Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Relaxo Footwears Ltd

Subdued performance in Q3

Consumer Discretionary	Sharekhan code: RELAXO
Reco/View: Buy ⇔	CMP: Rs. 1,232
	Price Target: Rs. 1,490 ⇔

↑ Upgrade ⇔ Maintain ↓ Downgrade

Summary

- Relaxo Footwear's (Relaxo) Q3FY2022 net revenue grew by 10.6% y-o-y to Rs. 743.5 crore, largely driven by price hikes undertaken; gross margin and OPM were down 572 bps and 577 bps, respectively, resulting in a 20.6% y-o-y decline in PAT.
- Average realisation per pair came it higher at Rs. 164 per pair (vs Rs. 134 per pair in Q3FY21) while volume was reported lower at 4.5 crore pairs (vs 5 crore pairs in Q3FY21).
- Capacity enhancement (capacity of 1.5 lacs per day commissioned during Q3) along with diverse portfolio, enhanced distribution network, sustained investment behind brands, and a customer-centric approach will aid Relaxo in achieving double-digit topline growth in the medium term.
- The stock has corrected by 15% from its recent high and trades at 77.7x/61.9x its FY2023/FY2024E EPS. We maintain Buy with an unchanged PT of Rs. 1,490.

Relaxo Footwear's (Relaxo) Q3FY2022 performance was affected by a sharp increase in raw-material prices, resulting in a 20.6% y-o-y decrease in PAT. Revenue grew by 10.6% y-o-y to Rs. 743.5 crore, aided by price hikes undertaken by the company. Q3FY2022 average realisation per pair was higher at Rs. 164 per pair against Rs. 134 per pair in Q3FY2021, while Q3FY2022 volume was reported lower at 4.5 crore pairs versus 5 crore pairs in Q3FY2021. Sharp increase in raw-material prices and additional margin offered to neutralise the impact of GST rate hike, which impacted margins with gross margin/operating profit margin (OPM) declining by 572/577 bps y-o-y. During Q3FY2022, Relaxo increased capacity by 1.5 lakh pair per day, taking total capacity to 10 lakh pairs per day.

Key positives

- Average realisation reported higher at Rs. 164 per pair against Rs. 134 per pair in Q3FY21.
- Capacity enhanced by 1.5 lakh pair per day, taking total capacity to 10 lakh pairs per day.

Key negatives

- Volume reported lower at 4.5 crore pairs versus 5 crore pairs in Q3FY2021.
- Gross margin/OPM declined by 572/577 bps y-o-y to 53.2%/16.4%, respectively, due to raw-material inflation and additional margin offered to neutralise the impact of GST rate hike.

Management Commentary

- Relaxo has undertaken calibrated price hikes to mitigate the impact of unprecedented raw-material inflation. Management expects to benefit from price hikes undertaken along with softening raw-material prices in FY2023.
- The company aims to achieve strong growth on the back of its consumer-centric approach, diverse portfolio, product innovation, and strong market reach and continues to adopt strategic initiatives to capture expanding market opportunities in unexplored geographies.

Revision in estimates – We have lowered our earnings estimates for FY2022/FY2023/FY2024 by 2-3% to factor in raw-material inflation and lower-than-earlier-estimated margins.

Our Call

Valuation – Maintain Buy with an unchanged PT of Rs. 1,490 - With a strong portfolio of value-for-money footwear products, enhanced capacity of 10 lakh pairs per day, and expansion in distribution reach (especially in southern markets), Relaxo is well poised to achieve revenue and earnings CAGR of 17% each over FY2021-FY2024E. The company has a strong balance sheet (zero net debt) with good cash generation ability. The stock price has corrected by 15% from its recent high and the stock currently trades at 77.7x/61.9x its FY2023/FY2024E earnings. Relaxo remains one of our portfolio picks with consistent operating performance in the past several years. We maintain our Buy recommendation on the stock with an unchanged price target (PT) of Rs. 1,490.

Key Risks

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

Valuations (standalone) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenues	2,359	2,792	3,288	3,814
OPM (%)	21.0	17.0	19.5	20.5
Adjusted PAT	305	270	394	493
Adjusted diluted EPS (Rs.)	12.3	10.9	15.9	19.9
P/E (x)	100.3	113.1	77.7	61.9
P/B (x)	19.5	17.3	14.7	12.2
EV/EBIDTA (x)	61.5	64.1	47.5	38.4
RoNW (%)	21.4	16.2	20.4	21.5
RoCE (%)	29.5	20.8	27.2	26.6

Source: Company; Sharekhan estimates

3R MATRIX

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

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		⇔	
RQ		⇔	
RV		⇔	

ESG Disclosure Score NEW

ESG RISK RATING 16.36

Updated Jan 08, 2022

Low Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

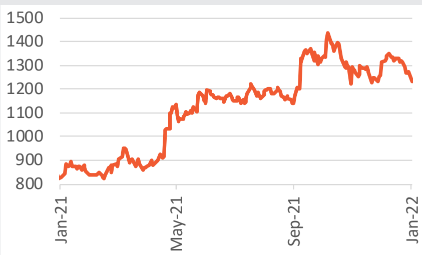
Company details

Market cap:	Rs. 30,656 cr
52-week high/low:	Rs. 1,447 / 810
NSE volume: (No of shares)	2.2 lakh
BSE code:	530517
NSE code:	RELAXO
Free float: (No of shares)	7.3 cr

Shareholding (%)

Promoters	70.8
FII	4.3
DII	7.1
Others	17.9

Price chart



Price performance

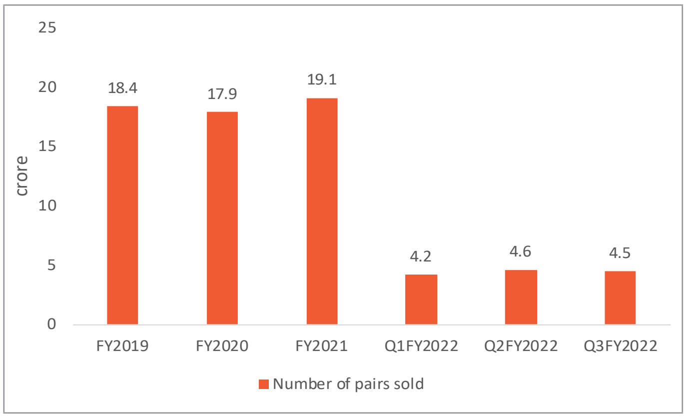
(%)	1m	3m	6m	12m
Absolute	-6.2	-7.7	7.2	48.3
Relative to Sensex	-5.8	-4.4	-2.3	28.9

Sharekhan Research, Bloomberg

Below par performance – Both revenue and profits miss expectations

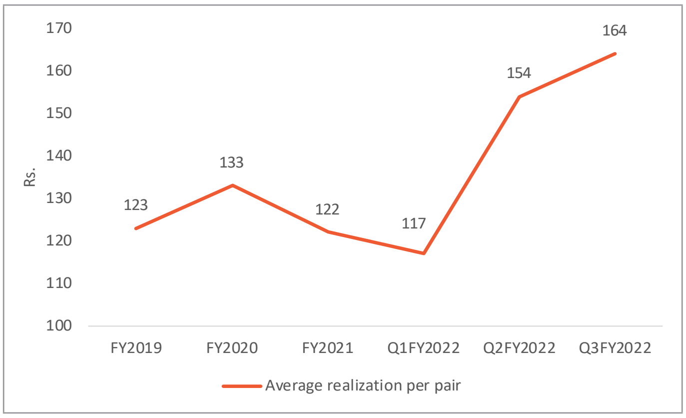
Q3FY2022 revenue grew by just 10.6% y-o-y and 4.1% q-o-q to Rs. 743.5 crore, below our and street expectation of Rs. 806.4 crore and Rs. 792 crore, respectively. Revenue growth was largely driven by price hikes undertaken by the company to pass on input cost inflation. Relaxo reported higher average realisation per pair during the quarter at Rs. 164 per pair against Rs. 134 per pair in Q3FY2021 and Rs. 154 per pair in Q2FY2022. However, the quarter registered lower volumes on a y-o-y and q-o-q basis at 4.5 crore pairs sold in Q3FY2022 versus 5 crore pairs sold in Q3FY2021 and 4.6 crore pairs sold in Q2FY2022. Gross margin decreased by 572 bps y-o-y to 53.2% and OPM decreased by 577 bps y-o-y to 16.4% (below our expectation of 16.7% and street expectation of 17%), affected by a sharp increase in input prices and additional margin offered to neutralise the impact of GST rate increase from 5% to 12% w.e.f. January 1, 2022. Operating profit decreased by 18.2% y-o-y to Rs. 121.6 crore. Reported PAT declined by 20.6% y-o-y to Rs. 71.5 crore, lower than our and street expectation of Rs. 82.7 crore and Rs. 110 crore, respectively, affected by a sharp drop in margins. During the quarter, additional capacity of 1.5 lakh pair per day of footwear was commissioned at unit located in Bhiwadi Rajasthan, taking the total capacity across all categories and plants to 10 lakh pair per day of footwear.

Trend in the number of pairs sold



Source: Company, Sharekhan Research

Trend in average realisation per pair



Source: Company, Sharekhan Research

Results (standalone) Rs cr

Particulars	Q3FY22	Q3FY21	y-o-y (%)	Q2FY22	q-o-q (%)
Net Revenue	**743.5**	**672.0**	**10.6**	**714.4**	**4.1**
Raw-material cost	348.0	276.1	26.0	323.0	7.7
Staff cost	84.7	81.7	3.7	86.7	-2.3
Other expenses	189.2	165.5	14.3	188.3	0.5
Total expenses	621.9	523.3	18.8	597.9	4.0
Operating profit	**121.6**	**148.7**	**-18.2**	**116.5**	**4.4**
Other Income	5.5	4.0	38.1	7.1	-22.6
EBITDA	127.1	152.7	-16.7	123.6	2.9
Interest expenses	3.8	4.0	-6.3	3.6	3.0
Depreciation & Amortization	28.0	27.8	0.8	28.3	-1.1
Profit before Tax	**95.4**	**120.9**	**-21.1**	**91.6**	**4.1**
Tax	23.8	30.8	-22.6	23.3	2.5
Reported PAT	**71.5**	**90.1**	**-20.6**	**68.4**	**4.6**
EPS	2.9	3.6	-20.6	2.8	4.6
			bps		**bps**
GPM (%)	53.2	58.9	-572	54.8	-159
OPM (%)	16.4	22.1	-577	16.3	5
NPM (%)	9.6	13.4	-378	9.6	5
Tax rate (%)	25.0	25.5	-49	25.4	-38

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 with consumption of 26 billion pairs after China with 42 billion pairs. The domestic market makes up ~90% of India's overall footwear market. The domestic footwear market was badly affected by the lockdown during the pandemic. The beginning of FY2022 was uncertain, but a rapid vaccination programme and dropping cases helped in robust recovery. Low per capita consumption at 1.66 pair p.a., decline in imports, and higher unorganised players provide a huge opportunity for top brands to scale up operations in the near to medium term. The Indian footwear market is expected to post a CAGR of ~11% over CY2021-CY2025 compared to global market growth of 5.5% CAGR over CY2021-CY2025.

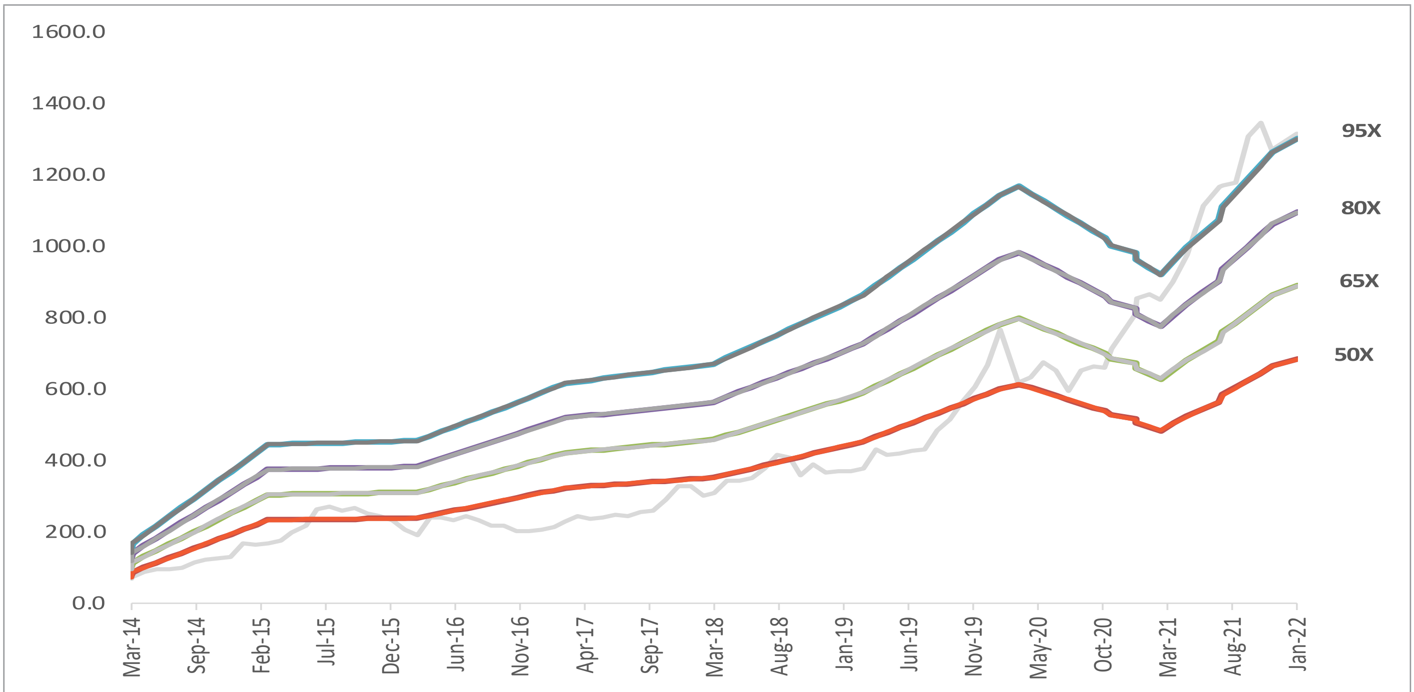
■ Company outlook – Medium-term outlook remains stable

FY2022 started on a strong note, but the second wave had an impact on performance from mid-April till May. A sharp increase in raw-material prices compelled domestic players to pass it to consumers through price hikes. Overall inflation and slowdown in the rural economy will have an impact on near-term sales performance. Further, any increase in GST rate on footwear below Rs. 1,000 pair will also have impact on value-for money products in the near term. FY2023 will see good performance, driven by market share gains from unorganised players, higher presence in e-commerce channels, and higher demand for value-for-money products. Lower per capita consumption in India, Relaxo's lower penetration in the South Indian market, and sustained product additions remain long-term growth drivers. Raw-material prices have moved up and will impact margins in the near term. However, better revenue mix an d efficiencies will help OPM to improve in the coming years.

■ Valuation – Maintain Buy with an unchanged PT of Rs. 1,490

With a strong portfolio of value-for-money footwear products, enhanced capacity of 10 lakh pairs per day, and expansion in distribution reach (especially in southern markets), Relaxo is well poised to achieve revenue and earnings CAGR of 17% each over FY2021-FY2024E. The company has a strong balance sheet (zero net debt) with good cash generation ability. The stock price has corrected by 15% from its recent high and the stock currently trades at 77.7x/61.9x its FY2023/FY2024E earnings. Relaxo remains one of our portfolio picks with consistent operating performance in the past several years. We maintain our Buy recommendation on the stock with an unchanged PT of Rs. 1,490.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Bata	-	-	56.6	103.8	38.3	24.6	-	8.7	14.3
Relaxo Footwears	-	-	77.7	61.5	64.1	47.5	29.5	20.8	27.2

Source: Company, Sharekhan estimates

About the company

Relaxo is a leading footwear company with a turnover of over Rs. 2,400 crore. The company has eight manufacturing facilities across northern India with a capacity of 10 lakh pairs per day. The company sells close to 190 million pairs per annum through its wide distribution network of over 50,000 retailers, ~650 distributors, and 402 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 registered sustained double-digit volume growth in the past 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 crore – Rs. 60,000 crore Indian footwear market, of which ~50% is unbranded. Capacity expansion, investment on brands, steady volume growth, and improving presence in untapped markets along with increasing price differential in imported and domestic footwear as a result of 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 competition in highly penetrated categories:** Heightened competition would threaten revenue growth.
- **Increased input costs:** Any significant increase in rubber prices or that of crude oil derivatives would affect profitability.

Additional Data

Key management personnel

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

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	VLS Securities Ltd.	6.6
2	VL Finance	4.0
3	SBI Funds Management Pvt. Ltd.	4.0
4	Capital Group Cos Inc.	1.0
5	UTI Asset Management Co. Ltd.	0.7
6	ICICI Prudential Asset Management	0.6
7	Vanguard Group	0.6
8	DSP Investment Managers Pvt. Ltd.	0.5
9	Daiwa Asset Management India Pvt. Ltd.	0.3
10	Principal Financial Group Inc.	0.3

Source: Bloomberg (Old data)

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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by BNP PARIBAS

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Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

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