Sharekhan
by BNP PARIBAS

Relaxo Footwears

On a stable footing

Sector: Consumer Discretionary
Result Update

	Change
Reco: **Buy**	↔
CMP: **Rs. 721**	
Price Target: **Rs. 825**	↑

↑ Upgrade ↔ No change ↓ Downgrade

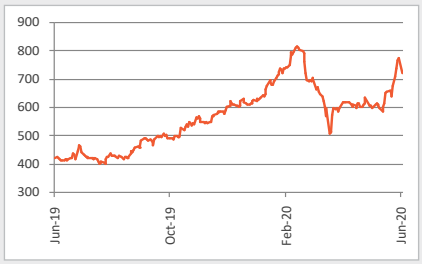
Company details

Market cap:	Rs. 17,899 cr
52-week high/low:	Rs. 830/389
NSE volume: (No of shares)	1.8 lakh
BSE code:	530517
NSE code:	RELAXO
Sharekhan code:	RELAXO
Free float: (No of shares)	7.2 cr

Shareholding (%)

Promoters	71.0
FII	3.0
DII	6.4
Others	19.7

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	19.4	8.7	18.4	68.5
Relative to Sensex	10.7	12.3	33.5	82.1

Sharekhan Research, Bloomberg

Relaxo Footwears Limited (Relaxo) posted mixed numbers in Q4FY2020 with revenues declining by 15% y-o-y (affected by lockdown) but higher gross margins leading to a 282 bps rise in reported OPM to 17.8% (comparable OPM improved by ~70 bps to 15.7%). FY2020 revenues grew by 5.2%y-o-y affected by lockdown in the fag end of Q4FY2020 (9MFY2020 revenue grew by 12.9%). Volumes declined by 2.7% in FY2020 affected by a lockdown in the last 10-15 days of March and higher sales of premium products (~20% of overall revenues). Q1FY2021 performance would be affected by no sales during the lockdown period. Gradual opening of lockdown would help in recovery in the footwear demand. Post the relaxation of lockdown norms, ~50% of the domestic market has opened up for the company. The capacity utilisation currently stands at ~70%. Demand for Relaxo Hawaii chappals (~40% of Relaxo's sales volumes) have started picking up. The company expects other segments to recover gradually post steady opening of key markets. Though FY2021 is expected to be subdued, we expect a strong recovery in FY2022. Some of the medium to long-term growth drivers are lesser penetration in the southern market, lower per-capita consumption in India at 1.66 pairs per annum compared to other developing countries at 6-7 pairs per annum and lower global export contribution at ~4%. Benign input prices would support overall margins in FY2021 while higher sales realisation due to good traction to premium products would help margin expansion to sustain in FY2022.

Key positives

- Revenue grew in double digits in 75-80 days of Q4 with volume growth of mid-single digit.
- Benign input prices and higher contribution from premium products aided Relaxo's gross margins to expand by 661 bps in Q4 and 367 bps in FY2020.
- Rural India is doing much better than urban India as pick-up in demand was faster due to opening up of the markets.

Key negatives

- Lockdown at fag-end of Q4 led to 15% decline in revenues.
- Volumes declined by 2.5% in FY2020

Our Call

View - Retained Buy with revised PT of Rs. 825: We have lowered our earnings estimates by 7% and 3%, respectively for FY2021 and FY2022 to factor in the impact of supply disruption caused by the lockdown. Once the pandemic situation eases, we expect faster recovery in Relaxo's operating performance on the back of its strong product portfolio (straddling the pyramid) and expansion of distribution reach. Further, strong cash flows and de-leveraged balance sheet (reduced debt by Rs. 110 crore; debt to equity stands at 0.02x) would help it to stay ahead of competition (especially from smaller unorganised players). Hence, despite recent run-up in the stock price, Relaxo remains a must have stock in the portfolio in view of long-term earnings visibility. We maintain our Buy recommendation on the stock with a revised price target of Rs. 825.

Key Risks

Any slowdown in recovery in sales or a spike in key input prices would act as a key risk to our earnings estimates in the near term.

Valuation (Standalone) Rs cr

Particulars	FY18	FY19	FY20	FY21E	FY22E
Revenues	1,949	2,292	2,410	2,335	3,045
OPM (%)	15.5	14.1	17.0	17.3	18.9
Adjusted PAT	161	175	226	219	341
% YoY growth	34.3	8.9	29.0	-3.1	55.6
Adjusted diluted EPS (Rs.)	6.5	7.1	9.1	8.8	13.8
P/E (x)	-	-	79.1	81.6	52.4
P/B (x)	23.5	16.2	14.1	12.4	10.4
EV/EBIDTA (x)	59.6	55.4	44.2	44.5	30.9
RoNW (%)	23.6	18.8	19.0	16.1	21.5
RoCE (%)	34.6	23.8	27.4	22.2	30.6

Source: Company; Sharekhan estimates
**we have included the impact of Ind AS 116 in FY2021 and FY2022 estimates*

Revenue declined by 15% y-o-y, soft input costs and premiumisation drive up margins: Revenue declined by 15% y-o-y to Rs. 540.6 crore adversely affected by store closures due to nationwide lockdown in the last few days of March 2020. However, the company registered double-digit growth in the January to March 15, 2020 period. Gross margins increased by 661 bps y-o-y to 59.8%, largely on account of benign raw material costs and premiumisation. This, along with operating efficiencies and Ind-AS 116 led reported OPM to expand by 282 bps to 17.8%. Comparable OPM increased by ~70 bps to 15.7%. Reported operating profit stood almost flat at Rs. 96.2 crore. Post Ind-AS 116, reported depreciation and finance costs rose significantly to Rs. 27.6 crore and 3.5 crore in Q4FY2020, respectively, as against Rs. 16.1 crore and Rs. 1.7 crore in Q4FY2019. This, along with lower revenue caused profit before tax (PBT) to decline by 12.3% y-o-y to Rs. 69 crore. However, lower incidence of tax limited the decline in adjusted PAT to 4.8%, which came in at Rs. 51.8 crore in Q4FY2020 as against Rs. 54.4 crore in Q4FY2019. The net impact of Ind-AS 116 on PBT stood at Rs. 1.5 crore in Q4FY2020.

Higher demand for open slippers as the operations have begun normalising; liquidity position remains stable: Due to the lockdown, Relaxo's manufacturing and sales operations were shut down in last few days of March and April 2020 to comply with government guidelines. Even though the overall demand for products has been impacted, but, due to easing of restrictions, demand for open slippers has improved during the period. However, due to restrictions in manufacturing operations, the company expects the fulfilment of such demand to be a challenge. After easing of the lockdown the company has not faced any inbound supply chain issues, though, outbound supply chain was marginally affected. The company has started operations in six manufacturing plants (at ~70% capacity) till date with reduced restrictions. It is in the process of starting operations in the remaining manufacturing plants. There has been constant improvement in collections and the company is also making regular payments to its vendors. The company does not have any long-term debt on its books and the working capital is stable at 29 days in FY2020. Operating cash flows increased from Rs. 209.7 crore in FY2019 to Rs. 402 crore in FY2020. The company's liquidity is comfortable to meet near-term obligations.

Enough headroom for growth in the Indian footwear industry: India is the second-largest footwear producer after China accounting for ~9% of the overall market of ~22 billion pairs. India exports only 10% of the current production whereas ~90% is sold in the domestic markets. The Indian footwear industry is expected to reach ~Rs. 1 lakh crore by 2021. Per capita footwear consumption in India stands at just ~1.66 pairs per annum as compared to global average of ~3 pairs per annum and developed countries' consumption of 6-7 pairs per annum, which provides huge scope for growth in the Indian footwear industry. Moreover, consumer buying behaviour is changing rapidly due to urbanisation, higher penetration of internet and growing awareness/ consciousness about trends, which has made footwear turn into a fashion accessory than a necessity. Consistent efforts by the government such as hike in customs duty on imported footwear, special package of Rs. 2,600 crore for the upliftment of the industry and GST will help the organised footwear industry to report strong growth in the medium to long term.

Other conference call highlights:

- Volumes declined by 2.7% in FY2020 due to the lockdown and unfavourable product mix (higher sale of premium products). Realisation growth stood at ~8%, which was driven by higher salience of the premium part of the portfolio as well as certain price hikes in the remaining portfolio. The premium segment contributed ~20% to overall revenue, and reported good growth, especially in low-penetration geographies such as the south and the west.
- In terms of channels, exclusive brand outlets (EBOs) contributed ~8% to overall revenue whereas contribution from online channels and exports stood at 7-8% and ~4% of overall revenue, respectively.
- Relaxo Hawaii contributed ~40% to overall volumes in FY2020, the balance being equally contributed by Bahamas and Flite. In terms of value, Relaxo Hawaii contributed ~25% to overall revenue and the balance was equally contributed by Bahamas and Flite. Sports shoes contribute ~5-10% to overall revenue. Premium products contribute ~20% to overall revenues and are growing much faster than value products. Average realisation per pair stood at Rs. 135 per pair for FY2020, which is expected to increase with higher sales of premium products.

- Relaxo's distribution reach stands at 50,000+ retailers served through distributors whereas the direct reach was at about 45,000 outlets in FY2020. The company has 390 EBOs as on FY2020 out of which 47 EBOs were added this year. The company has also added close to 100 distributors in FY2020.
- Post relaxation of the lockdown, the company has started operating at ~70% capacity utilisation and ~50% of the markets (largely north and east) are open for operations. Currently, the company is witnessing higher demand for open footwear and value-added products which contributed about two-thirds to overall revenue. Relaxo's open footwear brands include Hawaii, Bahamas and Flite.
- Polymers such as PU and EV form a major part of the company's raw material. With the raw material prices expected to remain benign in the coming quarters, margins are expected to sustain at current levels. If demand picks up from Q2FY2021, margins are expected to improve y-o-y.
- The company expects to incur capex of Rs. 100 crore for FY2021 on the new plant in Rajasthan and for maintenance purposes.
- Rural demand is picking up faster than the urban demand as rural markets are opening much faster than the urban markets due to easing of lockdown.

Results (Standalone) **Rs cr**

Particulars	Q4FY20	Q4FY19	YoY %	Q3FY20	QoQ %
Net Revenue	540.6	635.7	-15.0	599.8	-9.9
Raw-material cost	217.3	297.5	-27.0	252.9	-14.1
Staff cost	73.9	67.0	10.3	75.6	-2.2
Other expenses	153.2	176.0	-12.9	169.8	-9.8
Total expenses	444.4	540.5	-17.8	498.2	-10.8
Operating profit	96.2	95.2	1.0	101.6	-5.3
Other Income	4.0	1.3	-	2.2	83.9
EBITDA	100.2	96.5	3.8	103.8	-3.5
Interest expenses	3.5	1.7	-	4.4	-20.0
Depreciation & Amortization	27.6	16.1	71.6	27.5	0.6
PBT	69.0	78.7	-12.3	71.9	-4.0
Tax	17.2	24.3	-29.0	17.8	-2.9
Reported PAT	51.8	54.4	-4.8	54.2	-4.4
EPS	2.1	2.2	-4.9	2.2	-4.4
			bps		**bps**
GPM (%)	59.8	53.2	661	57.8	196
OPM (%)	17.8	15.0	282	16.9	86

Source: Company; Sharekhan Research

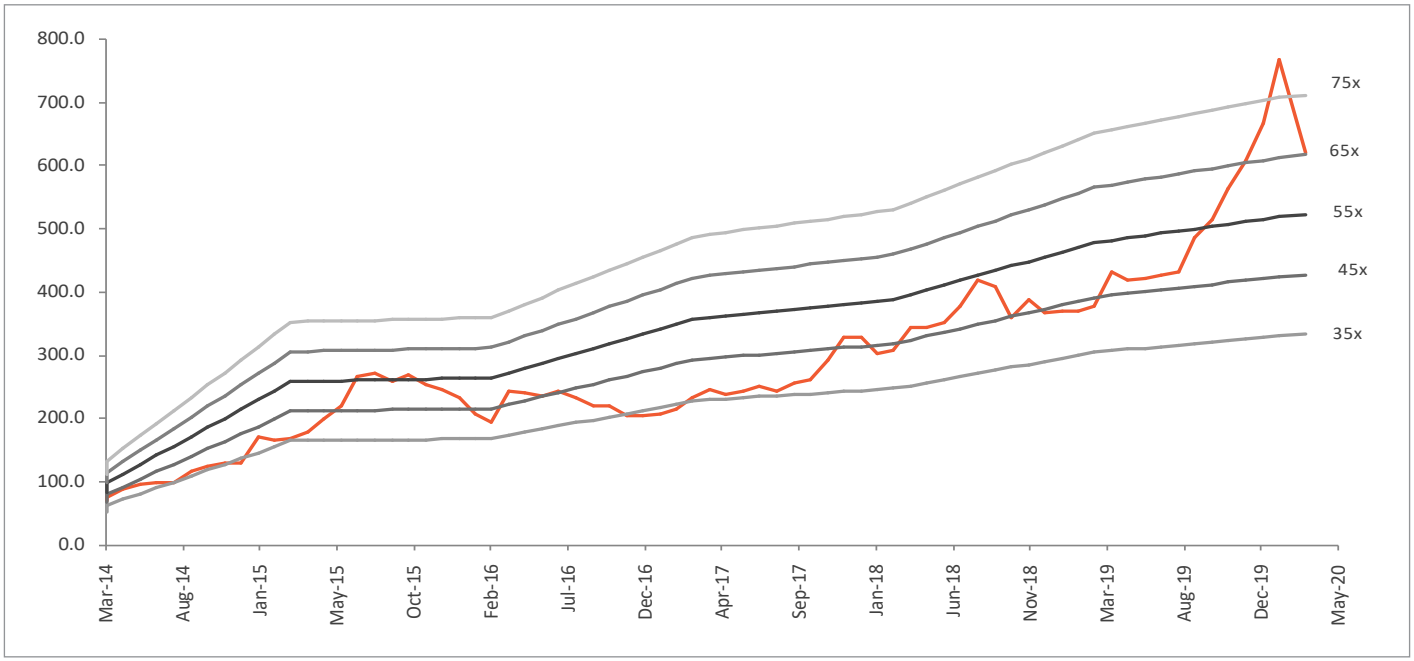
Outlook

FY2021 to be affected by lockdown; long-term growth prospects intact: FY2020 revenues grew by 6.2%y-o-y affected by lockdown in the fag-end of Q4FY2020. Volumes declined by 2.5% in FY2020 affected by lockdown in the last 10-15 days of March and higher sales of premium products (20% of overall revenues). Q1FY2021 performance would be affected by no sales during the lockdown period. The gradual opening of lockdown would help footwear demand to recover. North, East and Central markets have opened up for the company in phase one of unlock. The capacity utilisation currently stands at ~70%. Though FY2021 is expected to be subdued, we expect strong recovery in FY2022. Relaxo's lesser penetration in the southern market, lower per-capita consumption in India at 1.66 pairs per annum as compared to other developing countries at 6-7 pairs per annum. and lower global export contribution at ~4% are some of the key growth levers in the near to medium term. Benign input prices would support overall margins in FY2021 while higher sales realisation due to good traction to premium products would help margin expansion to sustain in FY2022.

Valuation

Retained Buy with revised PT of Rs. 825: We have lowered our earnings estimates by 7% and 3%, respectively for FY2021 and FY2022 to factor in the impact of supply disruption caused by the lockdown. Once the pandemic situation eases, we expect faster recovery in Relaxo's operating performance on the back of its strong product portfolio (straddling the pyramid) and expansion of distribution reach. Further, strong cash flows and de-leveraged balance sheet (reduced debt by Rs. 110 crore; debt to equity stands at 0.02x) would help it to stay ahead of competition (especially from smaller unorganised players). Hence, despite recent run-up in the stock price, Relaxo remains a must have stock in the portfolio in view of long-term earnings visibility. We maintain our Buy recommendation on the stock with a revised price target of Rs. 825.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

New Delhi-based Relaxo is a leading footwear company with a turnover of over Rs. 2,000 crore. It has eight manufacturing facilities across northern India with a capacity of over 7.5 lakh pairs per day. The company sells close to 180 million pairs per annum through its wide distribution network of over 50,000 retailers, ~700 distributors and 390 exclusive brand outlets (EBOs). Relaxo produces a wide range of footwear under nine brands including Sparx, Bahamas, Flite, Schoolmate and Relaxo Hawaii selling over 10,000 SKUs. Bahamas and Flite cater to the young and fashionable target consumers, while Sparx is marketed with durability as its USP whereas Schoolmate is specifically for school shoes.

Investment theme

Relaxo has clocked sustained double-digit volume growth in the last few quarters. With the implementation of GST, there is a shift from unbranded to branded products, which provides further scope for the company in the Rs. 55,000-60,000 crore Indian footwear market, of which ~50% is unbranded. Capacity expansions, investment on brands, steady volume growth and increasing presence in untapped markets along with increasing price differential in the imported and domestic footwear as a result of a hike in customs duty would be key growth drivers in the near to medium term.

Key Risks

- Slowdown in discretionary demand: Any slowdown in demand would affect revenue growth.
- Increased input costs: Any significant increase in rubber prices or those of crude oil derivatives would affect profitability.
- Increased competition in highly penetrated categories: Heightened competition would threaten revenue growth.

Additional Data

Key management personnel

Ramesh Kumar Dua	Managing Director
Sushil Batra	Chief Financial Officer
Vikas Kumar Tak	Company Secretary

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	VLS Securities Ltd	6.6
2	VL Finance	5.0
3	SBI Funds Management Pvt Ltd	4.0
4	Capital Group Cos Inc	1.5
5	ICICI Prudential Asset Management	0.7
6	DSP Investment Managers Pvt Ltd	0.4
7	Vanguard group	0.4
8	Daiwa Asset Management India Pvt L	0.3
9	Principal Financial Group Inc	0.3
10	Birla Sun Life Insurance Co Ltd	0.2

Source: Bloomberg

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