Relaxo Footwear

Reco: Buy

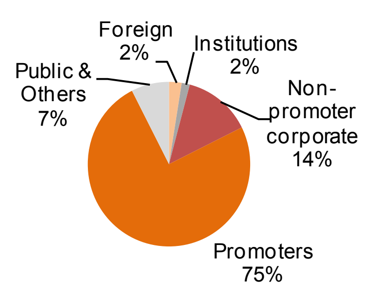
Healthy performance; maintain Buy with PT revised to Rs600

CMP: Rs457

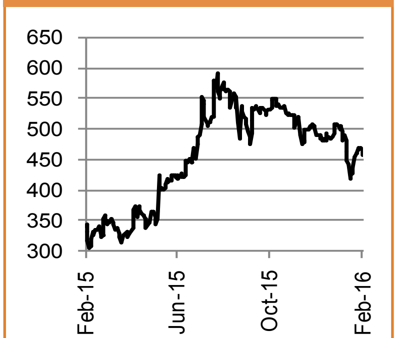
Company details

Price target:	Rs600
Market cap:	Rs5,480 cr
52-week high/low:	Rs614/185
NSE volume: (No of shares)	26,091
BSE code:	530517
NSE code:	RELAXO
Sharekhan code:	RELAXO
Free float: (No of shares)	3.0 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-8.1	-10.0	-16.9	41.8
Relative to Sensex	-3.5	-3.6	-6.4	64.1

Key points

- **Another healthy performance; operating profit up 27.2% YoY:** Relaxo Footwear (Relaxo) posted another quarter of healthy performance, wherein despite challenging times and muted on-ground demand, its top line grew at 16.6% YoY, driven by combination of volume and premiumisation. This double-digit growth is commendable and signifies the strong on-ground execution and brand salience efforts of the company. The growth in the revenue along with falling prices of raw materials (EVA and other chemicals that are crude derivatives) boosted the operating profit margin (OPM) by 116BPS in Q3FY2016, and the OPM stood at all-time high of 14%, driven by a healthy operating performance, the net earnings grew by 22.7% YoY.
- **Favourable industry dynamics coupled with enduring brands to keep financials strong:** With its economical price points (averaging at Rs118-124), the company is well placed to cash in on the transition towards branded shoes from the unorganised segment. We, thus, expect the company to post 20% revenue CAGR over FY2015-18. Further, the initiatives to improve efficiency and rationalise cost along with low raw material prices are likely to culminate into a healthy 29.7% earnings growth (CAGR) over FY2015-18. We have slightly moderated our revenue growth estimates for the company for FY2017 and FY2018. We expect Relaxo to post 21% growth for both the years, as against our earlier estimate of 22% growth.
- **Strong brands, focused management; maintain Buy:** Relaxo's strong presence in the lucrative mid-priced footwear segment (through its top-of-the-mind recall brands like *Hawaii*, *Flite* and *Sparx*) along with its integrated manufacturing set-up, lean working capital requirement and vigilant management puts it in a sweet spot to cash in on the strong growth opportunity unfolding in the footwear category due to a shift from unbranded to branded products. Thus, we remain positive on the stock with our price target revised to Rs600 (Rs635 previously).

Results Rs cr

Particulars	Q3FY16	Q3FY15	YoY (%)	Q2FY16	QoQ (%)
Net revenues	**387.7**	**332.5**	**16.6**	**386.3**	**0.4**
COGs	161.0	140.3	14.7	158.9	1.3
Sales (%)	40.8	42.2		40.8	
Staff cost	37.9	32.0	18.7	36.4	4.1
Sales (%)	9.8	9.6		9.4	3.8
Other expenses	134.6	117.6	14.4	139.9	-3.8
Sales (%)	34.7	35.4	-	36.2	
Total expenses	**333.5**	**289.9**	**15.0**	**335.2**	**-0.5**
Operating profit	**54.2**	**42.6**	**27.2**	**51.1**	**6.0**
OPM (%)	**14.0**	**12.8**	**116BPS**	**13.2**	**75BPS**
Interest expenses	6.3	4.3	44.5	5.8	8.0
Depreciation & amortisation	**12.2**	**9.8**	**24.2**	**11.4**	**6.4**
PBT	**36.2**	**29.0**	**24.9**	**39.1**	**-7.3**
Tax	11.8	9.1	29.8	12.0	-1.6
Reported PAT	**24.4**	**19.9**	**22.7**	**27.1**	**-9.8**
Adjusted PAT	**24.4**	**19.9**	**22.7**	**24.1**	**1.2**

Valuations Rs cr

Particulars	FY14	FY15	FY16E	FY17E	FY18E
Net sales	1,205.8	1,472.8	1,765.4	2,135.4	2,583.0
Change (%)	20.0	22.1	19.9	21.0	21.0
Operating profit	146.6	200.4	254.2	316.0	384.9
Change (%)	33.5	36.7	26.8	24.3	21.8
OPM (%)	12.2	13.6	14.4	14.8	14.9
Net earnings	65.6	103.1	133.3	173.4	219.1
Change (%)	46.5	57.0	29.3	30.1	26.3
Diluted EPS	5.5	8.6	11.1	14.5	18.3
PER (x)	84.3	53.7	41.5	31.9	25.3
EV/EBITDA	38.3	28.7	22.5	17.6	14.2
RoCE (%)	23.3	25.1	26.0	27.0	27.2
RoE (%)	20.4	23.4	22.2	21.8	24.2

Earnings highlights

Revenue growth aided by volume and realisation growth: In Q3FY2016, Relaxo posted a healthy revenue growth of 16.6% year on year (YoY), aided by both volume and realisation growth. This double-digit growth coming in an environment of muted consumer demand is commendable and signifies the growing brand salience of its brands along with its strong on-ground execution. The company would remain focused on consumers with the introduction of value-added and premium products under each of its brands. The newly launched flip flop range, Bahamas, has received a decent response from the market.

Soft raw material pricing led to robust margin expansion: Product mix premiumisation along with falling prices of raw materials (EVA and other chemicals that are crude derivatives) was reflected as a reduction in the raw material cost, which declined by 140 basis points (BPS) YoY. The effect of these benefits was visible in strong improvement in the OPM. Consequently, the OPM expanded by 116BPS YoY and was at 14% for the quarter.

Reported net earnings grew healthily at 22.7% YoY: Led by a strong operational performance the reported net earnings grew by a strong 22.7% YoY.

Key developments

- The company's foray into modern trade through institutional sales and online shopping access to customers to boost sales and have a presence in all trade options are yielding positive results.
- The company has already amicably settled the long drawn litigation on its brand Sparx with Bata India, adding further momentum to the growth as Sparx is one of the most promising brands in its portfolio with strong revenue and margin growth potential ahead.
- To keep pace with the strong growth momentum, the company is looking to augment its capacity for which plans are on the drawing board stage. The company has purchased a land parcel in Rajasthan (Bhilwara) at a cost of Rs48 crore for the project.
- Its key raw materials, ethylene vinyl acetate (EVA) and other chemicals, are crude derivatives and hence follow crude cycle with a lag effect. Prices of EVA have been ruling at 15-17% lower YoY and are currently trading at around Rs120 per kg as against Rs140-145 a kg a year ago. The management believes that apart from crude, the demand supply dynamics for EVA play an important role in determining the prices, and the prices have largely bottomed with minimal scope for further downside.

We expect revenues to grow at 20.6% over FY2015-18: Relaxo's product presence in the economy category and mid-priced category along with its integrated manufacturing set-up puts it in a sweet spot to cash in on the emerging consumer transition from the unorganised to the organised segment, capturing the benefits at all levels. We expect Relaxo to significantly outperform the industry growth rates led by both volume and realisation growth. We, thus, expect Relaxo to grow its revenues at a compounded annual growth rate (CAGR) of 20.6% over FY2015-18.

Net earnings to grow at 29.7% CAGR over FY2015-18E: A robust revenue growth, low prices of raw materials (rubber, EVA), the management's stiff eye on cost rationalisation and efficiency improvement along with efforts to weed out the loss-making stores are likely to have a positive effect on the margins of the company. We expect Relaxo's OPM to further expand hereon and reach 15% by FY2018. The net earnings are expected to grow at a 29.7% CAGR over FY2015-18. We have retained our positive stance on the stock due to its structural growth story. We have also retained our Buy rating on it with a revised price target of Rs600 (valued at 33x its FY2018E earnings).