



Titan Industries

STOCK INFO.	BLOOMBERG
BSE SENSEX: 14,356	TTAN IN
	REUTERS CODE
S&P CNX: 4,333	TITN.BO

31 July 2008

Neutral

Previous Recommendation: Neutral

Rs1,127

Equity Shares (m)	42.3
52-Week Range	1,795/692
1,6,12 Rel. Perf. (%)	7/10/6
M.Cap. (Rs b)	47.6
M.Cap. (US\$ b)	1.1

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
03/07A	20,902	1,158	26.5	21.0	42.5	14.5	35.4	29.7	2.4	23.8
03/08A	29,937	1,483	33.9	27.6	33.3	10.8	33.8	29.3	1.7	20.7
03/09E	38,921	1,930	43.5	28.5	25.9	8.2	33.2	36.1	1.3	15.4
03/10E	47,269	2,547	57.4	31.9	19.6	6.2	33.1	38.3	1.0	12.0

- ✦ Titan Industries has posted better than expected results for 1QFY09, with PAT growing 79% YoY to Rs322m (against our estimate of Rs211m). Net sales grew 23.2% YoY to Rs8.1b (v/s our estimate of Rs8.5b). Gross margins expanded 80bp while EBITDA margins were 130bp higher due to decline in labor and advertising cost. Adjusted PAT increased 79% YoY; tax rate declined 240bp.
- ✦ The Watches division reported a sedate 1.8% increase in sales to Rs1.72b. PBIT increased 54% to Rs170m, as margins expanded 340bp. We believe that watch volumes have shown a YoY decline in 1QFY09. The Jewelry business reported 32% increase in sales to Rs6.1b; gold prices increased by an estimated 35%. Sales growth being lower than the increase in gold prices despite the addition of 9 new stores indicates a decline in same store volumes. Profit margin has been propped up by increase in making charges and Rs20m gains from inventory. Adjusted margin expansion was 15bp.
- ✦ Precision Engineering reported sales of Rs80m in 1QFY09 v/s Rs110m in 1QFY08 and losses continued. Titan Eye+ (including *Fastrack* sunglasses) achieved sales of Rs150m. We expect increase in competition due to the entry of more retailers in this vertical.
- ✦ **Outlook – challenging times ahead; maintain Neutral:** Titan has reported negative volume growth in both Watches and Jewelry after sustained growth over the past few years. We expect volume growth to remain subdued in the event of slowdown in the economy. The company has aggressive store expansion plans, which could hurt margins in this economic environment. We have an EPS estimate of Rs43.5 for FY09 and Rs57.4 for FY10. These estimates do not factor in any impact of slowdown in consumer demand. The stock trades at 25.9x FY09E and 19.6x FY10E earnings. We maintain **Neutral**.

QUARTERLY PERFORMANCE

Y/E MARCH	FY08				FY09				FY08	FY09E
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE		
Net Sales	6,575	7,114	8,024	8,225	8,103	9,413	10,750	10,655	29,937	38,921
YoY Change (%)	49.1	35.9	51.6	37.9	23.2	32.3	34.0	29.5	43.2	30.0
Total Exp	6,206	6,318	7,523	7,487	7,543	8,395	10,090	9,738	27,533	35,766
EBITDA	369	797	501	738	561	1,018	660	917	2,404	3,156
Margins (%)	5.6	11.2	6.2	9.0	6.9	10.8	6.1	8.6	8.0	8.1
Depreciation	72	72	74	79	77	84	88	95	297	344
Interest	48	39	51	63	52	43	44	32	201	172
Other Income	5	4	5	4	8	9	12	12	18	41
PBT	254	689	381	600	440	900	540	802	1,923	2,681
Tax	74	199	72	95	117	270	147	216	440	751
Rate (%)	29.1	28.9	19.0	15.8	26.7	30.0	27.2	27.0	22.9	28.0
Adjusted PAT	180	490	308	505	322	630	393	585	1,483	1,930
YoY Change (%)	158.5	43.1	4.2	6.2	79.1	28.7	27.4	15.9	25.3	30.2
Extraordinary Income	-54	-27	0	100	0	0	0	0	20	0
Reported PAT	126	463	308	605	322	630	393	585	1,503	1,930

E: MOST Estimates

Margin expansion in Watches boosts profits

Titan Industries has posted better than expected results for 1QFY09, with PAT growing 79% YoY to Rs322m (against our estimate of Rs211m). Net sales grew 23.2% YoY to Rs8.1b (v/s our estimate of Rs8.5b). Gross margins expanded 80bp while EBITDA margins were 130bp higher due to 90bp decline in labor cost and 20bp decline in advertising cost. The company shifted to lower duration advertisements to counter media inflation. EBITDA grew 52% YoY while adjusted PAT increased 79% YoY; tax rate declined 240bp.

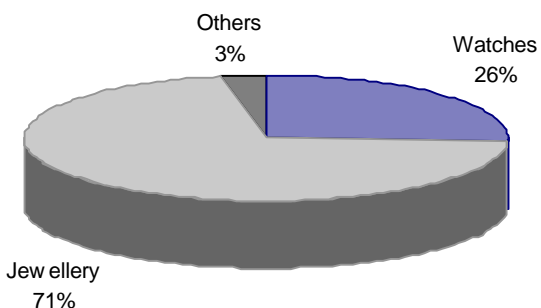
Margin expansion was aided by strong performance in the Watches segment. Watches PBIT margins expanded 340bp YoY to 9.9% on better sales mix. Jewellery contributed 76% of sales in 1QFY09, up from 66.7% in FY08 and 71% in 1QFY08 due to low growth in Watches.

SEGMENTAL BREAKUP (RS M)

	1QFY09	1QFY08	FY08	FY07
Sales				
Watches	1,719	1,688	9,187	7,838
Growth (%)	2	14	17	20
Jewellery	6,157	4,664	20,280	12,920
Growth (%)	32	62	57	63
Others	235	227	960	627
Growth (%)	4	67	53	69
PBIT				
Watches	170	110	1,280	1,074
Growth (%)	55	-16	19	3
PBIT Margin (%)	9.9	6.5	13.9	13.7
Jewellery	355	247	1,057	857
Growth (%)	44	342	23	85
PBIT Margin (%)	5.8	5.3	5.2	6.6
Others	(20)	(27)	(143)	(112)

Source: Company/Motilal Oswal Securities

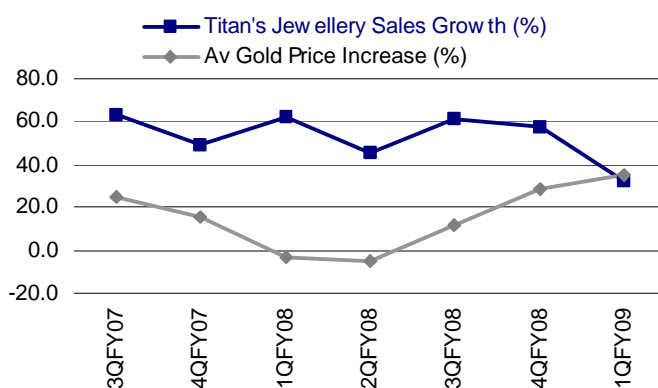
SALES MIX – 1QFY08



Challenging times ahead

Titan is facing a challenging operating environment, in our view. Though the Jewelry division has seen 32% sales growth in 1QFY09, this has been mainly due to higher gold prices. Gold price have increased ~35% YoY in 1QFY09, which implies negative volume growth for Titan’s Jewelry division. The company added 9 new stores – five *Tanishq* and four *Goldplus* outlets – during the quarter. Rising inflation might see some down-trading in lower end watches, which might hurt *Sonata* volumes. Further, its new initiatives – Eyewear and Precision Engineering – might see execution challenges.

HIGH GOLD PRICES IMPACT JEWELRY SALES

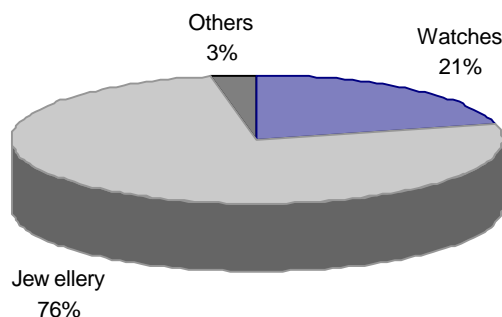


Source: Bloomberg/Motilal Oswal Securities

Watches: volume growth turns negative; richer sales mix boosts PBIT margins

Watches reported a sedate 1.8% increase in sales to Rs1.72b. PBIT grew 54% to Rs170m as margins expanded 340bp. Titan had taken 5% increase in watch prices in April

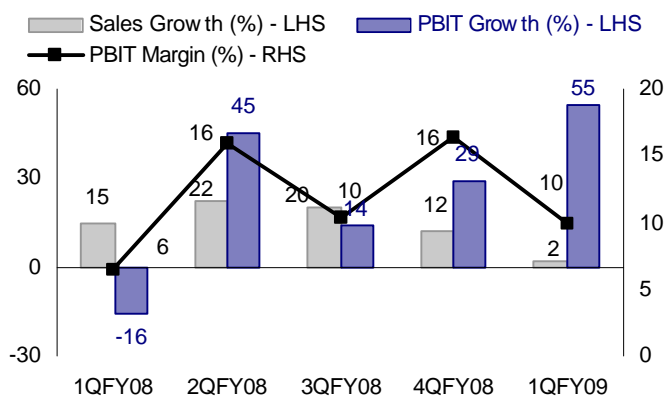
SALES MIX – 1QFY09



Source: Company/Motilal Oswal Securities

to pass on input cost increase. *Sonata* reported volume de-growth, while *Titan* and *Fastrack* brands did well. We estimate that watch volumes have shown YoY decline in 1QFY09. Improved sales mix in Watches has been one of the key contributors to margin expansion. The company has opened 10 World of Titan stores in 1QFY09 and plans to add 100 outlets in the coming 18 months. Sales in the Diwali season would determine the real trend, as the first quarter represents the slack season.

WATCHES: NEGATIVE VOLUME GROWTH BUT BETTER SALES MIX

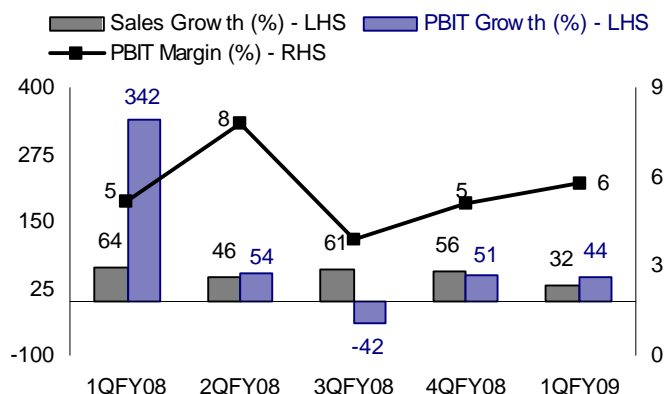


Source: Company/Motilal Oswal Securities

Jewelry: rising gold prices the key concern

The Jewelry business reported 32% increase in sales to Rs6.1b. PBIT increased 44% to Rs355m, as margins expanded 50bp. We estimate 35% increase in average gold prices in 1QFY09 YoY, implying negative volume growth. The number of *Goldplus* outlets has increased from 20 to 24 and this format contributed 10% to sales. *Tanishq* has added five boutiques, taking the total to 112. Given the strong ramp-up in store additions, we estimate a decline in same store volume growth in 1QFY09. 22-carat gold jewelry has shown decline in volume growth. Profit margin has been propped up by increase in making charges and Rs20m gains from inventory. Adjusted for these, margin expansion is 15bp. We believe that consistent increase in gold prices could adversely impact the company’s volume and profit growth in the coming quarters.

JEWELRY: SALES GROWTH DRIVEN BY INCREASE IN GOLD PRICE



Source: Company/Motilal Oswal Securities

Precision Engineering reports lower sales; losses sustain

Precision Engineering reported sales of Rs80m in 1QFY09 v/s Rs110m in 1QFY08 due to delay in the dispatch of one machine worth Rs40m. The business continued to make losses due to slow pick up in sales. Slowdown in automotive sales in developed countries could de-rail the projected growth trajectory, in our view.

Titan Eye+ ramp up ahead of schedule; execution risks ahead

The company intends to increase the number of Titan Eye+ outlets from 10 to 60 in the current year and to 300 in the coming three years. This division (including *Fastrack* sunglasses) achieved sales of Rs150m in 1QFY09. We expect heightened competitive activity, as more retailers are warming up to this concept. After Titan, Reliance Retail seems to be in the fray and Odyssey (100% subsidiary of Deccan Chronicle Holdings) has also opened “The Eyewear Store” in its pilot launch. Entry of other players will expand the market; however, Titan would not have the huge first mover advantage in this business vertical as it has had in other formats. We believe that fast expansion would pose execution risks and expect higher losses in the coming couple of years.

Outlook – challenging times ahead; maintain Neutral

Titan has reported negative volume growth in both Watches and Jewelry after sustained growth over the past few years. We expect volume growth to remain subdued in the event of slowdown in the economy. The company has aggressive

store expansion plans, which could hurt margins in this economic environment. We have an EPS estimate of Rs43.5 for FY09 and Rs57.4 for FY10. These estimates do not factor in any impact of slowdown in consumer demand. The stock trades at 25.9x FY09E and 19.6x FY10E earnings. We maintain **Neutral**.

Titan Industries: an investment profile

Company description

Titan Industries is a joint venture between Tata Group and TIDCO (Tamilnadu Industrial Development Corporation). The company is the largest specialty retailer and market leader in branded watches and jewellery products in India. The company has also been able to tap the fast growing demand for accessories and precision engineering components. Major brands of the company include Titan, Tanishq, Sonata, and Fastrack.

Key investment arguments

- ✍ Titan Inds has a 50% market share in branded jewellery market. Strong growth and low penetration of branded jewellery will result in rising profit margins.
- ✍ Watches are expected to report steady growth due to strong brands and huge success of Sonata.
- ✍ Only company in this sector generating free cash flows.

Key investment risks

- ✍ Consistent increase in gold prices could adversely impact the company's volume and profit growth
- ✍ Slower than expected ramp up in the precision engineering business.
- ✍ Longer than expected breakeven time for new retail stores.

Recent developments

- ✍ The company added 9 new stores – five *Tanishq* and four *Goldplus*.
- ✍ The company has opened 10 World of Titan stores.

Valuation and view

- ✍ We estimate EPS of Rs43.5 for FY09 and Rs57.4 for FY10.
- ✍ The stock is trading at 25.9x FY09E EPS and 19.6x FY10E EPS. We maintain **Neutral**.

Sector view

- ✍ We are positive on the retail sector. We expect the sector to clock a revenue growth of 30-35% CAGR over the next five years.
- ✍ Players with a strong hypermarket format and presence in larger number of categories are likely to be bigger winners.
- ✍ Ability to increase private labels, squeeze costs and extract higher margins from branded players will be a key factor in maintaining margins in the long term.

COMPARATIVE VALUATIONS

		TITAN	PANTALOON	SHOPPERS
P/E (x)	FY09E	25.9	24.8	104.0
	FY10E	19.6	16.7	30.1
EV/EBITDA (x)	FY09E	15.4	10.8	12.5
	FY10E	12.0	7.4	8.2
EV/Sales (x)	FY09E	1.3	0.9	0.8
	FY10E	1.0	0.6	0.6
P/BV (x)	FY09E	8.2	3.5	3.5
	FY10E	6.2	2.1	3.3

SHAREHOLDING PATTERN (%)

	JUN-08	MAR-08	JUN-07
Promoter	53.1	53.1	53.1
Domestic Inst	5.9	3.0	1.5
Foreign	11.5	12.8	12.9
Others	29.6	31.1	32.5

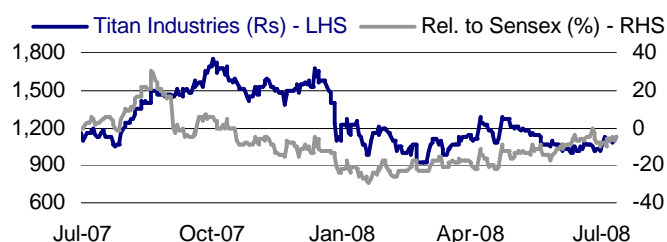
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY09	43.5	44.9	-3.1
FY10	57.4	59.9	-4.1

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
1,127	1,147	1.8	Neutral

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT					
(RS MILLION)					
Y/E MARCH	2006	2007	2008	2009E	2010E
Net Sales	14,369	20,902	29,937	38,921	47,269
Change (%)	310	45.5	43.2	30.0	214
Total Expenditure	-12,761	-18,817	-27,533	-35,766	-43,225
EBITDA	1,608	2,085	2,404	3,156	4,043
Change (%)	25.8	29.7	5.3	31.3	28.1
Margin (%)	11.2	10.0	8.0	8.1	8.6
Depreciation	-197	-256	-297	-344	-369
Int. and Fin. Charges	-248	-204	-201	-172	-120
Other Income - Recurring	24	32	18	41	84
Deferred Revenue Expenc	-101	-101	0	0	0
Profit before Taxes	1,086	1,556	1,923	2,681	3,638
Change (%)	65.0	43.3	23.5	39.4	35.7
Margin (%)	7.6	7.4	6.4	6.9	7.7
Tax	-179	-370	-367	-863	-1,255
Deferred Tax	56	-29	-73	113	164
Tax Rate (%)	-114	-25.6	-22.9	-28.0	-30.0
Profit after Taxes	963	1,158	1,483	1,930	2,547
Change (%)	58.3	20.3	28.0	30.2	31.9
Margin (%)	6.7	5.5	5.0	5.0	5.4
Extraordinary Items	-250	-240	20	0	0
Reported PAT	713	918	1,503	1,930	2,547

BALANCE SHEET					
(RS MILLION)					
Y/E MARCH	2006	2007	2008	2009E	2010E
Share Capital	423	444	444	444	444
Preference Share Capital	400	0	0	0	0
Reserves	1,470	2,831	3,950	5,372	7,248
Net Worth	2,293	3,274	4,394	5,816	7,692
Loans	2,679	2,470	2,609	1,728	1,578
Deferred Tax	238	174	254	367	531
Capital Employed	5,210	5,919	7,257	7,911	9,801
Gross Block	4,204	5,155	5,721	6,247	6,781
Less: Accum. Depn.	-2,440	-2,643	-2,899	-3,180	-3,486
Net Fixed Assets	1,765	2,511	2,822	3,067	3,294
Intangibles		588	525	462	399
Capital WIP	196	160	30	30	30
Investments	270	270	270	270	1,752
Curr. Assets, L&A	6,468	8,858	11,226	13,976	16,561
Inventory	3,744	6,775	8,387	10,379	12,120
Account Receivables	901	921	1,638	2,169	2,632
Cash and Bank Balance	383	507	481	609	880
Others	1,440	655	720	820	929
Curr. Liab. and Prov.	3,599	5,923	7,617	9,894	12,236
Account Payables	2,932	4,586	6,387	8,458	10,529
Other Liabilities	426	864	518	524	531
Provisions	241	472	712	912	1,176
Net Current Assets	2,869	2,935	3,609	4,082	4,326
Miscellaneous Expenditur	110	42	0	0	0
Application of Funds	5,210	5,919	7,257	7,911	9,801

E: MOST Estimates

RATIOS					
Y/E MARCH	2006	2007	2008E	2009E	2010E
Basic (Rs)					
EPS	21.9	26.5	33.9	43.5	57.4
Cash EPS	26.6	32.9	40.1	52.3	67.5
BV/Share	54.2	77.5	103.9	137.6	182.0
DPS	4.0	7.4	7.6	9.8	12.9
Payout %	18.3	27.8	22.5	22.5	22.5
Valuation (x)					
P/E		42.5	33.3	25.9	19.6
Cash P/E		34.2	28.1	21.5	16.7
EV/Sales		2.4	1.7	1.3	1.0
EV/EBITDA		23.8	20.7	15.4	12.0
P/BV		14.5	10.8	8.2	6.2
Dividend Yield (%)		0.7	0.7	0.9	1.1
Return Ratios (%)					
RoE	42.0	35.4	33.8	33.2	33.1
RoCE	25.6	29.7	29.3	36.1	38.3
Working Capital Ratios					
Debtor (Days)	23	16	20	20	20
Asset Turnover (x)	2.8	3.5	4.1	4.9	4.8
Leverage Ratio					
Debt/Equity (x)	12	0.8	0.6	0.3	0.2

CASH FLOW STATEMENT					
(RS MILLION)					
Y/E MARCH	2006	2007	2008E	2009E	2009E
OP/(loss) before Tax	1,411	1,830	2,107	2,811	3,674
Int./Div. Received	24	32	18	41	84
Depreciation and Amort.	197	256	297	344	369
Interest Paid	-248	-204	-201	-172	-120
Direct Taxes Paid	-179	-370	-367	-863	-1,255
(Incr)/Decr in WC	56	58	-701	-345	28
CF from Operations	1,261	1,602	1,152	1,817	2,781
Extraordinary Items	-250	-240	20	0	0
(Incr)/Decr in FA	-301	-915	-437	-526	-534
(Pur)/Sale of Investments	0	0	0	0	-1,482
CF from Invest.	-551	-1,155	-417	-526	-2,016
Issue of Shares	0	21	0	0	0
Incr/(Decr) in Debt	-503	-209	139	-880	-150
Dividend Paid	-169	-311	-322	-414	-546
Others	-97	176	-578	131	203
CF from Fin. Activity	-769	-323	-761	-1,163	-493
Incr/Decr of Cash	-59	124	-26	128	272
Add: Opening Balance	442	383	507	481	609
Closing Balance	383	507	481	609	880

N O T E S



For more copies or other information, contact

Institutional: Navin Agarwal. **Retail:** Manish Shah

Phone: (91-22) 39825500 Fax: (91-22) 22885038. E-mail: inquire@motilaloswal.com

Motilal Oswal Securities Ltd, 3rd Floor, Hoechst House, Nariman Point, Mumbai 400 021

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Disclosure of Interest Statement

Titan Industries

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|---|----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
| 4. Investment Banking relationship with company covered | No |

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