10.2	10.6	11.2	11.5
Depreciation	874	982	1,105	1,314	1,705	1,903	2,142
Int. and Fin. Charges	807	424	377	529	539	562	745
Other Income - Recurring	643	739	705	889	1,063	1,179	1,756
Profit before Taxes	10,562	8,681	10,777	15,492	19,111	24,321	30,465
Change (%)	4.0	-17.8	24.1	43.7	23.4	27.3	25.3
Tax	2,410	1,710	3,021	4,500	5,351	6,810	8,530
Deferred Tax	82	-206	261	221	0	0	0
Tax Rate (%)	22.0	22.1	25.6	27.6	28.0	28.0	28.0
Profit after Taxes	8,233	6,765	8,018	11,213	13,760	17,511	21,935
Change (%)	11.1	-17.8	18.5	39.9	22.7	27.3	25.3
Margin (%)	6.9	6.0	6.0	7.0	7.2	7.6	8.0
Extraordinary income	0	0	-1,027	-167	0	0	0
Reported PAT	8,233	6,765	6,991	11,047	13,760	17,511	21,935

Balance Sheet							(INR M)
Y/E March	2015	2016	2017	2018	2019E	2020E	2021E
Share Capital	888	888	888	888	888	888	888
Reserves	32,637	34,178	41,700	49,993	49,872	57,752	67,623
Net Worth	33,525	35,066	42,587	50,881	50,760	58,640	68,511
Loans	998	1,131	0	790	500	250	250
Deferred Tax	64	131	-33	-329	-329	-329	-329
Capital Employed	34,587	36,327	42,555	51,342	50,931	58,561	68,432
Gross Block	11,824	13,559	9,858	13,384	15,509	17,584	19,659
Less: Accum. Depn.	5,103	6,054	1,220	2,137	3,842	5,745	7,886
Net Fixed Assets	6,720	7,506	8,638	11,247	11,667	11,840	11,773
Intangibles	102	200	3,337	3,495	3,495	3,495	3,495
Capital WIP	552	1,067	1,432	430	430	430	430
Investments	290	26	3,937	16	16	16	16
Curr. Assets, L&A	50,932	54,624	66,698	79,694	92,797	106,016	132,940
Inventory	40,493	44,472	49,257	59,248	67,191	77,871	92,177
Account Receivables	1,897	1,925	2,076	2,957	3,039	4,084	4,900
Cash and Bank Balance	2,138	1,442	8,159	6,523	9,957	9,560	19,186
Others	6,403	6,785	7,205	10,965	12,610	14,502	16,677
Curr. Liab. and Prov.	24,010	27,095	41,488	43,540	57,474	63,236	80,222
Current Liabilities	22,943	25,794	40,056	41,909	56,064	61,825	78,812
Provisions	1,067	1,302	1,433	1,631	1,411	1,411	1,411
Net Current Assets	26,922	27,529	25,210	36,154	35,323	42,781	52,717
Application of Funds	34,587	36,327	42,555	51,342	50,931	58,561	68,431

E: MOSL Estimates

Financials and valuations

Ratios

Y/E March	2015	2016	2017	2018	2019E	2020E	2021E
Basic (INR)							
EPS	9.3	7.6	9.0	12.6	15.5	19.7	24.7
Cash EPS	10.3	8.7	10.2	14.0	17.4	21.9	27.1
BV/Share	37.8	39.5	48.0	57.3	57.2	66.1	77.2
DPS	2.8	5.4	3.6	4.6	7.7	10.8	13.6
Payout %	29.8	70.3	39.7	36.3	50.0	55.0	55.0

Valuation (x)

P/E	100.2	121.9	102.9	73.6	59.9	47.1	37.6
Cash P/E	90.6	106.9	90.8	66.3	53.3	42.5	34.3
EV/Sales	6.9	7.3	6.1	5.1	4.3	3.6	2.9
EV/EBITDA	71.0	88.2	70.3	49.8	40.2	31.8	25.5
P/BV	24.6	23.5	19.4	16.2	16.2	14.1	12.0
Dividend Yield (%)	0.3	0.6	0.4	0.5	0.8	1.2	1.5

Return Ratios (%)

RoE	28.0	19.7	20.6	24.0	27.1	32.0	34.5
RoCE	26.1	20.0	21.0	24.7	27.7	32.7	35.4
RoIC	30.2	19.9	24.8	29.8	31.5	38.3	43.6

Working Capital Ratios

Debtor (Days)	6	6	6	7	6	7	7
Asset Turnover (x)	3.4	3.1	3.1	3.1	3.8	3.9	4.0

Leverage Ratio

Debt/Equity (x)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
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Cash Flow Statement

Y/E March	2015	2016	2017	2018	2019E	2020E	2021E
(INR M)							
OP/(loss) before Tax	10,489	8,681	9,733	15,298	19,111	24,321	30,465
Int./Div. Received	77	-95	31	-81	-1,063	-1,179	-1,756
Depreciation & Amort.	896	982	1,105	1,314	1,705	1,903	2,142
Interest Paid	165	-152	-136	-113	539	562	745
Direct Taxes Paid	2,449	2,025	2,768	4,561	5,351	6,810	8,530
Incr in WC	4,152	1,631	-9,158	12,365	-4,265	7,855	311
CF from Operations	5,026	5,761	17,123	-507	19,206	10,942	22,755
Incr in FA	2,070	2,522	2,511	2,993	2,125	2,075	2,075
Free Cash Flow	2,956	3,239	14,613	-3,500	17,081	8,867	20,680
Investments	-2	-55	3,254	-4,115	0	0	0
Others	-301	-1,058	2,986	-273	8,804	947	-198
CF from Invest.	-1,767	-1,409	-8,750	1,395	-10,929	-3,022	-1,877
Incr in Debt	0	0	0	0	-290	-250	0
Dividend Paid	1,852	3,944	36	2,774	4,014	7,506	10,507
Others	8,194	1,104	1,621	-249	539	562	745
CF from Fin. Activity	-10,047	-5,048	-1,656	-2,524	-4,843	-8,317	-11,252
Incr/Decr of Cash	-6,787	-696	6,717	-1,637	3,434	-398	9,626
Add: Opening Balance	8,926	2,138	1,442	8,159	6,523	9,957	9,559
Closing Balance	2,138	1,442	8,159	6,523	9,957	9,559	19,185

E: MOSL Estimates

NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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