Sharekhan by BNP PARIBAS

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Stock Update

Bata India Limited

Subdued Q2, recovery ahead

Consumer Discretionary	Sharekhan code: BATAINDIA	Result Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 1,327**	
Price Target: **Rs. 1,550**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

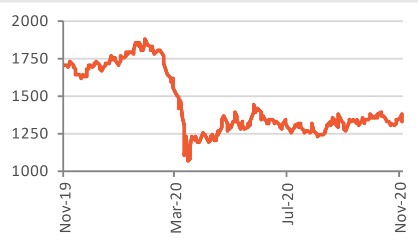
Company details

Market cap:	Rs. 17,061 cr
52-week high/low:	Rs. 1,897 / 1,017
NSE volume: (No of shares)	6.1 lakh
BSE code:	500043
NSE code:	BATAINDIA
Free float: (No of shares)	6.0 cr

Shareholding (%)

Promoters	53.0
FII	4.7
DII	26.4
Others	16.0

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-2.1	8.0	0.5	-22.1
Relative to Sensex	-9.5	-5.6	-37.7	-30.2

Sharekhan Research, Bloomberg

Summary

- Q2FY2021 business recovered to ~50% of pre-COVID levels, improving from just ~15% recovery in Q1FY2021. Higher demand was seen in semi-urban areas, whereas metros remained slower.
- The company is focusing on expanding its presence through the e-commerce/omni-channel and is innovating its product portfolio with relevant products to drive growth in the medium to long term.
- H1FY2021 was subdued and demand in stores will take time to revive. Post-pandemic recovery is likely in H2FY2021 amid festive/wedding season. Strong recovery is expected in FY2022.
- Strong cash position of ~Rs. 800 crore as of H1FY2021 will help meet near-term expansion plans without any disruptions. With strong brand identity, sturdy balance sheet, and good parental backing, we recommend Buy on the stock with a PT of Rs. 1,550.

Bata India's (Bata) Q2FY2021 revenue declined by ~49% y-o-y to Rs. 367.9 crore. Recovery in metros and urban areas was much slower than semi-urban areas, which saw increasing demand. Post the easing of the lockdown, almost all stores have become operational. Recovery has improved to ~50% of pre-COVID levels in Q2 from ~15% in Q1. To register an early recovery, the company has undertaken relevant steps such as enhancing product portfolio with some value-added products, boosting presence in the e-commerce channel and stringently managing its costs going forward. The company has scaled up its digital initiatives by widening its portfolio on its website, while strengthening its presence across online market places. Newly launched channels such as Bata ChatShop, Bata Home Delivery, and Bata Store on Wheels contribute over 10% to store revenue. Bata has also changed its portfolio mix from formals and fashion categories to more relevant casuals, fitness and essential categories, which has led to faster pick up in volumes. The company has also renegotiated lease rentals, the benefit of which will be seen in the coming quarters. The company expects more and more consumers to be shifting to top brands and would be buying value-based products in the near term. Moreover, there might be some wedding/festive demand seen in H2FY2021. Overall, we expect FY2021 to be subdued and strong recovery is expected in FY2022 once the pandemic situation normalises. The company has a strong cash balance of ~Rs. 800 crore as of H1FY2021, which will help the company take care of near-term obligations in an uncertain environment.

Key positives

- Digital initiatives helped in enhancing revenue contribution from digital channels to 10% of revenue.
- To respond to semi-urban demand, the company opened its 200th franchisee store in Andhra Pradesh.

Key negatives

- Gross margin declined significantly by 600 bps to 50.4%, OPM was down from 25.7% to 4.9%.

Our Call

View - Recommend Buy with a PT of Rs. 1,550: Bata is focusing on expanding its presence through e-commerce/omni-channel and innovating its product portfolio with new relevant variants to drive growth in the medium to long term. Further, the company will benefit from the shift from non-branded to branded products. Bata is a debt-free company with strong cash balance of close to Rs. 800 crore, which along with negative working capital and improving store fundamentals will help the company take care of its near-term expansion plans without any disruptions. The stock has corrected by ~41% from its recent high and is currently trading at 42.9x its FY2023E EPS, which is a discount to its historic average and factors in the near-term headwinds. In view of this and long-term prospects, we recommend Buy on the stock with a PT of Rs. 1,550.

Key Risks

If the lockdown sustains and normalisation takes longer than expected, it will further affect H2FY2021 earnings due to sustenance of store closures, resulting in an overall earnings disruption for FY2021.

Valuations (Standalone) Rs cr

Particulars	FY19	FY20*	FY21E*	FY22E*	FY23E*
Revenue	2,928	3,053	1,807	2,886	3,318
OPM (%)	16.3	27.2	18.5	24.5	26.5
Adjusted PAT	330	327	19	287	398
EPS	25.6	25.4	1.5	22.3	31.0
P/E (x)	51.8	52.2	-	59.5	42.9
P/B (x)	9.8	9.0	9.4	8.5	7.4
EV/EBIDTA (x)	29.7	19.4	39.4	20.5	16.4
RoNW (%)	20.4	17.9	1.0	15.0	18.4
RoCE (%)	19.4	15.0	2.7	9.8	11.6

Source: Company; Sharekhan estimates
**estimates include the impact of Ind-AS 116*
Note: We have converted Bata to stock update from Viewpoint earlier

Revenue declined by 49%, margins remained impacted: For Q2FY2021, revenue declined by 49% y-o-y to Rs. 367.9 crore, in-line with our expectation of Rs. 361 crore and ahead of street expectation of Rs. 327 crore. However, recovery was stronger at ~50% from ~15% recovery in Q1. Digitally enabled channels contributed over 10% to store revenue. Gross margin slumped by 600 bps to 50.4%, largely led by an unfavourable product mix (higher contribution from value-added products). This along with lower operating leverage led to a significant decline in OPM to 4.9%, in-line with our expectation of 4.8%. Operating profit declined by 90.2% to Rs. 18.2 crore. Other income was lower from Rs. 17.7 crore to Rs. 14.4 crore. Loss before tax came in at Rs. 58.5 crore in Q2FY2021 as compared to profit of Rs. 97.5 crore in Q2FY2020. Reported loss stood at Rs. 44.4 crore (in-line with our expectation of loss of Rs. 43 crore).

Other key highlights

- Bata is witnessing higher semi-urban demand. Hence, the company responded by opening up its 200th franchise store at Tenali, Andhra Pradesh, a small town in Guntur district.
- As demand was stronger in tier II-V towns, given lesser impact of the pandemic, Bata also leveraged the opportunity to expand its presence via distributor-led multi-brand outlets. Bata is now present in over 30,000 MBOs.
- Newly launched digitally-enabled channels such as Bata ChatShop, Bata Home Delivery, and Bata Store on Wheels contribute over 10% to store revenue. The company's website continues to witness increasing demand and sales, driven by better assortment and conversion.
- The company has evolved its portfolio mix from formals and fashion categories to more relevant casuals, fitness, and essential categories, which has led to faster pick-up in volumes.
- The company continued to optimise its retail network and focused on cost-savings across rentals and operations, manufacturing, and driving efficiencies in its value chain, which will help enhance the company's profitability in the near to medium term.
- With the festive season underway, the company has launched the new campaign 'Kick Out 2020' along with its new collection, 'Ready Again,' which is resonating well with consumers.

Results (Standalone) Rs cr

Particulars	Q2FY21	Q2FY20	YoY %	Q1FY21	QoQ %
Net Revenues	367.9	722.0	-49.0	134.8	-
COGS	182.5	314.8	-42.0	80.3	-
Employee expenses	82.6	89.0	-7.2	84.8	-2.5
Rent	0.1	9.7	-	0.0	-
Other expenses	84.5	123.1	-31.4	55.8	51.4
Total expenses	349.7	536.6	-34.8	220.9	58.3
Operating profit	18.2	185.4	-90.2	-	-121.1
Other Income	14.3	17.7	-19.2	52.0	-72.5
EBITDA	32.5	203.1	-84.0	-34.1	-
Interest expenses	26.5	30.8	-13.8	27.8	-4.7
Depreciation & Amortization	64.5	74.9	-13.9	73.1	-11.8
PBT	-58.5	97.5	-	-135.0	-
Tax	-14.1	26.1	-	-33.9	-
Reported PAT	-44.4	71.4	-	-101.1	-
Adj. EPS	-3.5	5.6	-	-7.9	-
			bps		bps
GPM (%)	50.4	56.4	-600	40.4	999
OPM (%)	4.9	25.7	-	-	-

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector Outlook - Long-term growth prospects of the footwear industry are intact

India is the second largest footwear manufacturer after China, accounting for 9% of the world market with 22 billion pairs. The domestic market contributes ~90% to the overall footwear market in India. The domestic footwear market was badly affected by the lockdown during the pandemic environment (Q1 was worst affected). Closure of retail stores and restriction of out-of-home mobility affected sales in Q1FY2021. However, with easing of lockdown norms and gradual opening of retail stores/malls, footwear sales gained some momentum in Q2. With the ongoing festive season, gradual opening of the economy and likely opening of educational institutes by Q4, we expect the footwear industry to come back to pre-COVID levels (at least in the value segment). Having said that, low per-capita consumption at 1.66 pairs per annum, lower share of exports, and higher unorganised play provide a large opportunity for top brands to scale up operations in the near to medium term.

■ Company outlook - Strong recovery expected in FY2022

Bata has been focusing on increasing its omni-channel presence and is focusing on adding relevant products to its portfolio to drive demand in the near term. The company has recovered to ~50% of pre-COVID levels. Faster recovery has been witnessed in semi-urban areas. If the pandemic situation improves, we might see some recovery in H2FY2021 amid the festive/wedding season. We expect same-store-sales growth (SSSG) to improve gradually in the coming quarters. Lower operating leverage will put margins under pressure in FY2021. However, the same is expected to recover in FY2022, driven by improving product mix, operating efficiencies, cost-saving initiatives, and a stronger demand recovery.

■ Valuation - Recommend Buy with a PT of Rs. 1,550

Bata is focusing on expanding its presence through e-commerce/omni-channel and innovating its product portfolio with new relevant variants to drive growth in the medium to long term. Further, the company will benefit from the shift from non-branded to branded products. Bata is a debt-free company with strong cash balance of close to Rs. 800 crore, which along with negative working capital and improving store fundamentals will help the company take care of its near-term expansion plans without any disruptions. The stock has corrected by ~41% from its recent high and is currently trading at 42.9x its FY2023E EPS, which is a discount to its historic average and factors in the near-term headwinds. In view of this and long-term prospects, we recommend Buy on the stock with a PT of Rs. 1,550.

Peer valuation

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E
Relaxo Footwears	76.3	74.8	53.7	42.6	41.7	31.1	27.4	23.1	28.2
Bata India	52.2	-	59.5	19.4	39.4	20.5	15.0	2.7	9.8

Source: Company, Sharekhan estimates

About company

Bata is the largest retailer and manufacturer of footwear in India. The company has a retail network of over 1,400 stores, including 150 franchised stores, which sell total of ~47 million pairs of footwear annually. The retail channel contributes ~82% to the company's total revenue, whereas the balance 18% is contributed by multi-brand outlets and the e-commerce channel. Bata currently has a 15% value market share in the organised footwear market.

Investment theme

Bata has rebranded itself as a modern footwear player recently. This will help the company report double-digit revenue growth. With the implementation of GST, there is a shift from unbranded to branded products, which provides further scope for Bata in the Rs. 55,000 crore-60,000 crore footwear market in India, of which ~50% is unbranded. Consistent store expansion, investment behind the brand, mid to high single-digit SSSG, and premiumisation strategies would be key growth drivers for Bata in the near to medium term.

Key Risks

- **Slowdown in discretionary demand:** Any slowdown in SSSG due to fall in demand/footfalls would affect revenue growth.
- **Increased competition in highly penetrated categories:** Heightened competition would act as a threat to revenue growth.

Additional Data

Key management personnel

Ashwani Windlass	Chairman
Rajeev Gopalakrishnan	Managing Director
Sandeep Kataria	Chief Executive Officer
Ram Kumar Gupta	Chief Financial Officer
Nitin Bagaria	Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	5.1
2	Aditya Birla Sun Life Asset Management Co Ltd	3.4
3	Aditya Birla Sun Life Trustee Co Pvt Ltd	2.7
4	Kotak Mahindra Asset Management Co	2.3
5	FundRock Management Co SA	1.9
6	Axis Asset Management Co	1.5
7	Tata Asset Management Ltd	1.3
8	DSP Investment Managers Pvt Ltd	1.3
9	IDFC Mutual Fund	1.0
10	Vanguard Group Inc	0.9

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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