Sharekhan by BNP PARIBAS

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Stock Update

Result Update

Bata India

Mixed Q2; Strategies in place to drive growth

Consumer Discretionary	Sharekhan code: BATAINDIA
Reco/View: Buy ↔	CMP: Rs. 1,739
	Price Target: Rs. 2,055 ↓

↑ Upgrade ↔ Maintain ↓ Downgrade

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 19.55

Updated Oct 08, 2022

Low Risk

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

Source: Morningstar

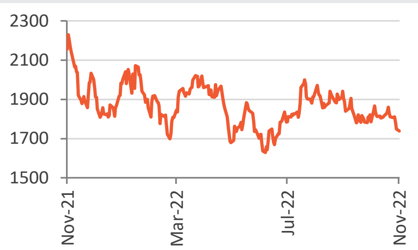
Company details

Market cap:	Rs. 22,354 cr
52-week high/low:	Rs. 2,262 / 1,608
NSE volume: (No of shares)	3.4 lakh
BSE code:	500043
NSE code:	BATAINDIA
Free float: (No of shares)	6.4 cr

Shareholding (%)

Promoters	50.2
FII	8.3
DII	29.0
Others	12.6

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-2.6	-11.8	2.9	-19.4
Relative to Sensex	-9.0	-14.7	-13.5	-20.9

Sharekhan Research, Bloomberg

Summary

- Bata India (Bata) delivered mixed performance in Q2FY2023. Revenue grew strongly by (35% y-o-y), while EBITDA margin remained flat y-o-y due to higher input cost inflation and change in channel mix. PAT delivered strong 48% y-o-y growth.
- The company added 68 stores, including 10 COCO stores, 30 franchisee stores, and 28 Shop-In-Shops, during the quarter, taking the total store count to 1,956 across 1,108 towns at Q2FY2023-end. Bata aims higher contribution from franchisee stores going ahead and targets 500 stores by FY2024 from 353 stores currently.
- Casualisation of product portfolio, store expansion through the franchisee and MBO route, renovation of existing stores, and digital footprint expansion are some of the key growth levers that will help the revenue growth momentum to sustain in the quarters ahead. Focus remains on regaining volume growth in retail stores.
- The stock trades at 57.4x and 42.3x its FY2023E and FY2024E earnings, respectively. We maintain a Buy rating on the stock with a revised PT of Rs. 2,055.

Bata India (Bata) registered revenue growth of 35% y-o-y and 15% over Q2FY2020 (pre-COVID level) to Rs. 829.8 crore, driven by higher footfalls, network expansion, relevant communication, and portfolio casualisation. Gross margins improved by 210 bps y-o-y to 55%. However, higher other expenses led to EBITDA margin remaining flat y-o-y at 19.4%. EBITDA grew by 35.1% y-o-y to Rs. 160.9 crore, while reported PAT grew by 48.1% y-o-y to Rs. 54.8 crore. In H1FY2023, revenue grew by 2x y-o-y to Rs. 1,772.8 crore, while EBITDA margin improved sharply from 9.7% in H1FY2022 to 22.9% in H1FY2023. The company reported PAT of Rs. 174.2 crore in H1FY2023 against loss of Rs. 44.9 crore in H1FY2022. The company added 68 stores and the total the number of stores as of September 2022 stood at 1,956 stores (18% of stores are franchisee stores).

Key positives

- Gross margins improved by 210 bps y-o-y to 55%.
- Floatz registered 132% q-o-q growth.
- The e-commerce channel reported y-o-y growth of 1.5x; Sneaker sales (digital channel) grew by 126% y-o-y.

Key negatives

- Other expenses were higher by 62% y-o-y due to normalisation of rent expenses, increased contribution from the low-margin e-commerce channel, and higher marketing investments..

Management Commentary

- The mass categories witnessed demand pressure due to inflation and GST on lower-priced footwear. However, the company is witnessing strong traction for premium brands and has launched the Red Label concept with 2.5x ASP than normal brands to further accelerate this demand.
- In Q2FY2023, revenue grew by 15% over Q2FY2020, with volume growth of 6-7%, while price-led growth stood at 7%. Management targets to achieve volume-based growth in the quarters ahead and has strategies in place to achieve the same.
- Advertisement expenses for the quarter stood at 2.5% of sales. Management has stated that the company targets to increase the spends to 3% of sales.
- Digital business achieved its highest revenue during the quarter. Sales through digitally enabled channels continued its momentum and contributed 11% to total sales in Q2FY2023. E-commerce channel reported y-o-y growth of 1.5x in Q2FY2023.
- Bata's EBITDA margin stood lower compared to pre-COVID levels. Management has indicated that company-level margins were impacted by channel mix and that Bata aims to improve margins at the channel level. Management targets to cross the pre-covid level margins in the medium term.
- Bata added 68 stores in Q2FY2023, taking the total number of stores to 1,956 at Q2FY2023-end. The company opened 10 company-owned-company-operated (COCO) stores, 30 franchisee stores, and 28 shop-in-shop (SIS) during the quarter. The total franchisee stores stood at 353 stores across more than 300 towns at Q2FY2023-end and contributed 18% to the overall sales in Q2FY2023. The company targets 500 franchisee stores by FY2024 at a run rate of opening 30-40 stores per quarter. The company continued to expand its distribution business by adding 29 towns to cross its presence across 1,108 towns.

Revision in estimates – We have lowered our earnings estimates for FY2023 and FY2024 to factor in lower-than-earlier-expected margins due to the normalisation of key costs post the pandemic and higher contribution from the low-margin e-commerce channel. We have introduced FY2025 estimates through this note.

Our Call

View: Maintain Buy with a revised PT of Rs. 2,055: Bata's Q2FY2023 performance was mixed with strong double-digit revenue growth, while EBITDA margin remained flat y-o-y. Management expects growth momentum to continue, aided by growth levers such as casualisation of portfolio, expanding retail footprint through the franchisee route, and scaling up the digital revenue. Profitability is expected to improve going ahead and the company targets to cross pre-COVID level EBITDA margin in the medium term. The stock trades at 57.4x/42.3x its FY2023E/FY2024E EPS and 25.3x/20.4x its FY2023E/FY2024E EV/EBITDA. We maintain our Buy recommendation on the stock with a revised price target (PT) of Rs. 2,055.

Key Risks

Slowdown in sales due to change in consumer sentiments or increased competition from large players will affect recovery momentum and will act as a key risk to our earnings estimates.

Valuation (Standalone) Rs cr

Particulars	FY21	FY22	FY23E	FY24E	FY25E
Revenue	1,708	2,388	3,564	4,098	4,590
EBITDA (%)	9.5	17.5	22.8	24.1	24.3
Adjusted PAT	-85	103	389	529	631
% YoY growth	-	-	-	35.9	19.2
EPS (Rs.)	-6.6	8.0	30.3	41.1	49.1
P/E (x)	-	-	57.4	42.3	35.4
P/B (x)	12.7	12.3	10.6	8.8	7.3
EV/EBITDA (x)	87.1	47.6	25.3	20.4	17.6
RoNW (%)	-	5.8	19.8	22.8	22.5
RoCE (%)	-	5.3	12.7	15.6	16.6

Source: Company; Sharekhan estimates

Strong revenue growth; Miss on margins

Bata's revenue grew by 35.1% y-o-y to Rs. 829.8 crore, ahead of our as well as average street expectation of Rs. 768 crore – Rs. 797 crore, aided by strong demand for footwear with opening up of the economy. Growth was driven by a mix of volume and value. The company opened 30 new franchisee stores, taking the total count to above 250 stores. Gross margins improved by 210 bps y-o-y to 55%. However, EBIDTA margin stood flat on a y-o-y basis at 19.4% due to higher other expenses (up by 62% y-o-y). EBITDA margin decreased sequentially by 655 bps and was lower than our as well as average street expectation of 25-25.5%. Operating profit grew by 35.1% y-o-y to Rs. 160.9 crore, while reported PAT grew by 48.1% y-o-y to Rs. 54.8 crore, lower than our as well as average street expectation of Rs. 89 crore – Rs. 91 crore. In H1FY2023, revenue grew by 2x y-o-y to Rs. 1,772.8 crore, while EBITDA margin improved sharply from 9.7% in H1FY2022 to 22.9% in H1FY2023. The company reported PAT of Rs. 174.2 crore in H1FY2023 against loss of Rs. 44.9 crore in H1FY2022.

Store expansion and renovation on track

Bata added 68 stores in Q2FY2023, taking the total number of stores to 1,956 at Q2FY2023-end. The company opened 10 COCO stores, 30 franchisee stores, and 28 shop-in-shop (SIS) during the quarter. The total franchisee stores stood at 353 stores across more than 300 towns at Q2FY2023-end and contributed 18% to overall sales in Q2FY2023. The company targets 500 franchisee stores by FY2024 at a run rate of opening 30-40 stores per quarter. The company continued to expand its distribution business by adding 29 towns to cross its presence across 1,108 towns. Sneaker Studio was implemented in 250 stores across the country to display up to 300 styles across nine brands. Bata continued its store renovation strategy to enhance customer experience and undertook 54 renovations and facelifts in H1FY2023 (27 undertaken in Q2), with capex of Rs. 20-50 lakh per store. Management has guided that sales are expected to increase by 7-8% due to renovation.

Key conference call highlights

- **Demand momentum expected to continue:** Demand for the footwear category is strong and the company expects portfolio freshness, consumer/market investments, and higher sales on digital platforms to drive consistent revenue growth in the quarters ahead. Further, the company is focusing on improving sales per retail store by restructuring the retail staff per store, improving customer satisfaction, and optimising staff strengths during festivals and key periods. The company is witnessing strong traction for its premium brands and has launched Red Label concept with 2.5x ASP than normal brands to further accelerate this demand.

- **Volume-based growth in the quarters ahead:** In Q2FY2023, revenue grew by 15% over Q2FY2020, with volume growth of 6-7%, while price-led growth stood at 7%. Management targets to achieve volume-based growth in the quarters ahead and has strategies in place to achieve the same.

- **Broad-based growth across categories and brands:** In Q2FY2023, Floatz grew by 132% q-o-q, while Hush Puppies and North-Star were leading categories. In terms of categories, men's dress category continued to lead, while school footwear bounced back strongly. The company launched pilot on men's/ladies open value-added range during the quarter. The mix of open and closed footwear stood at 50:50 in Q2 and management indicated that the mix varies as per the season.

- **Increased footfalls driven by marketing investments:** The company continued its marketing investments and conducted regional campaigns, which focused on festivities leading to better customer engagement. Bata's continuous investment in marketing drove retail footfall and online sessions and led to higher orders. The company witnesses increased traction in Hush Puppies ladies category, resulting in higher share. Advertisement expenses for the quarter stood at 2.5% of sales. Management has stated that the company targets to increase the spends to 3% of sales.

- **Digital channel continued growth momentum:** The digital business achieved its highest revenue during the quarter. Sales through digitally enabled channels continued its momentum, driven by levers such as D2C bata.in e-store, marketplaces, and omnichannel home delivery and contributed 11% to total sales in Q2FY2023. The e-commerce channel reported y-o-y growth of 1.5x in Q2FY2023. During the quarter, complaints on e-commerce fell to 5.1%. Women category's contribution grew by 1.3X y-o-y, while Sneaker sales grew by 126% y-o-y.
- **Other expenses higher in Q2 due to multiple reasons:** In Q2FY2023, other expenses were higher by 62% y-o-y due to normalisation of rent expenses and higher investments towards brands. Management has guided that as the channels start gaining momentum, they would start providing benefit and aid in reducing the costs.
- **EBIDTA margin to improve ahead:** Bata's EBITDA margin stood lower compared to pre-COVID levels. The company is focusing on variabilisation of the cost (including employee cost), improved product mix to high-margin products, increased contribution of sales through franchisee stores, and various cost-efficiency measures to improve margins in the coming years. Management has indicated that company-level margins are impacted by the channel mix and Bata aims to improve margins at the channel level. Management targets to cross pre-covid level margins in the medium term.

Results (Standalone) **Rs cr**

Particulars	Q2FY23	Q2FY22	y-o-y (%)	Q1FY23	q-o-q (%)
Revenue	**829.8**	**614.1**	**35.1**	**943.0**	**-12.0**
COGS	373.5	289.4	29.1	409.1	-8.7
Employee expenses	107.0	89.7	19.4	104.8	2.1
Other expenses	188.2	116.0	62.3	184.4	2.1
Total expenses	668.8	495.0	35.1	698.3	-4.2
Operating profit	**160.9**	**119.1**	**35.1**	**244.7**	**-34.2**
Other Income	11.9	11.5	3.6	9.3	27.7
EBITDA	172.8	130.6	32.3	254.0	-32.0
Interest expenses	27.2	22.0	23.7	24.9	9.1
Depreciation & Amortization	73.6	58.6	25.6	69.3	6.1
PBT	72.1	50.0	44.0	159.7	-54.9
Tax	17.2	13.0	32.8	40.4	-57.3
Reported PAT	**54.8**	**37.0**	**48.0**	**119.4**	**-54.1**
EPS (Rs.)	4.3	2.9	48.0	9.3	-54.1
			bps		bps
GPM (%)	55.0	52.9	210	56.6	-163
OPM (%)	19.4	19.4	0	25.9	-655
NPM (%)	6.6	6.0	57	12.7	-605
Tax rate (%)	23.9	25.9	-202	25.3	-135

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Long-term growth prospects 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 severely affected by COVID-led lockdown in FY2021. FY2022 was volatile as the second and third waves of COVID-19 affected demand, but a rapid vaccination programme and dropping cases helped in recovery. In the near term, demand is expected to be subdued owing to continued extraordinary inflation hitting consumers' discretionary spends. However, low per capita consumption at 1.7 pairs per annum, footwear now being considered as an important fashion accessory rather than a necessity, growing trend of premiumisation in the Indian footwear industry, and the shift to branded footwear provide a huge opportunity for top brands to scale up operations in the medium-long 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 - Strong growth expected in FY2023

Bata delivered strong performance in H1FY2023, registering revenue growth of 2x y-o-y and a sharp improvement in EBITDA margin from 9.7% in H1FY2022 to 22.9% in H1FY2023 on a low base of last year. The company has been focusing on increasing its omnichannel presence and adding relevant products to its portfolio to drive demand in the near term. Demand for the footwear category is strong and the company is banking on portfolio freshness, consumer/market investments (advertising and promotional spends as a % of sales stood at 2.5% of revenue in Q2) and higher sales on the digital platform to drive consistent revenue growth in the quarters ahead. Further, the company is focusing on improving sales per retail store through restructuring the retail staff per store, improving customer satisfaction, and optimising staff strengths during festivals and key periods. Margins are expected to recover in FY2023/FY2024, driven by improving product mix, recovery in retail sales, operating efficiencies, and cost-saving initiatives.

■ Valuation - Maintain Buy with a revised price target of Rs. 2,055

Bata's Q2FY2023 performance was mixed with strong double-digit revenue growth, while EBITDA margin remained flat y-o-y. Management expects growth momentum to continue, aided by growth levers such as casualisation of portfolio, expanding retail footprint through the franchisee route, and scaling up the digital revenue. Profitability is expected to improve going ahead and the company targets to cross pre-COVID level EBITDA margin in the medium term. The stock trades at 57.4x/42.3x its FY2023E/FY2024E EPS and 25.3x/20.4x its FY2023E/FY2024E EV/EBITDA. We maintain our Buy recommendation on the stock with a revised PT of Rs. 2,055.

Peer Comparison

Companies	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Relaxo Footwears	98.4	-	82.0	55.4	64.5	45.5	17.5	13.4	22.0
Bata India	-	57.4	42.3	47.6	25.3	20.4	5.3	12.7	15.6

Source: Company; Sharekhan Research

About company

Bata is the largest footwear retailer in India, offering footwear, accessories, and bags across brands such as Bata, Bata Red Label, Hush Puppies, Naturalizer, Power, Marie Claire, Weinbrenner, North Star, Scholl, Bata Comfit, and Bubble gummers, to name a few. The company has established a leadership position in the industry and is the most-trusted name in branded footwear. The company has a retail network of over 1,950 stores, including 300+ franchised stores, which sell a 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, which will help the company report double-digit revenue growth. With the implementation of GST, there is a shift from unbranded to branded products, providing further scope for Bata in the Rs. 55,000-60,000 crore footwear market in India, of which ~50% is unbranded. To drive growth in the near to medium term, the company has identified certain strategic levers such as the focus on portfolio evolution, accelerating expansion via franchisee and distribution, bringing back marketing investments and getting youth to brand Bata, exploring digital footprint, building an agile and efficient supply chain, and staying nimble on costs in a dynamic environment. We expect the company's revenue and EBITDA to post a CAGR of 24% and 83% over FY2022-FY2025, respectively.

Key Risks

- **Slowdown in discretionary demand:** Any slowdown in SSSG due to a 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
Gunjan Shah	MD and CEO
Vidhya Srinivasan	Director - Finance and CFO
Nitin Bagaria	Company Secretary

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Kotak Mahindra AMC	4.87
2	Aditya Birla Sun Life AMC Ltd.	3.59
3	Axis Asset Management Co. Ltd	3.48
4	Life Insurance Corp of India	2.93
5	Mirae Asset Global Investments	2.69
6	HDFC Life Insurance Co. Ltd.	2.04
7	DSP investment managers Pvt. Ltd.	1.85
8	Nippon Life India Asset Management Company	1.82
9	Vanguard Group Inc.	1.49
10	ICICI Prudential Life Insurance Cof	1.12

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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by BNP PARIBAS

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Compliance Officer: Ms. Binkle Oza; 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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