Relaxo Footwears (RELFOO)

ICICI direct Research

CMP: ₹ 1018	Target: ₹ 1100 (8%)	Target Period: 12 months	HOLD

May 16, 2022

Result Update

RM inflation dents margins; long term story intact….

About the stock: Relaxo is India's leading footwear manufacturing company, boasting of largest capacity of 10.0 lakh pairs per day. It is a dominant player in the open footwear space (~80% of sales), with its strong portfolio of brands ('Flite', 'Bahamas', 'Sparx', 'Relaxo).

- Market leader in value priced segment selling ~19 crore pairs annually
- Relaxo, over the years, has maintained b/s prudence with controlled working capital cycle, healthy asset turns of 2.5x and generating RoCE of 20%+

Q4FY22 Results: Higher inflationary raw material pressure hampered profitability.

- Revenue de-grew 7% YoY to ₹ 698.2 crore. Volumes declined 26% YoY as calibrated price hikes (up 27% YoY), impacted consumer sentiments
- On account of input cost inflation (crude based) and a significantly higher base, EBITDA margins declined 586 bps YoY (44 bps QoQ) to 15.9%
- PAT for the quarter declined 38% YoY (down 10% QoQ) to ₹ 62.92 crore

What should investors do? Relaxo has been an exceptional performer with stock price appreciating at ~ 35% CAGR in the last five years.

- Relaxo has witnessed ~18% decline in share price since our last result update owing to unprecedented inflation scenario (35% RM based on crude derivatives) and uncertainties on the demand outlook. We remain structurally positive on the business model given its strong brand salience in tier II/III towns and healthy balance sheet to weather the crisis. However, premium valuations and near term headwinds may cap upsides. Hence, we reiterate **HOLD** rating on the stock with a revised target price

Target Price and Valuation: We value Relaxo at ₹ 1100 i.e. 65x FY24E EPS

Key triggers for future price performance:

- Despite selling ~18 crore pairs, Relaxo's current market share is <10%. Given its robust balance sheet and strong brand patronage, we believe there is enough headroom for long-term growth and market share gains
- While the north region remains the main fortress for the company (50%+ revenues), west and south remain relatively underpenetrated markets. Relaxo has geo-tagged ~100000 outlets (currently present in ~60000 outlets), which signifies immense opportunity to penetrate new territories
- We model revenue CAGR of 18.5% in FY22-24E with volumes expected to pick up pace in FY24E (as customers get accustomed to price hikes). Expect margins to improve 260 bps to 18% in FY22-24E

Alternate Stock Idea: Apart from Relaxo, in our retail coverage we also like Bata.

- Bata India has a strong b/s, diversified branded product portfolio and pan India network, which would enable sustained long term profitable growth
- BUY with a target price of ₹ 2360

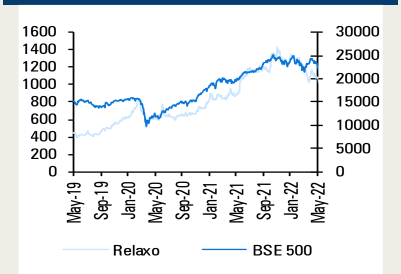
Particulars

Particulars	Amount
Market Capitalisation (₹ crore)	25,256.6
Total Debt (FY22) (₹ crore)	20.0
Cash & invetment (FY22) (₹ crore)	206.8
EV (₹ crore)	25,069.8
52 Week H / L	1447 /898
Equity Capital (₹ crore)	24.9
Face Value (₹)	1.0

Shareholding pattern

	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Promoter	70.9	70.9	70.9	70.8	70.8
FII	3.9	3.5	3.6	3.8	3.2
DII	7.0	7.3	7.2	7.1	6.9
Others	18.2	18.3	18.4	18.3	19.1

Price Chart



Recent event & key risks

- Gross margin contraction owing to higher input costs
- **Key Risk:** (i) Re-imposition of lockdown can lower sales (ii) Better than expected margin can lead to higher profitability

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ICICI Securities – Retail Equity Research

Key Financial Summary

Financials	FY20	FY21	FY22	5 year CAGR (FY17-22)	FY23E	FY24E	2 year CAGR (FY22-24E)
Net Sales	2,410.5	2,359.2	2,653.3	10.0%	3,120.2	3,728.1	18.5%
EBITDA	409.0	495.5	415.8	12.0%	496.1	682.2	28.1%
Adjusted PAT	226.3	291.6	232.7	14.0%	287.6	422.7	34.8%
P/E (x)	111.6	86.7	108.9		88.1	59.9	
EV/Sales (x)	10.5	10.6	9.5		8.0	6.6	
EV/EBITDA (x)	61.8	50.3	60.6		50.2	36.3	
RoCE (%)	23.9	26.0	18.3		20.7	26.3	
RoE (%)	17.8	18.5	13.2		14.8	19.0	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter

- Relaxo reported weak revenue growth, significantly weighed down by subdued volumes. Revenue for the quarter declined 7% YoY (6% QoQ) to ₹ 698.9 crore. Steep price hike (~25% YoY) and a very strong base resulted in volumes declining by ~26% YoY to 4.2 crore pairs in Q4FY22. The quarter was further impacted by covid related disruptions in Jan and increase in GST rates from 5% to 12% for footwear priced below ₹ 1000. For FY22, the company registered 12% YoY topline growth to ₹ 2653 crore with average realisations of ₹ 150/pair (up 22% YoY). Relaxo in FY21 had recorded its highest sales volume (19.1 crore pairs) as the pandemic led restrictions had given a fillip to demand for open footwear (slippers & sandals). However, as restrictions eased in FY22, demand for open footwear (~80% of sales) started to moderate
- In FY21, the company had recorded one of the best EBITDA margins to the tune of 21%, which was on the back of benign RM prices (highest ever gross margins of ~58%) and lower marketing spends. With prices of crude based polymers reversing sharply in FY22 (certain RM prices as high as 80% YoY), coupled with normalisation of selling and admin expenses, average quarterly margins declined to 16%. The company has taken four price hikes in FY22 amounting to ~ 25% increase YoY, which is the highest in its history in a single year. While the current price hike should be adequate to maintain current level of gross margins (52-53%), the company continues to monitor the dynamic situation and will take appropriate action keeping in mind the competitive pricing strategy
- On the balance sheet front, the company has witnessed a significant increase in inventory (up 60% YoY) with net working capital days increasing to 97 (vs. average 60 days). Apart from higher RM prices, the reason for increase in inventory days is increase in RM inventory (to avoid disruption of production in a rising input cost scenario). Also, lower sales have led to higher finished good inventory further pressurising the working capital position of the company. Increased sales of sports/athleisure shoes, which has a higher lead time has also contributed to the increase in inventory. The company expects the situation to improve over the next two quarters as the company is able to liquidate the finished good inventory. Despite negative FCF in FY22, Relaxo continues to have healthy cash and investments worth ₹ 200+ crore

Q4FY22 conference call highlights:

- The management indicated that the overall business scenario remained challenging owing to significant increase in product prices across categories (due to higher input cost and GST rate hike) negatively impacting volume growth. Volumes saw a significant decline after the latest price hike taken in December 2021 but volumes are recovering as the consumers get used to the new price levels. The average price increase across categories has been ~ 25%
- The consumer sentiment is a bit subdued due to high inflation, which is particularly impacting the lower priced products. There are instances of down trading by consumers in favour of unorganised players in low price point products due to negative impact on the purchasing power of consumers. However, the management indicated that it is a transitionary phase and consumers would revert to aspirational branded products like Relaxo as the quality of products offered by unbranded players is inferior to that offered by Relaxo. Also, the management indicated that the impact on volumes has been more in rural and urban areas while metros have performed better
- On the raw material scenario, the management indicated that things have not yet stabilised and the company is monitoring the situation and will take appropriate action keeping in mind the competitive pricing strategy
- On the margin front, the management indicated that FY22 margins have been impacted due input cost inflation and GST support to dealers/distributors (Q3FY22- ₹ 15-18 crore, Q4FY22 ₹ 8-10 crore). The management is hopeful of achieving EBITDA margin in line with its FY20 performance of ~ 17%
- The normalisation of consumer footfalls and opening up of schools, colleges and offices has led to increased demand for closed footwear while demand for open footwear has been lower than it was in the pandemic period
- Channel wise, e-commerce is the among the fastest growing channels and its share has increased from 10% in FY21 to 11.5% in FY22. Online revenue share for Relaxo's Sparx brand was at 25%. The company expects the growth momentum for the e-commerce channel to sustain driven by increased spend on the e-commerce channel and consequent increase in its share in the overall revenue over next few years. The company does not adopt a different pricing strategy for the e-commerce channel. Also, margins are in line with the overall company margin
- Over the last two years, the company has restructured its distribution footprint. The company has reduced the number of distributors from 800 two years ago to ~ 680 in FY22. Relaxo has removed the low performing distributors as cost of servicing those distributors was higher compared to other distributors on account of low revenues generated through them. On the overall retail touch points, the company has added 10000 outlets (mainly in west & south) in FY22 to and total number of retail touch points currently stands at 60000 outlets
- Brand wise, Hawaii contributes 25% of total revenue while Flight and Sparx contribute 37% and 38%, respectively. Shoes contribute ~ 60% of Sparx revenues while rest 40% is contributed by sandals. The price increase has been more in Hawaii and Bahamas because of higher proportion of EVA (price of which has spiralled over the last few quarters) used in these products

- The company currently has a capacity of manufacturing 10 lakh pieces per day and is operating at a capacity utilisation of ~ 65% and is not looking to increase the capacity in the near term
- North India continues to be the dominant revenue generating region for the company with revenue share of 50%, while east contributes 18% and west and south India contribute 18% and 13%, respectively. The Northern and eastern regions have seen more volume decline compared to west and southern regions

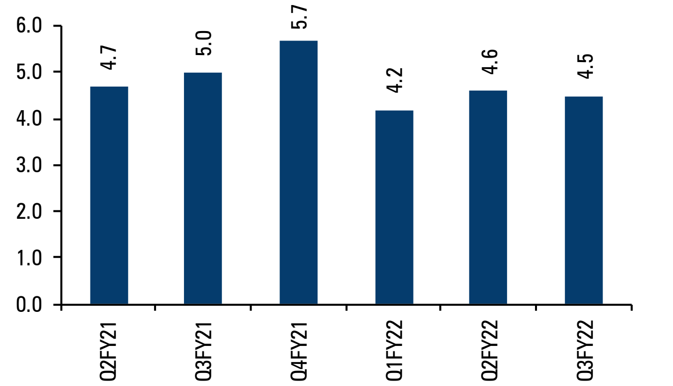
Exhibit 1: Variance Analysis

	Q4FY22	Q4FY21	YoY (%)	Q3FY22	QoQ (%)	Comments
Revenue	698.2	747.7	-6.6	743.5	-6.1	Volumes declined by 26% YoY to 4.2 crore pairs. Realisations increased 27% YoY to ₹ 165/pair
Raw Material Expens	319.5	322.8	-1.0	348.0	-8.2	
Gross Profit	378.7	424.9	-10.9	395.5	-4.3	
Gross Profit Margin	54.2	56.8	-259 bps	53.2	104 bps	Gross margins declined YoY owing to higher RM inflation
Employee exp	89.9	89.4	0.6	84.7	6.1	
Other Exp	177.7	172.6	2.9	189.2	-6.1	
EBITDA	111.1	162.9	-31.8	121.6	-8.6	
EBITDA Margin (%)	15.9	21.8	-587 bps	16.4	-44 bps	Owing to negative operating leverage, EBITDA margins declined marginally by 587 bps YoY
Depreciation	28.7	27.0	6.5	29.1	-1.3	
Other Income	5.9	6.9	-14.2	5.5	8.0	
Interest	3.9	5.2	-24.9	4.1	-3.9	
Exceptional Income	-	-		-		
PBT	84.4	137.6	-38.6	94.0	-10.1	
Tax Outgo	21.5	35.4	-39.3	23.9	-9.9	
PAT	62.9	102.2	-38.4	70.1	-10.2	

Source: Company, ICICI Direct Research

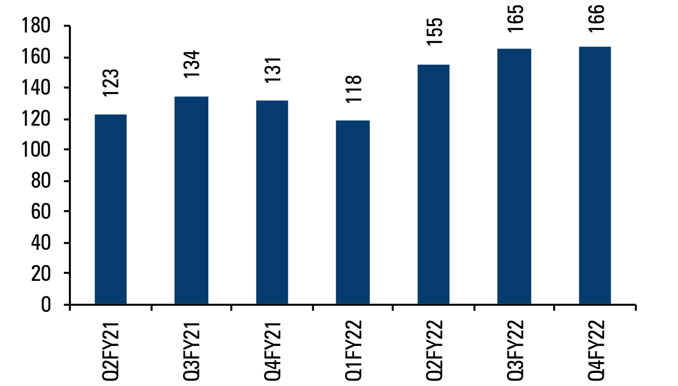
Financial story in charts

Exhibit 2: Quarterly volume trend (crore pairs)



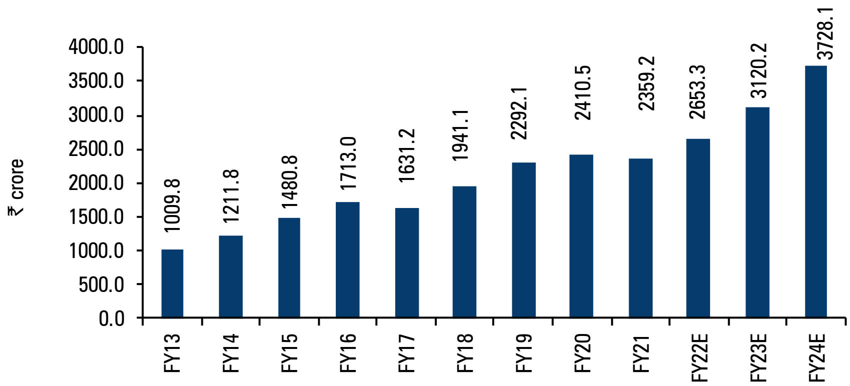
Source: Company, ICICI Direct Research

Exhibit 3: Realisation trend (₹/ pair)



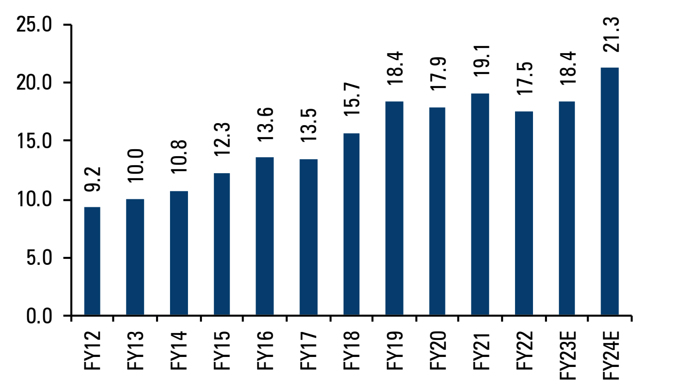
Source: Company, ICICI Direct Research

Exhibit 4: Revenue trend



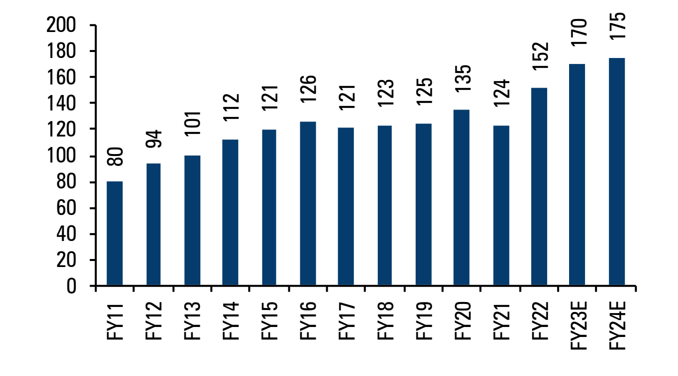
Source: Company, ICICI Direct Research

Exhibit 5: Volume trend (crore pairs)



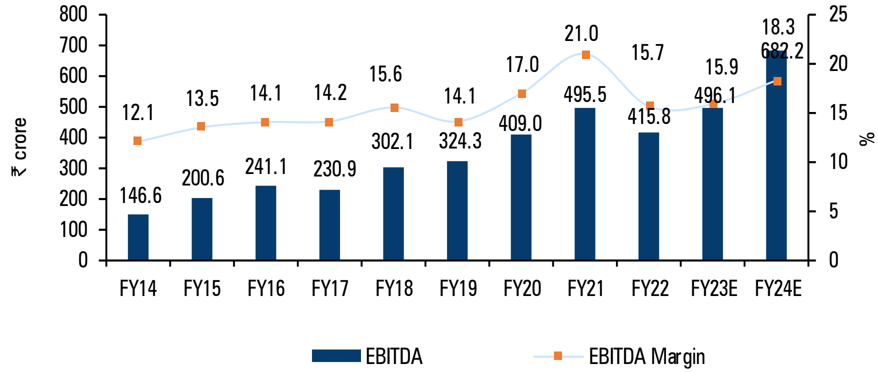
Source: Company, ICICI Direct Research

Exhibit 6: Realisation trend (₹ /pair)



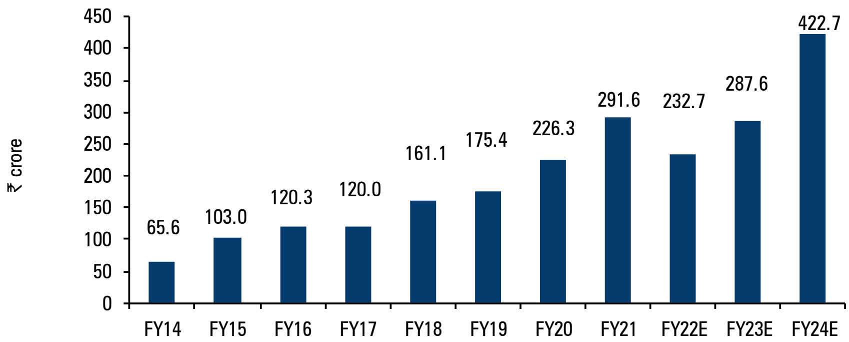
Source: Company, ICICI Direct Research

Exhibit 7: EBITDA and EBITDA margin trend



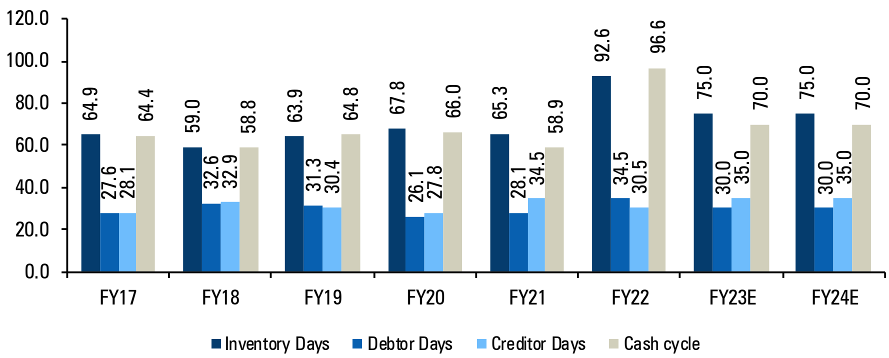
Source: Company, ICICI Direct Research

Exhibit 8: Net profit trend



Source: Company, ICICI Direct Research

Exhibit 9: Net working capital days



Source: Company, ICICI Direct Research

Financial Summary

Exhibit 10: Profit and loss statement ₹ crore

(Year-end March)	FY21A	FY22E	FY23E	FY24E
Net Sales	2,359.2	2,653.3	3,120.2	3,728.1
Growth (%)	(2.1)	12.5	17.6	19.5
Total Raw Material Cost	1,003.3	1,216.7	1,460.3	1,696.3
Gross Margins (%)	57.5	54.1	53.2	54.5
Employee Expenses	301.4	334.7	368.2	425.0
Other Expenses	559.0	686.1	795.7	924.6
Total Operating Expenditure	1,863.7	2,237.5	2,624.1	3,045.8
EBITDA	495.5	415.8	496.1	682.2
EBITDA Margin	21.0	15.7	15.9	18.3
Interest	17.1	15.3	17.9	20.2
Depreciation	110.0	113.5	123.9	132.2
Other Income	22.8	23.7	30.0	35.0
Exceptional Expense	-	-	-	-
PBT	391.2	310.6	384.3	564.8
Total Tax	99.6	77.9	96.7	142.2
Profit After Tax	291.6	232.7	287.6	422.7

Source: Company, ICICI Direct Research

Exhibit 11: Cash flow statement ₹ crore

(Year-end March)	FY21A	FY22E	FY23E	FY24E
Profit/(Loss) after taxation	291.6	232.7	287.6	422.7
Add: Depreciation	110.0	113.5	123.9	132.2
Net Increase in Current Assets	56.0	-271.6	13.7	-189.5
Net Increase in Current Liabilities	62.0	-12.2	78.4	59.3
CF from operating activities	**519.6**	**62.5**	**503.6**	**424.6**
(Inc)/dec in Investments	-338.0	143.9	-107.2	45.0
(Inc)/dec in Fixed Assets	-123.3	-150.5	-109.8	-107.0
Others	-13.4	1.7	9.1	0.0
CF from investing activities	**-474.7**	**-4.8**	**-208.0**	**-62.0**
Inc / (Dec) in Equity Capital	0.0	0.1	0.0	0.0
Inc / (Dec) in Loan	-19.2	20.0	-20.0	0.0
Others	-22.2	-72.8	-139.2	-188.3
CF from financing activities	**-41.3**	**-52.8**	**-159.2**	**-188.3**
Net Cash flow	3.6	4.9	136.4	174.3
Opening Cash	4.1	7.7	12.6	148.9
Closing Cash	**7.7**	**12.6**	**149.0**	**323.2**

Source: Company, ICICI Direct Research

Exhibit 12: Balance Sheet ₹ crore

(Year-end March)	FY21A	FY22E	FY23E	FY24E
Equity Capital	24.8	24.9	24.9	24.9
Reserve and Surplus	1,547.6	1,735.0	1,922.0	2,196.7
Total Shareholders funds	1,572.4	1,759.9	1,946.9	2,221.6
Total Debt	-	20.0	-	-
Non Current Liabilities	164.0	173.9	173.9	173.9
Source of Funds	**1,736.4**	**1,953.8**	**2,120.8**	**2,395.5**
Gross block	975.3	1,099.6	1,219.6	1,349.6
Less: Accum depreciation	254.2	330.2	415.6	507.4
Net Fixed Assets	721.1	769.4	804.0	842.2
Capital WIP	112.2	145.2	135.0	112.0
Intangible assets	39.1	32.4	32.4	32.4
Investments	338.2	194.3	301.5	256.5
Inventory	422.1	673.3	641.1	766.0
Cash	7.7	12.5	148.9	323.2
Debtors	181.5	250.8	256.5	306.4
Loans & Advances & Other CA	146.1	97.2	110.0	124.6
Total Current Assets	757.3	1,033.7	1,156.5	1,520.2
Creditors	222.8	221.7	299.2	357.5
Provisions & Other CL	216.6	205.5	206.4	207.4
Total Current Liabilities	439.4	427.2	505.6	564.9
Net Current Assets	318.0	606.5	650.8	955.3
LT L& A, Other Assets	207.9	206.1	197.1	197.1
Other Assets	0.0	0.0	0.0	0.0
Application of Funds	**1,736.4**	**1,953.8**	**2,120.7**	**2,395.5**

Source: Company, ICICI Direct Research

Exhibit 13: Key ratios

(Year-end March)	FY21A	FY22E	FY23E	FY24E
Per share data (₹)				
EPS	11.7	9.3	11.6	17.0
Cash EPS	16.2	13.9	16.5	22.3
BV	63.3	70.7	78.2	89.3
DPS	0.0	2.5	4.1	6.0
Cash Per Share	0.3	0.5	6.0	13.0
Operating Ratios (%)				
EBITDA margins	21.0	15.7	15.9	18.3
PBT margins	16.6	11.7	12.3	15.2
Net Profit margins	12.4	8.8	9.2	11.3
Inventory days	65.3	92.6	75.0	75.0
Debtor days	28.1	34.5	30.0	30.0
Creditor days	34.5	30.5	35.0	35.0
Return Ratios (%)				
RoE	18.5	13.2	14.8	19.0
RoCE	26.0	18.3	20.7	26.3
RoIC	34.6	20.8	27.3	35.9
Valuation Ratios (x)				
P/E	86.7	108.9	88.1	59.9
EV / EBITDA	50.3	60.6	50.2	36.3
EV / Sales	10.6	9.5	8.0	6.6
Market Cap / Revenues	10.7	9.5	8.1	6.8
Price to Book Value	16.1	14.4	13.0	11.4
Solvency Ratios				
Debt / Equity	0.0	0.0	0.0	0.0
Debt/EBITDA	0.0	0.0	0.0	0.0
Current Ratio	1.7	2.4	2.0	2.1
Quick Ratio	0.7	0.8	0.7	0.8

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%

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