2011

VANTAGE SECURITIES

Titan Industries Ltd

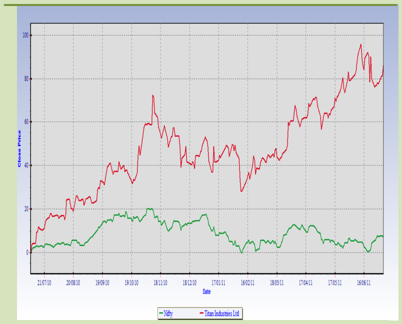
Industry – Retail

CMP: ₹224
Target Price: ₹225
Potential upside: 0%

Titan Industries Ltd

NEUTRAL

Relative Performance



Source: Capital Line

Stock Data

No. of shares	: 888mn
Market Cap	: 198.9bn
52 week high	: ₹238
52 week low	: ₹205
TTM P/E	: 46.7x
Bloomberg code	: TTAN IN
Reuter's code	: TITN.BO

Shareholding (%) March 2011

Promoters	: 53.49%
FIIs	: 9.73%
MFs/UTI	: 9.37%
Others	: 27.41%

Performance Table

Month	Stock	Nifty
1 month	2.3%	1.2%
6 month	31%	-4.7%
12 month	86.7%	7.3%

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Under penetration levels in Watches and Jewellery segments of biz

The total estimated market size of the Indian Watch industry in 2009-10 was to the tune of ₹ 35bn. India is an under-penetrated market for watches with only 27 % of Indians owning a watch and only 3.5% of the country's total population owning multiple watches. In terms of volumes, the organized players currently command 40% of the industry market share (~46mn units annually) and the balance 60% is held by the unorganized segment. According to CARE the total size of the jewellery market in India is estimated at $22 bn with branded jewellery comprising a paltry 10% out of the total market. This presents a huge opportunity to TIL in expanding rapidly in both its core business segments going ahead.

Large Distribution Network a perfect connect with Retail consumers

TIL has more than 8,10,000 sq.ft of retail space spanning across business divisions and with a distribution network spread amongst more than 11,000 dealers across 250 towns. TIL is also planning a capex of ₹1500-2000 mn in FY12 to expand its existing network of stores. TIL had 311 World of Titan stores which accounted for more than 40%+ of the total sales in the watches segment in FY11 and it plans to increase them to 350 by FY12. In the Eyewear segment TIL is in an investment mode and is expected to rapidly increase the network (from the current 150 stores) by 100 stores in FY12E. Its vast distribution network would act as a strong entry barrier for new players entry in these markets.

Strong Brand Equity

TIL has 65% & 40% market share in the organized watches and branded jewellery segments respectively which have been predominantly controlled by the unorganized sector. Inspite of this the majority share still lies with the unorganized sector which presents a tremendous growth opportunity for TIL going ahead. TIL with the backing of TATA brand, its high focus on service & quality, comprehensive product offerings, innovation in designs and transparency, has won customers trust and gained a strong foothold in the highly competitive watches and jewellery markets.

Healthy Financials

TIL has posted a robust 6 year (FY05-11) CAGR of 34.3% in sales, 36.8% in EBITDA and CAGR 41.5% in PAT. The jewellery segment has posted an impressive 5 yr CAGR of ~35% and the watches segment has grown steadily at a 5 yr CAGR of 10%. We expect the watches segment to deliver a 16% CAGR growth from FY11-FY13E with the jewellery segment posting a CAGR of 26% for the same period. We expect the watches division to post PBIT margins of 17% by FY13E, and maintain them going ahead with Jewellery division registering 9% PBIT margins by FY13E on the back of increasing share of diamond studded jewellery in total jewellery sales.

Titan a attractive bet on the Indian Consumer Story: NEUTRAL

The huge potential in the underpenetrated watches and Jewellery segments in India and the dominant positioning of TIL in these areas ensures TIL is well poised to grow at a rapid pace in the years going ahead. At current market price of ₹224 the TIL stock is valued at 34.5x its FY12E EPS of ₹6.5 and 27.7x its FY13E EPS of ₹8.1 We believe TIL can leverage its brand, designing capabilities, large reach, sound and experienced management, strong financials (sustainable margins and high capital return ratios) and favourable macro economics factors to maintain its leadership position in years to come. Our Target Price of ₹225 values the stock at 27.8x its FY13E EPS with a NEUTRAL rating on the stock. Any correction in the stock should be used as a buying opportunity.

Financial Performance -

Year	Net Sales	EBITDA	Rep.PAT	EPS	ROCE
Standalone	**(₹ Mn)**	**(₹ Mn)**	**(₹ Mn)**	**(₹)**	**%**
FY 09	38034	2965	1590	2	36%
FY10	46744	3950	2503	3	45%
FY11	65209	5856	4304	5	64%
FY12E	82899	7878	5731	6	62%
FY13E	98561	9810	7159	8	58%

Source: Vantage Securities

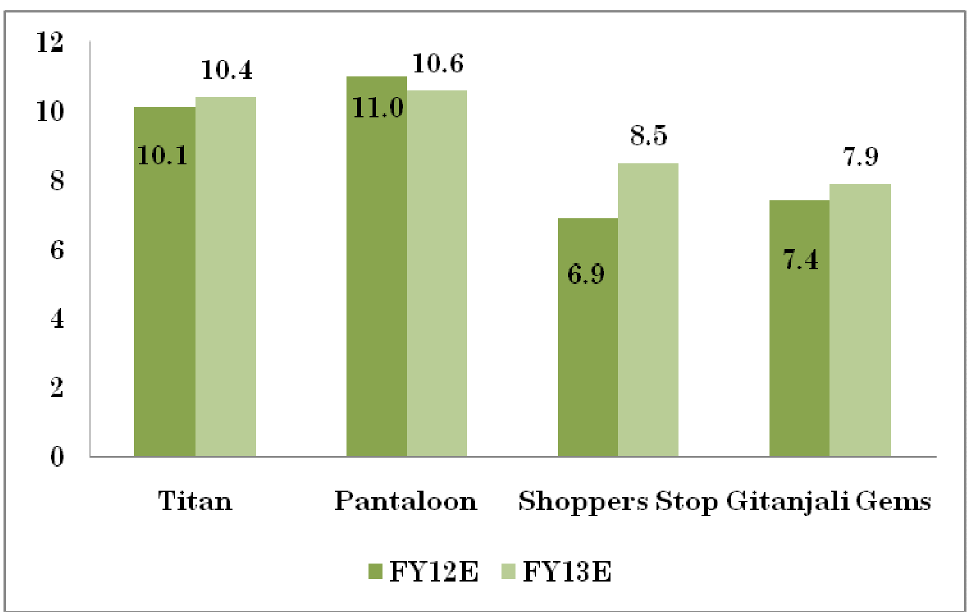
Relative Valuation –

Consolidated Nos	FY 10	FY 11	FY 10	FY 11	FY 09	FY 10
(₹ Mn)	ShoppersStop		Gitanjali Gems		Pantaloon Retail*	
Sales	15,855	24,478	65,276	94,564	76,690	97,869
EBITDA	1,093	1,311	4,391	6,143	5,050	8,198
EBITDA Margin	6.9%	5.4%	6.7%	6.5%	6.6%	8.4%
PAT	359	432	2,002	3,387	97	675
EPS (₹)	10	6	24	42	1	3
PE (x)	46	85	12	7	568	99
ROCE (%)	16	14	10	11	6	9

*Source: Capitaline, * Year ending June*

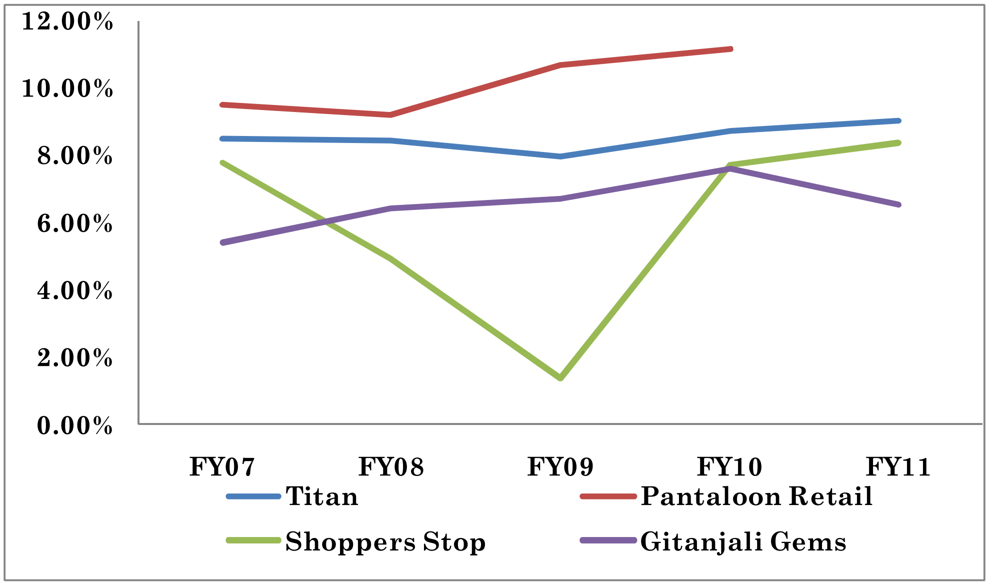
Peer Comparison on Margins and Return Ratio Parameters –

Standalone EBITDA Margins (In %)



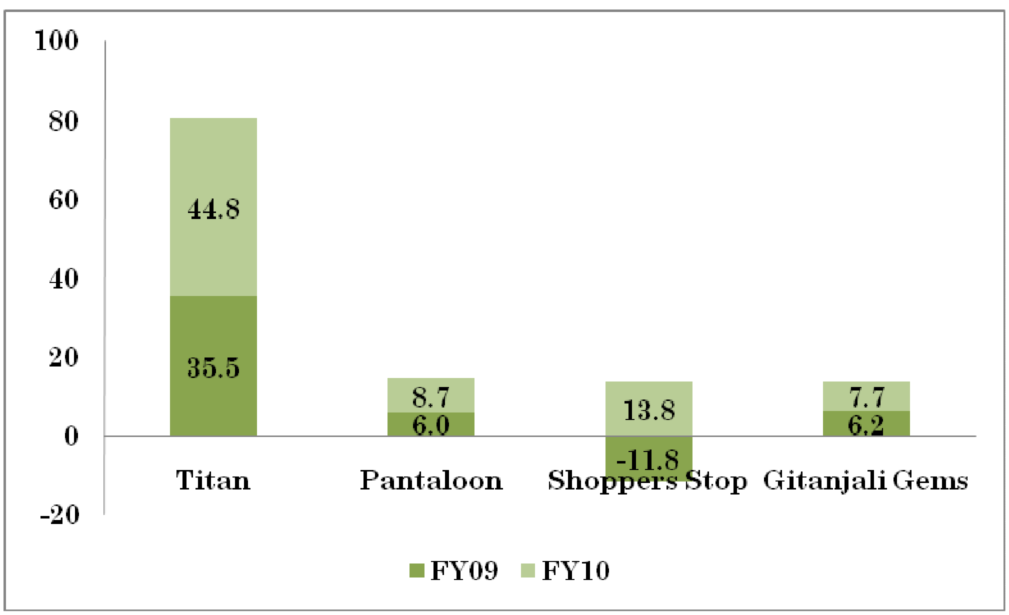
Source: Consensus Estimates and Vantage Securities

Standalone EBITDA Margins (In%)



Source: Capitaline

ROCE (In %)



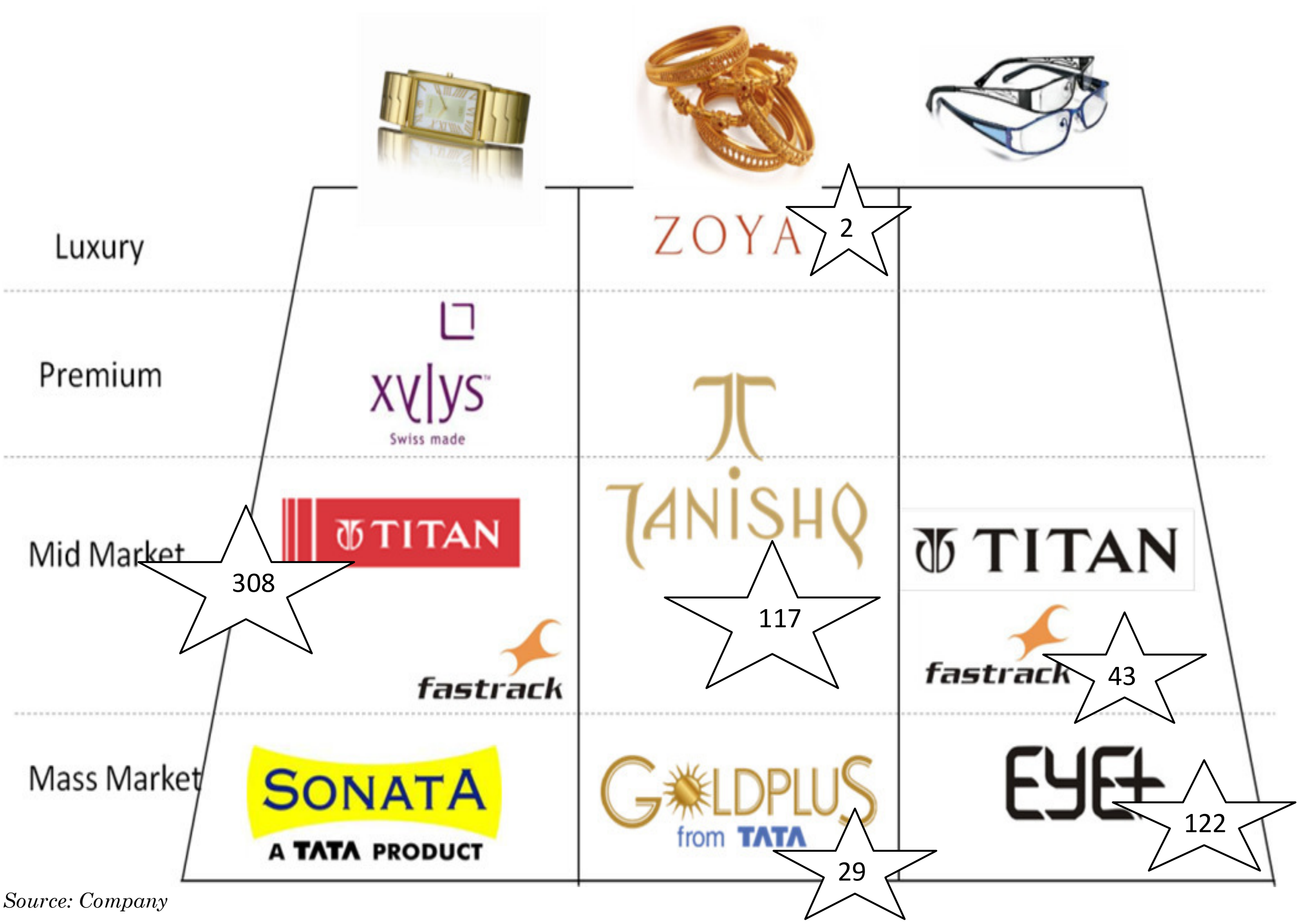
Source: Company and Capitaline

Company Description -

Titan Industries Limited (Titan) was started as a joint venture between the Tata group and Tamil Nadu Industrial Development Corporation in 1984 for manufacturing and marketing of watches. Titan has sold 100 million watches world over and manufactures 12 million watches every year. Titan has also acquired a license to sell premium fashion watches of global brands like Tommy Hilfiger, Hugo Boss, Fcuk, Xylys etc. Titan's business activities are divided predominantly into four business divisions namely Time Products, Jewellery, Eyewear and Precision Engineering. The company diversified into jewellery in 1995, marketing under the brand name Tanishq. Tanishq has gone on to become India's leading branded Jewellery player. Titan Industries has also made its foray into eyewear, launching Fastrack eyewear and sunglasses, as well as prescription eyewear. Titan has leveraged its manufacturing competencies and entered into precision engineering products and machine building.

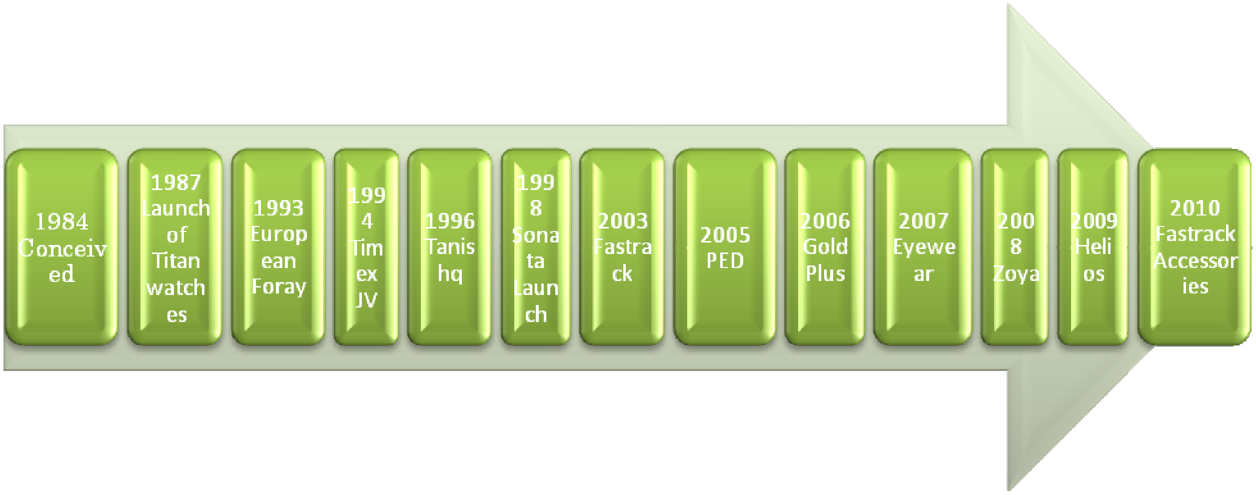
India's Largest Retail Network –

With over 624 retail stores across a carpet area of over 7,70,848 sq. ft. Titan has India's largest retail network with the distribution chain spanning more than 10,000 Multi brand outlets. This retail network has placed Titan amongst World's Top 5 Watch manufacturer's with 65% market share in the organized watch market. The company's Sonata brand is the largest selling watch brand in India. Titan's Titan Eye+ brand also boasts of the largest retail chain in eyewear.



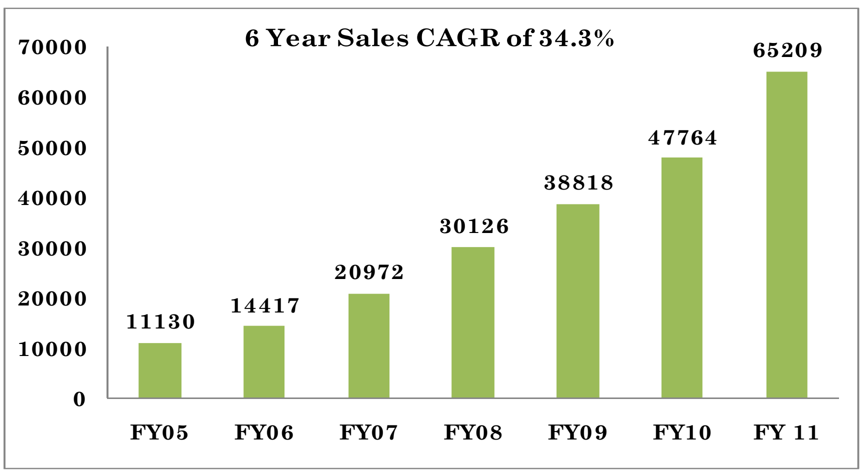
Source: Company

Milestones achieved in GCL's History –



Source: Company

Historical Financial Performance -



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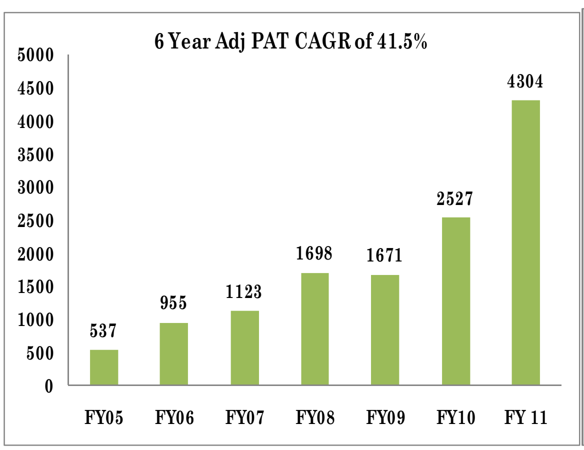
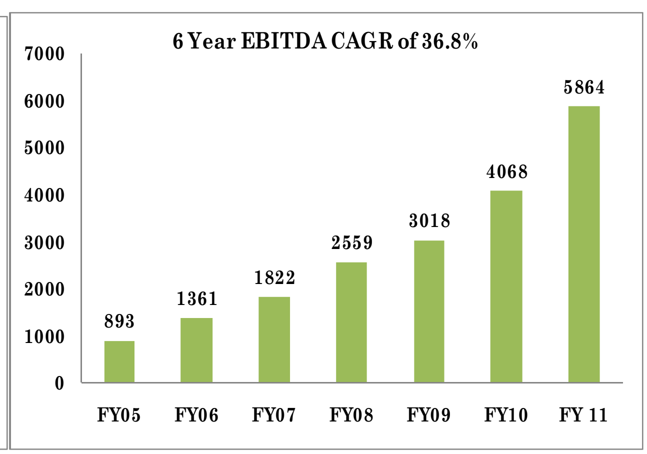




Source: Company

Management Team Profile –

Bhaskar Bhat – Managing Director

Bhaskar Bhat assumed the position of Managing Director of Titan Industries on 1st April 2002.
He is a B.Tech (Mechanical Engineering) degree holder of IIT - Madras, and a post graduate diploma holder in Management from IIM - Ahmedabad.
Most of Bhaskar's working experience has been in Sales & Marketing. Having started his career as a management trainee with Godrej & Boyce Manufacturing Co. in 1983 he moved on after 5 years, and joined the Tata Watch Project (initiated at Tata Press Ltd.)
Since 1983, Bhaskar has been associated with the Tata Watch Project – later to become Titan Watches Ltd., and now Titan Industries Ltd. At Titan, Bhaskar dealt with Sales & Marketing, HR, International Business and various general managerial assignments.
Bhaskar is a member of the Governing Council at the T.A. Pai Management Institute, Manipal and the SDM Institute of Management and Development, Mysore.

Harish Bhat – COO Time Products division

Harish the COO, Time Products Division, Titan Industries, leads the watches business of Titan. Earlier, Harish was COO of the Jewellery Division. Harish is a member of the Tata Administrative Service (T.A.S.). During his tenure with the Tata group, he held several senior portfolios. Harish is an alumnus of BITS Pilani and IIM – Ahmedabad, and has to his credit the IIM - Ahmedabad Gold Medal for Scholastic Excellence (1997), and the Chevening Scholarship for Young Managers, awarded by the British Government. He is currently Secretary General of the All India Federation of Horological Industries.

C.K. Venkataraman - COO Jewellery Products division

Venkataraman has headed the Jewellery Division since January 2005. He is a post graduate diploma holder in Management from IIM – Ahmedabad. Venkataraman joined Titan Industries in 1990, and worked in the Advertising and Marketing functions before becoming the Head of Sales & Marketing for the Titan brand in 2003.

Ravi Kant – COO Eyewear Business & Sr. Vice President Corporate Communications

Mr. S Ravi Kant joined Titan in 1988 in Marketing, with a Masters in Business Management from FMS, Delhi. He soon moved to Retailing and Exports and headed the initiation of the watch assembly plant in Dehradun. Between 1995 and 2005 Ravi headed the Middle East and African operations as MD of Titan International (ME). He subsequently headed the International Business Division of Titan Industries – Bangalore, managing performance of both businesses – watches and jewellery in 30+ countries.

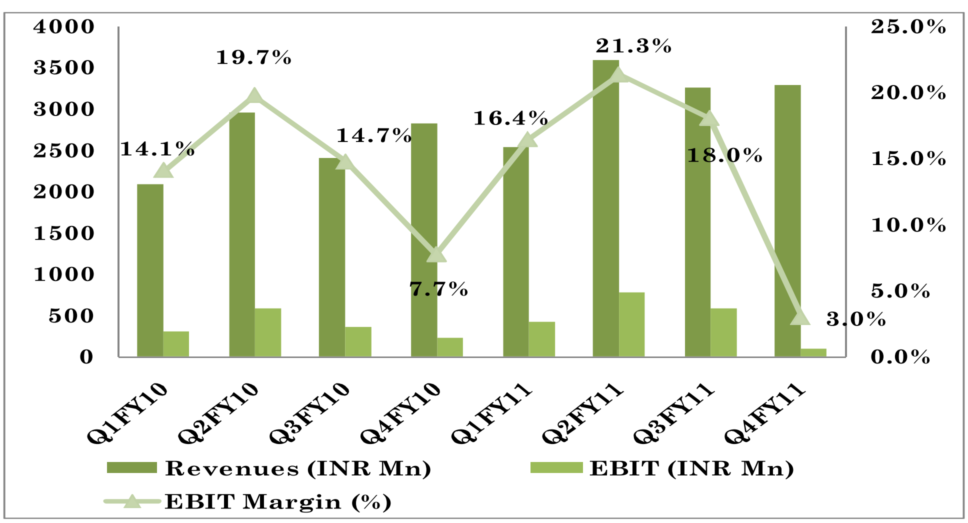
Business Profile of Strategic Business Divisions

Watches Division:-

The Time Products division has placed Titan amongst the world's largest retail networks and earned the company the position of 5th largest integrated watch manufacturer in the world. Titan has a 65% market share in the organized watch market. The four major brands offered by Titan's watch division are: Titan(Mid segment), Sonata (Mass segment), Fastrack (Youth brand), Xylys (Premium segment) and license agreements to sell International brands such as Tommy Hilfiger, Hugo Boss and Fcuk. Titan leverages its vast distribution network of 11,000 dealers across 2500 towns to maintain its brand and market leadership of >50%. Titan's highly rated design studio is the place where the popular watches and eyewear are conceptualized. The design studio serves as a one-stop shop for the design needs of the four brands: Titan, Fastrack, Sonata and Xylys. Titan's watches are sold in India and 26 countries across the world. Titan has garnered 25% volume share and 45% value share of the retail watch market in CY10. The watches segment has contributed ~19% of the total FY11 revenues of the company.

Source: Company

Financial Metrics of the Watches Division - One off Bonus payment done in Q4FY11



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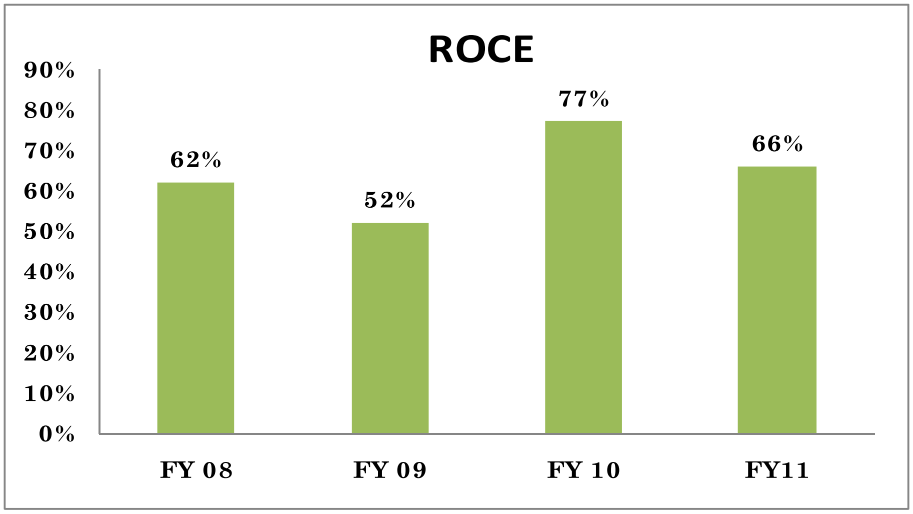

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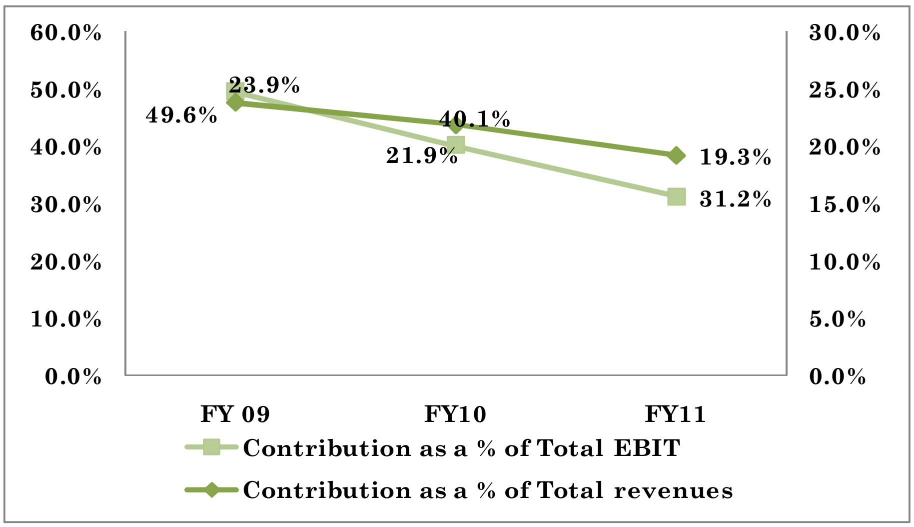
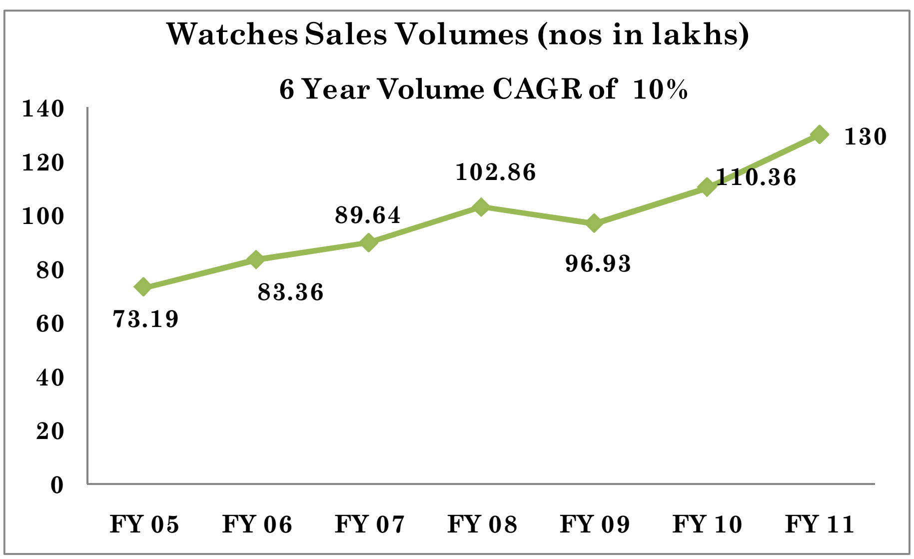


Source: Company and Vantage Securities



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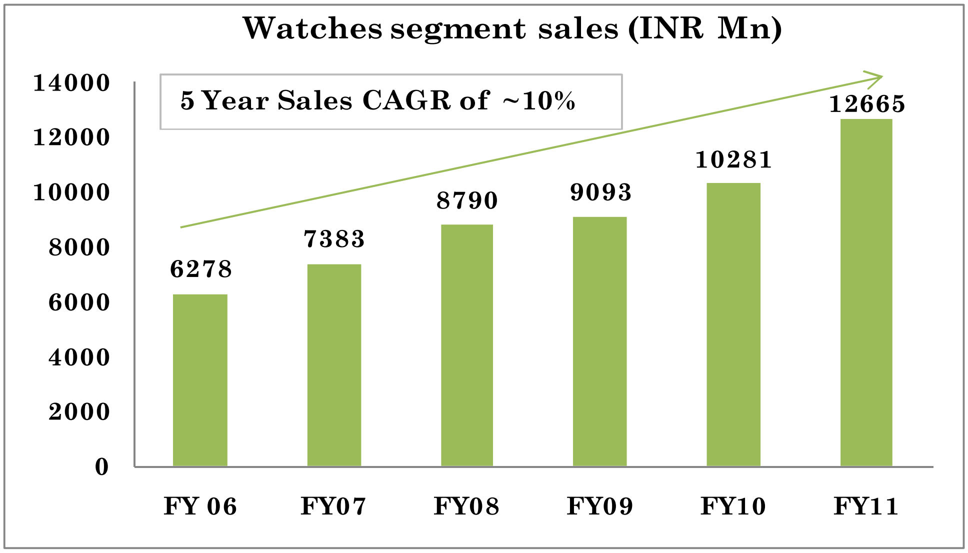
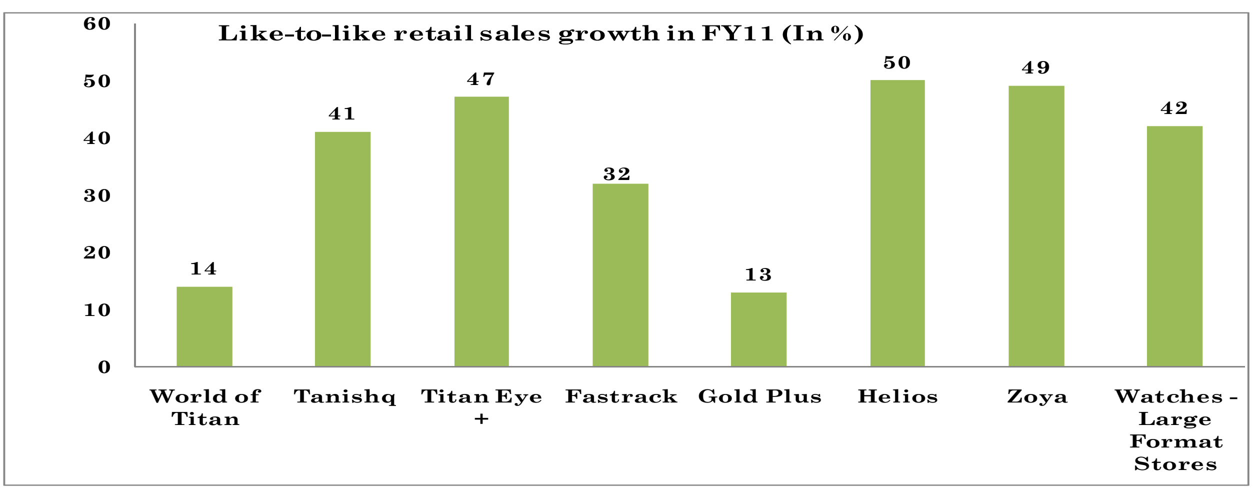


Source: Company

Future Prospects -
We expect the Watches division to post sales CAGR of 15.9% for the period FY11E to FY13E. This would be led by 15.2% CAGR in volumes and increase of ~2.3% in sales realizations (value growth) for FY11E-FY13E and the rest coming from better product mix. For the period ended FY11 the Watches segment has reported 23.3% Y-o-Y value growth which was above the average growth rate of 10% seen in the watches industry. The EBIT margin for the period ended FY11 stood at 14.7% as compared to 14.1% in the corresponding period of the previous year. According to the management it has planned to add 40 stores to its existing number of 311 stores of Titan in FY12E. The company is also focused on adding about 30 stores of Helios and 100 stores of Fastrack for selling its casual range of watches and accessories. Titan will stick to its strategy of new launches (15 to 17 collections in a year are introduced) at higher price points instead of increasing prices for current products as new products are expected to attract consumer attention which would push up the realizations. TIL is seeing robust volume growth of watches in price points above ₹5000 and sees this as an inflexion point in the watches industry. The World of Titan has experienced 14% growth in Sales per square feet of area in FY11 over FY10.

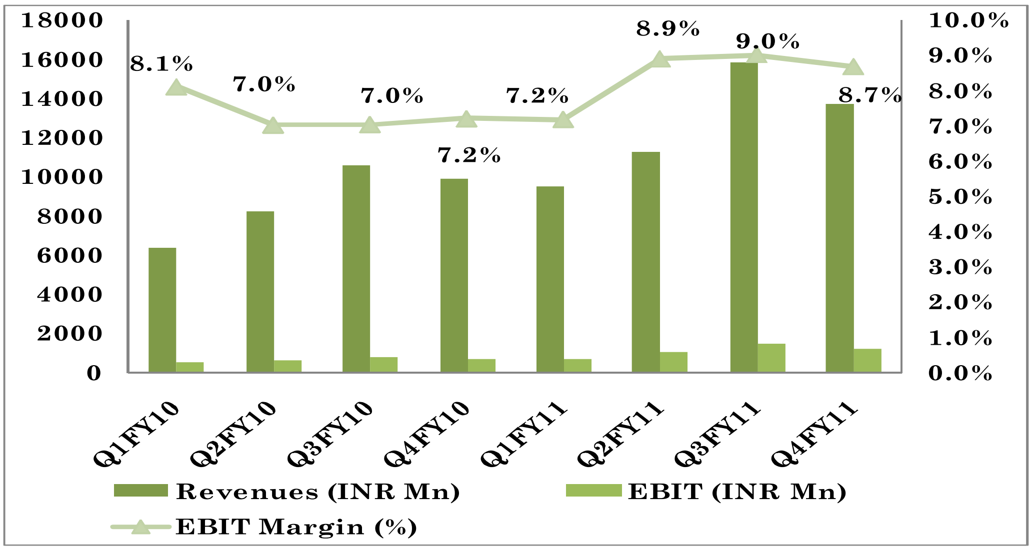


Source: Company

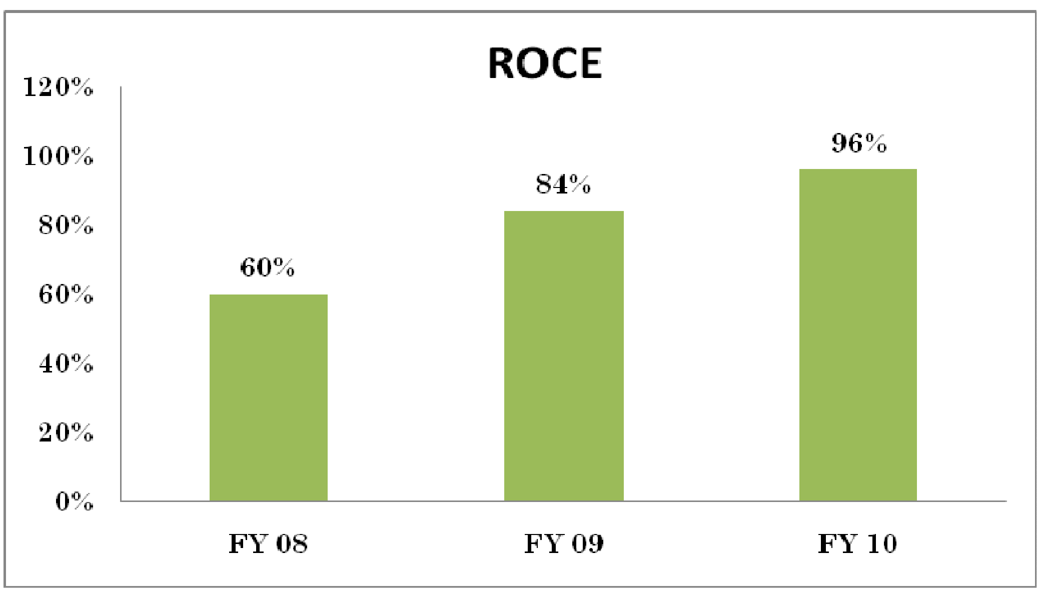
Jewellery Division –

The division contributed ~76% of Titan's total revenues in FY11. Titan's Jewellery division comprises of three major brands Tanshiq, Gold Plus and Zoya. It is the largest jewellery retailer with 120 Tanishq boutiques in 75 towns in prime high-street locations, 29 Gold Plus stores which present an opportunity in the vicinity of over ₹ 300bn and 2 Zoya stores. Subsequently Titan's Tanishq enjoys a market share of ~40% of the branded jewellery segment. It has manufacturing facilities in Hosur and Dehradun. The company has come up with new innovative services such as Golden harvest/future scheme, gift vouchers, gold exchange schemes and made to order facility. It is also running loyalty programmes like Anuttara and Ananta.

Financial Metrics of the Jewellery Division –



Source: Company



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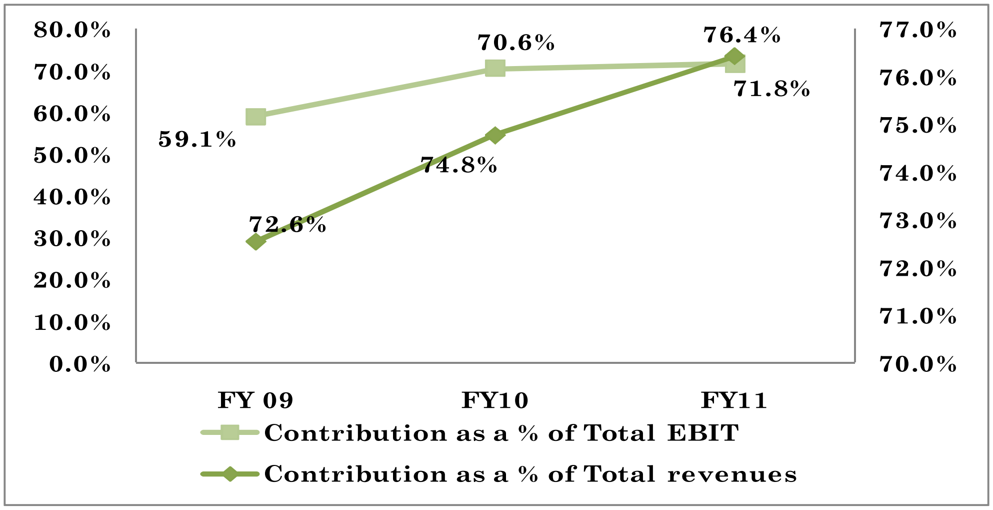
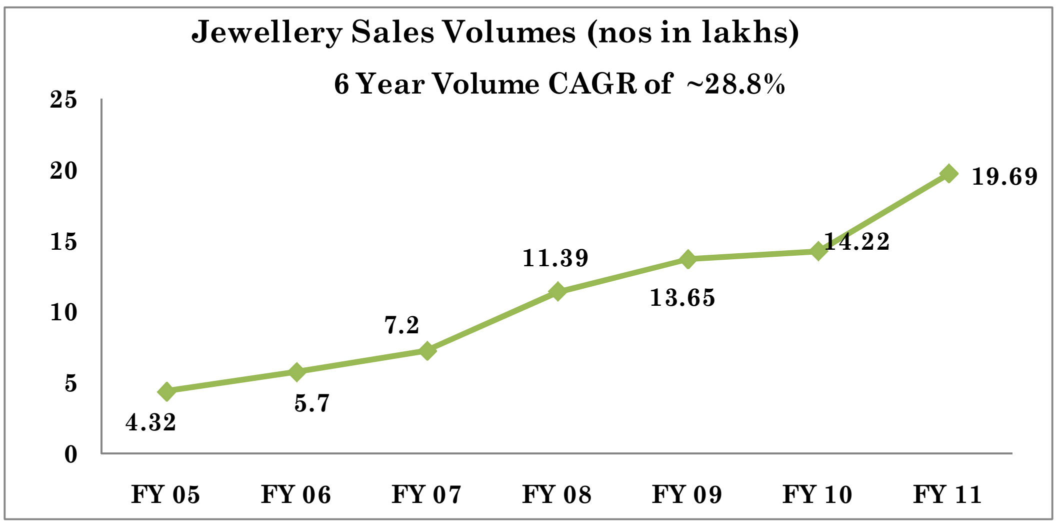


Source: Company and Vantage Securities



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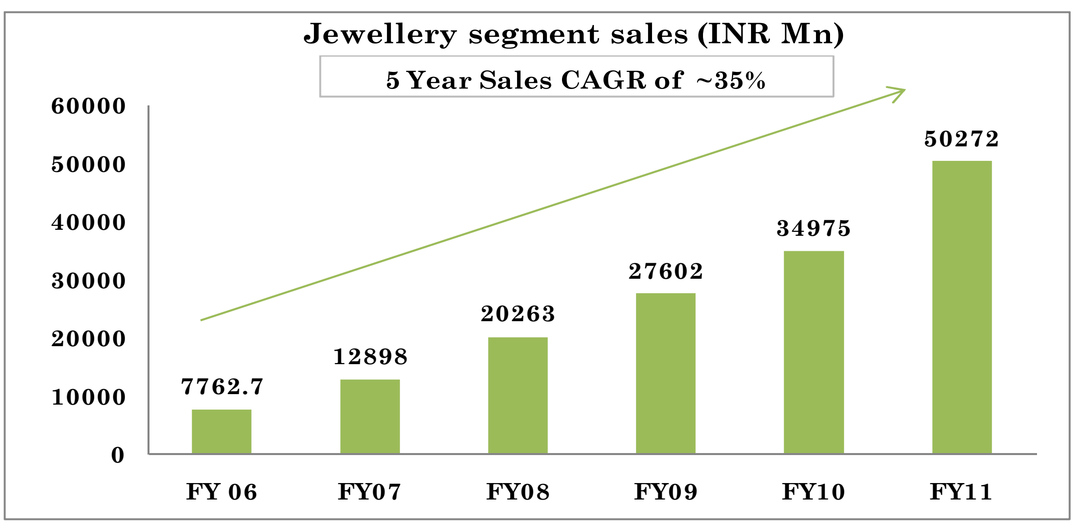
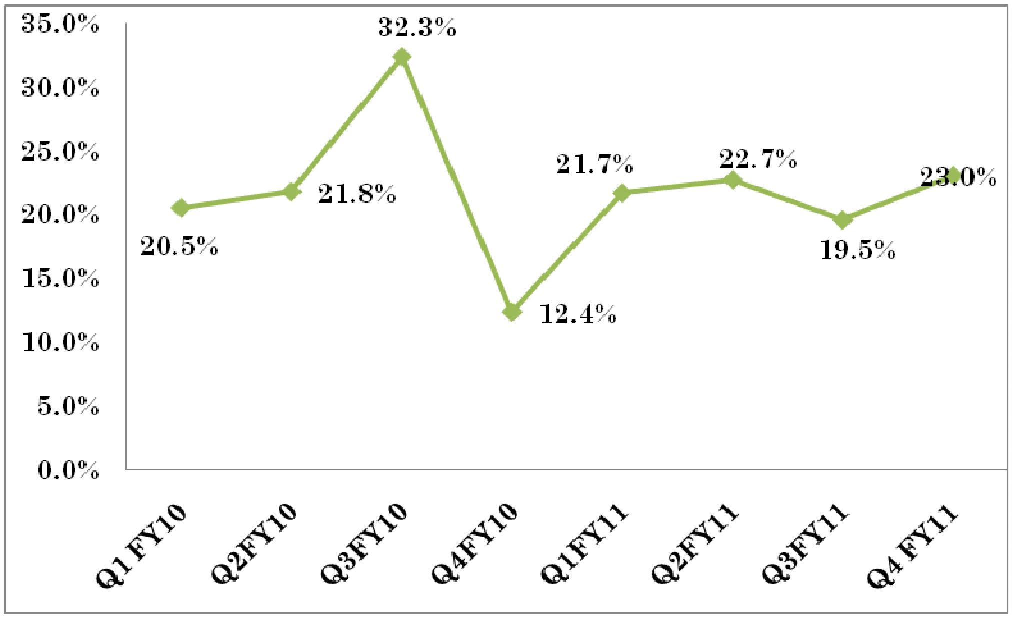


Source: Company

Gold Prices Y-o-Y Growth Increase -



Source: World Gold Council and Vantage Securities

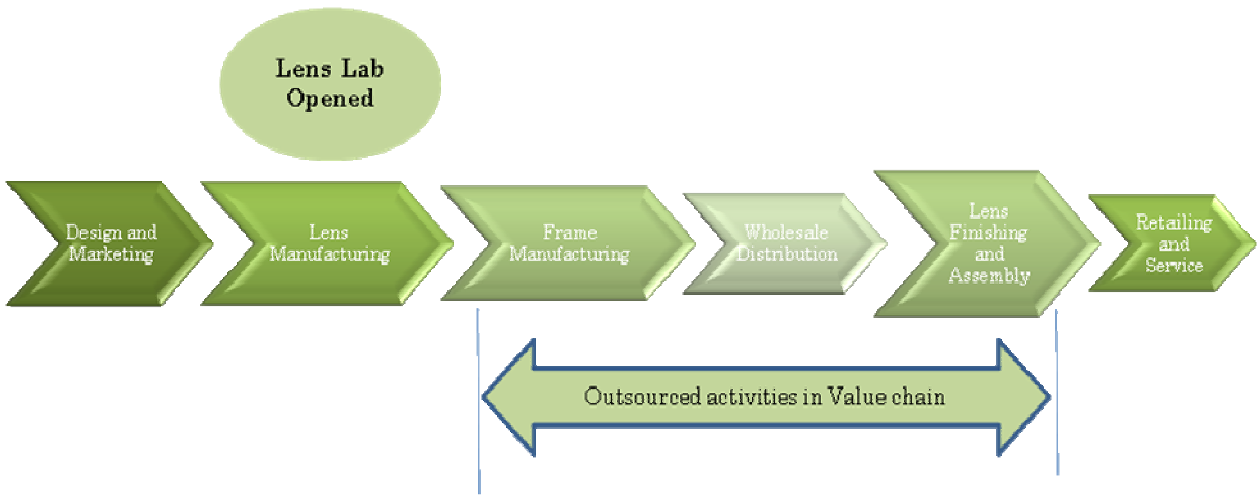
Future Prospects -

We expect the Jewellery division to post sales CAGR of 25.6% for the period FY11E to FY13E. This would be led by 18% CAGR in volumes and increase of ~8% in sales realizations (value growth) for FY11E-FY13E and the rest coming from higher contribution from studded jewellery in the overall segment. For the period ended FY11 the Jewellery segment has reported 43.7% Y-o-Y value growth which was above the average growth rate of 30-40% seen in the Organized Retail Jewellery industry. The EBIT margin for the period ended FY11 stood at 8.5% as compared to 7.3% in the corresponding period of the previous year which was an increase of 120 bps. The same store sales growth is ~20% in the Jewellery segment. Share of studded jewellery continues to rise and currently in FY11 contributes ~27-30%% of total jewellery sales versus 25% in FY10. The shift is beneficial, since studded jewellery has higher margins versus gold jewellery. TIL changed its pricing strategy from fixed making charges by linking them partly with gold prices. This has enabled it to maintain stable operating margins, especially when gold price rises and volumes drop. Interestingly, despite fixed making charges, Titan's profit per gram of gold sold has improved consistently due to improving product mix and higher operating leverage as SSS growth has been robust. According to the management it has planned to add 20 stores to its existing number of 120 stores of Tanishq in FY12E. Titan is also focusing on expanding into Tier II and Tier III cities through its Gold Plus stores. Gold Plus stores are the mass oriented plain vanilla gold stores targeting the middle and lower middle income classes. It plans to add 6-7 stores in FY12E to its existing network of 29 stores. The company has estimated a market size of over ₹ 30bn in the semi-urban and rural areas. Titan will stick to its strategy of new launches at higher price points instead of increasing prices for current products as new products are expected to attract consumer attention which would push up the realizations. The Tanishq and Gold Plus stores have experienced 25% and 10% respective growth in Sales per square feet of area in FY11 over FY10.

Eyewear Division -

Titan has India's largest optical retail chain with 150 stores. It possesses state of the art eye-testing facilities. It has three in-house brands namely Titan, Eye+ and Dash. Its products include frames, sunglasses, contact lenses, ready readers, lens cleaning solutions and other accessories. It also has several International and Luxury brands like Gucci, D&G, Armani, BOSS, Esprit, Daniel Swarowski and Mont Blanc. 30% of population typically needs correction in vision (i.e. ~300mn) with an estimated 84 mn using corrective vision eyewear. The consumers change their eyewear once in 3 to 4 years on an average with repeat purchase a regular feature from adolescence to old age. The market size of the eyewear industry has been estimated to be ~25-35 mn units i.e. to the tune of ₹ 150-180 bn.

Tactical Positioning in the Value Chain by Titan

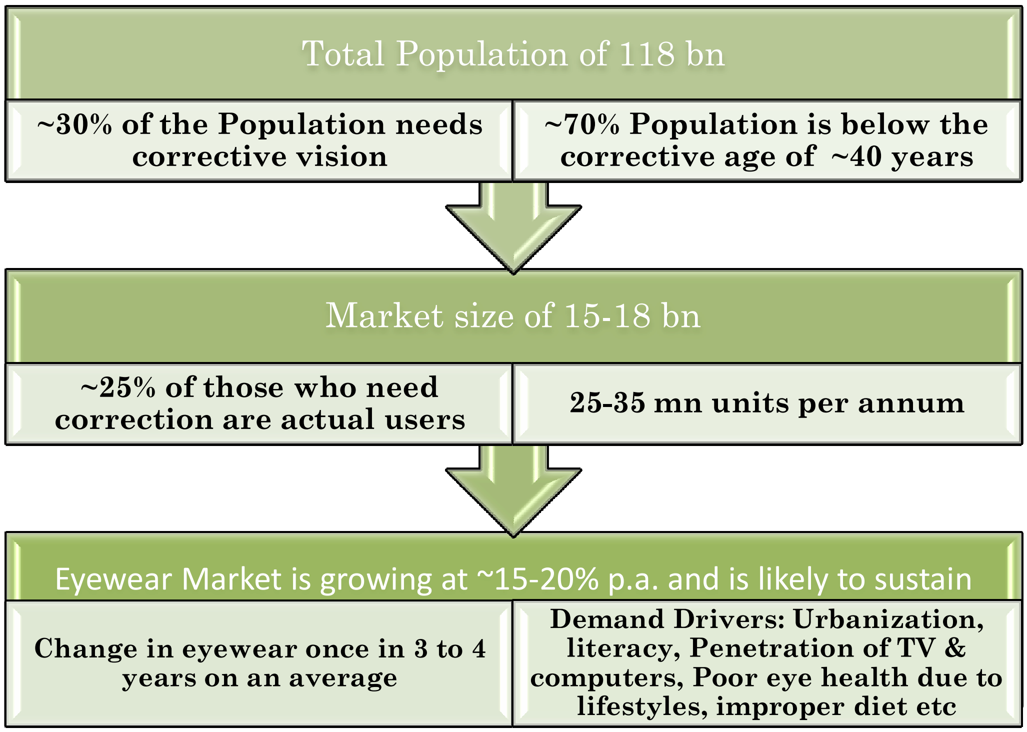


Source: Company

The product or service offering by the Eyewear Division of Titan as a retail brand would be follows:

- Eye checking, Optometry
- Range of frames: Titan & Licensed brands
- Range of branded Lenses
- Sunglasses – Titan, Fastrack and Licensed brands
- Contact Lenses, Accessories

Untapped Potential in the Eyewear Market



Source: Company

Future Prospects -

The Eyewear store expansion is ahead of the company's targets and the SBU is expected to end the year with 150 stores (with 100 stores to be added in FY12) and the breakeven for the business is likely to be achieved by FY13. We are of the view that once the Eyewear division becomes EBIT positive then it would contribute substantially to the company's margins and help valuation re-rating for the company.

Precision Engineering Division (PED) -

The Precision Engineering Division leverages its engineering capabilities and balances the B2C business (i.e. watches, jewellery and eyewear) risks through its B2B business model. India being a $32 bn size global market and growing market catering to industries like Aerospace, Automotive, Oil Exploration & Production, Machine building and Automation business. Titan's clients include Eaton US, Hamilton Sunstrand, Microtechnica, Pratt & Witney, Ford, Bosch, Timken, Visteon, Lucas, Tata Motors, Turbo Energy, Stanadyne, Tyco Electronics etc.

The current market size of Precision components, dash board instruments and sub systems combining the domestic as well as international market is ~₹ 1350bn. The domestic automation solutions market is estimated to be ~₹6bn market size. The PED is not expected to break even on an EBIT level in FY11E.

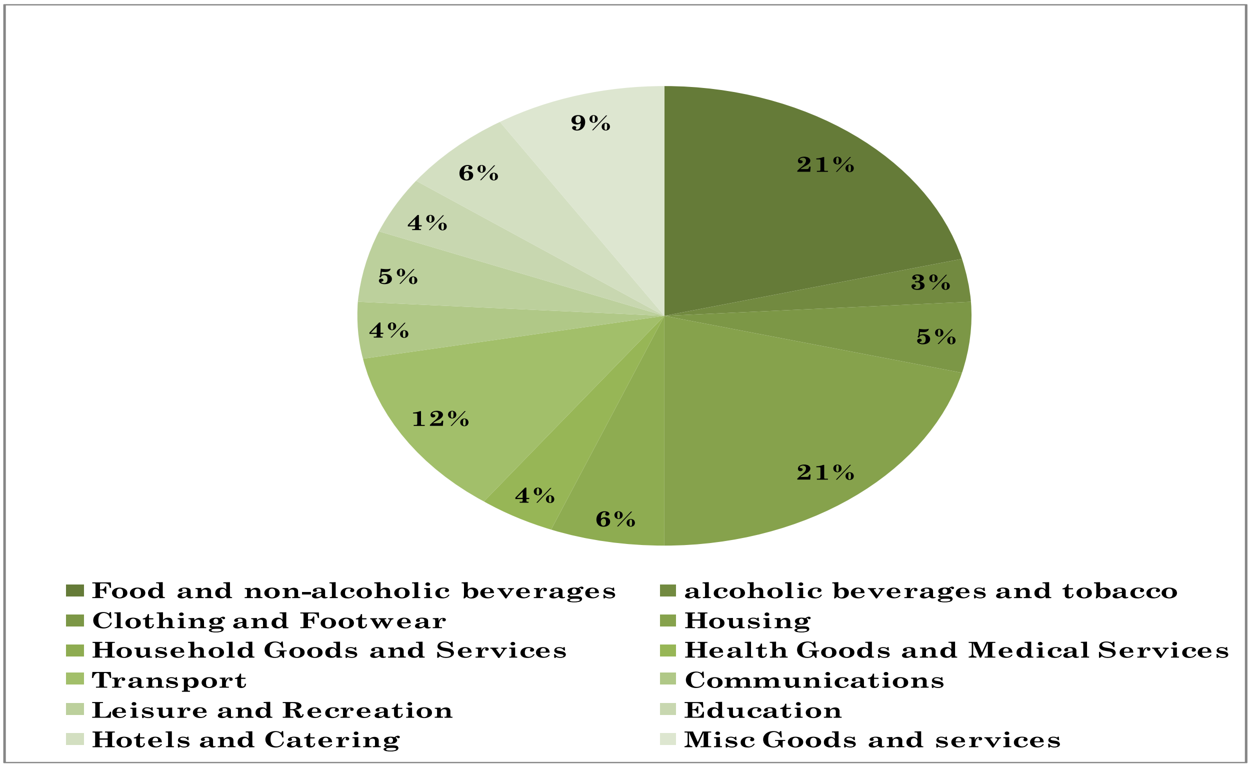
Future Prospects -

During the FY2009-10 the PED was significantly impacted due to the global melt down and the consequent slow down of the Indian manufacturing sector. Hence the revenues from PED dropped by 27% during FY2009-10. With the global markets slowly coming out of the downturn this business division is expected to recover primarily driven by Machine building and Automation.

Industry Description -

The McKinsey Global Institute (MGI) believes India is on the verge of the second greatest urban migration the world has ever seen. MGI sees India's urban population ballooning to 590 mn nearly twice the size of the US by 2030. As the population's discretionary income increases, people tend to use their money to improve living conditions by buying goods or adding utilities to their homes. MGI estimates that the number of Indian households with discretionary spending could jump from just 13 million in 2005 to 89 million by 2025. MGI says discretionary spending will account for 70 percent of consumption growth. The age dependency ratio, which is the ratio of population that is either below or above working age, is expected to shrink from 67.7 percent of the population in 1991 to just over 48 percent of the population by 2025.

Consumer expenditure by sector in 25 key Emerging market economies: 2020



Source: Euromonitor International from national statistical offices/OECD/Eurostat/Euromonitor International
Note: ***Miscellaneous goods and services includes expenditure on personal care, jewellery, silverware, watches and clocks,*** *travel goods, personal effects, social protection, insurance, financial services and other goods and services.*

The key findings from the MGI Report are as follows:

- Indian incomes will triple over the next two decades, significantly reducing poverty.
- India will emerge as the world's fifth largest consumer economy.
- A large urban middle class will develop, but rural areas will benefit too
- Patterns of consumption wills shift rapidly towards discretionary spending
- Income and consumption growth will create opportunities and challenges for business and government

The overall Indian luxury market was valued at around $3.5 billion in 2005-06 annually and is forecasted to expand to $30 billion by 2015, according to a 2010 Mckinsey report with India slated to overtake Germany as the world's fifth-largest consumer market by 2025.
McKinsey data also estimates that while the total population will increase by almost 30 percent between 2005 and 2025, the middle class population will increase by a factor of approximately 10, or almost 1000 percent, during the same period. Over a two-decade period from 2007, India's middle class segment is seen rising from about 5 percent of the population to more than 40 percent.

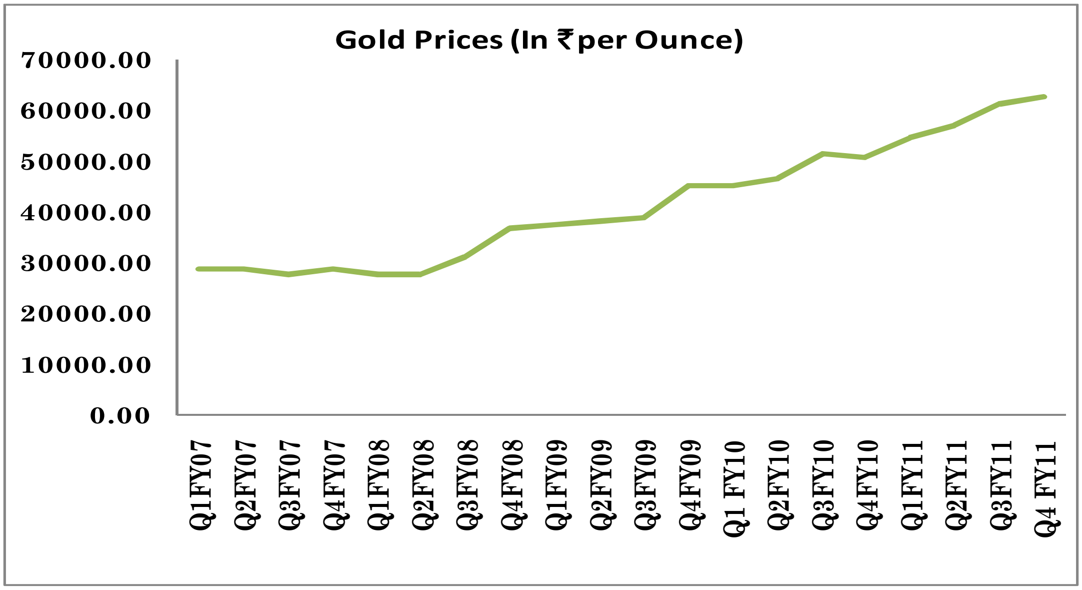
McKinsey estimates that by 2015, the number of consuming class households (earnings $4000 per year) will likely triple to 64 million. Meanwhile, at the top end of the market, there is a continuously expanding number of super-wealthy Indians who are likely to create strong demand for big-ticket items. The number of high net worth individuals grew by as much as 51 percent to 126,700 in 2009 from 84,000 in 2008, according to the 2010 Merrill Lynch-Capgemini World Wealth Report.

Two further elements that are seen providing a boost to growth in India are ongoing urbanization, and the comparative youth of India's population. Currently, only around 30 percent of India's population, or around 300 million people, live in cities, but over the next 20 years, that number is forecast to grow by a further 300 million. The new city-dwellers, inevitably, will adopt the more sophisticated styles and fashions of their neighbours, including jewellery purchases. That is likely to be all the more the case, says McKinsey research, since a large proportion of the new city inhabitants will be in their twenties and with the levels of disposable income necessary to splash out money on jewellery and fashion items.

Jewellery Industry -

The Indian domestic jewellery market is currently worth about $16 billion, according to a report by Credit Analysis and Research Limited (CARE). However, the value of the branded jewellery market in India is estimated at less than 10 percent of the total domestic jewellery market, CARE said. That could be because the domestic jewellery is 96 percent "unorganized", meaning the approximately 300,000 traditional retailers or family-owned businesses with a presence in just one town, while just 4 percent is in the "organized" sector. The CARE report forecasts sales of non-branded jewellery products will grow at around 12 percent annually, with growing numbers of Indians being persuaded to buy due to hallmarking of precious metals and the rising number of certificates being provided with diamonds. The country's organised retail jewellery sector is growing by 30-40% annually, however it still accounts for a measly 3% of the consolidated jewellery retail space, which is estimated at ₹700bn (*Source: Industry Sources*). Meanwhile, the Indian jewellery export sector is growing at around 7 percent annually, and is forecast to reach exports of $23.5 billion by 2012. As a result of the global financial crisis, many jewellery exporters have moved away from the traditional markets such as the United States and Europe to Hong Kong, Australia and Russia. And that has paid off with growth in exports in the first half of the current fiscal of around 10-15 percent.

In addition to Indian brands such as Tanishq, Nakshatra, Gili, Cygnus, Sangini, Asmi, and D'damas, India has also been penetrated by well-know foreign brands, such as Tiffany, Bulgari, Chopard, Cartier, and Harry Winston. Italian brands, such as Damiani and Di Modolo, sell via exclusive boutiques in five-star hotels, while international companies such as Thailand's Pranda Jewelry, and Christian Dior, are also reported to be looking into establishing a presence in the Indian jewellery retail sector.



Source: World Gold Council

The Indian jewellery industry is also changing its approach to the type of jewellery it is manufacturing, taking into account the need to make items that will appeal to young, upwardly mobile people who may not yet be earning salaries that enable them to buy big-ticket items. As a result, the domestic market is seeing more lightweight and highly fashionable designs that fall in a price range that is affordable.

Watches Industry -

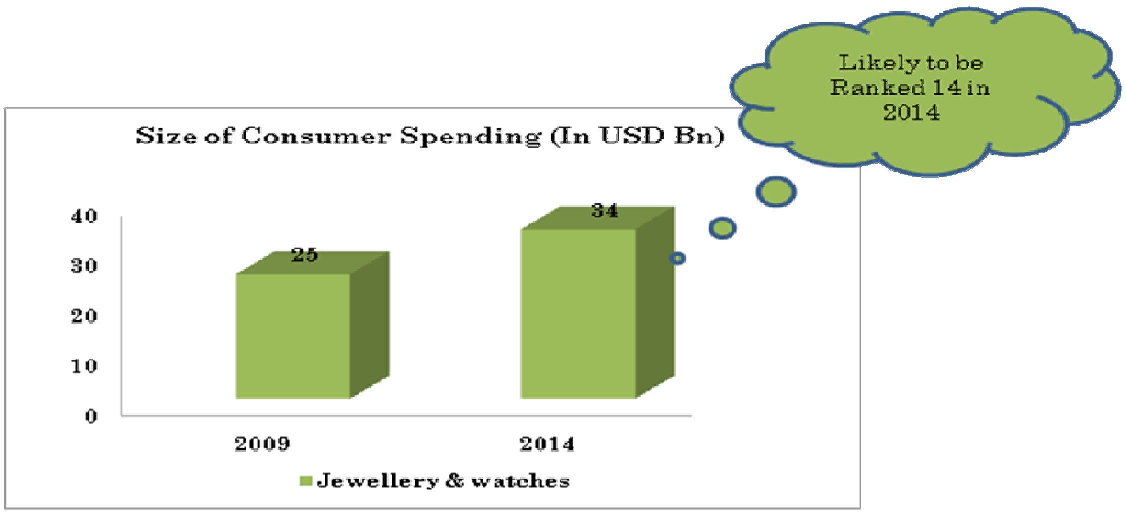
Indian Time Wear Industry 2010 - published by All India Federation of Horological Industries (AIFHI) and consultancy firm Technopak Advisors, the current size of watch market in India is about Rs 40-42bn. According to the report the Indian watch market is set to more than double in the next five years to around Rs 85bn growing at 10-15% every year, driven by youth and premium segment of consumers. India is an under-penetrated market for watches with only 27 % of Indians owning a watch which is amongst the lowest in the world. Only 3.5% of the country's total population owns multiple watches. The vast proportion of the Indian market is below ₹ 500 i.e. $11 which is ~65% of the total volumes and constitute ~24% by value. In terms of volumes, the organized players currently command 40% of the industry (~46mn units annually) and the rest 60% is by the unorganized segment which consists of smuggled watches, cheap imported watches and those assembled by small unorganized players. The market has been split into Low end, Mass market, Premium and Luxury segments. The total estimated market size in 2009-10 was to the tune of ₹ 31bn i.e. a volume of ~44mn units.

The Swatch Group reported sales for 2010 totalling 6.4 billion Swiss Francs ($6.6 billion), an increase at constant exchange rates of 21.8 percent over 2009 and 12.7 percent over 2008. The production segment of the company, which supplies movements and components to third-party watchmakers in Switzerland and around the world, reported an increase of 7.5 percent for the year. The Indian Watch industry has also been estimated to be growing at 10% p.a in volume terms.

Investment Positives

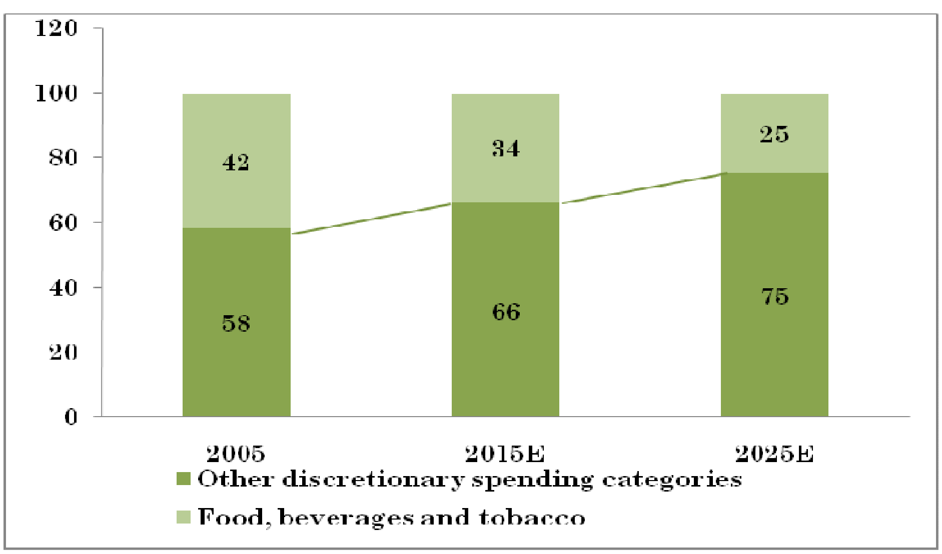
Favourable demographics and consumption patterns of India

We believe Titan being a dominant player in the consumer retail market in India and could be a significant beneficiary of the evolving demographics and changing consumer tastes of the population in India. With rising urbanization the current population of 300mn living in cities is set to add another 300mn in the next 20 years. The new city-dwellers, inevitably, will adopt the more sophisticated styles and fashions of their neighbours, including jewellery purchases. The demographic profile is turning extremely favourable towards sustaining growth in economic activity and in consumption, with almost 550 million consumers across urban and rural India in the 15+ age group.



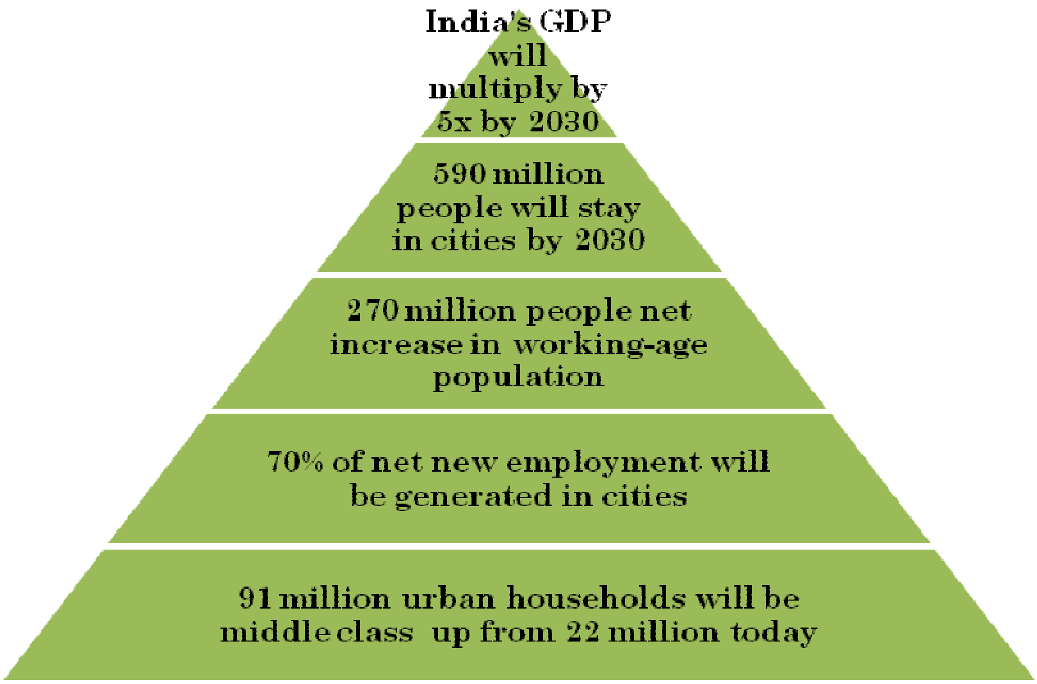
Source: MGI

All India Average Changes in consumer spending on items



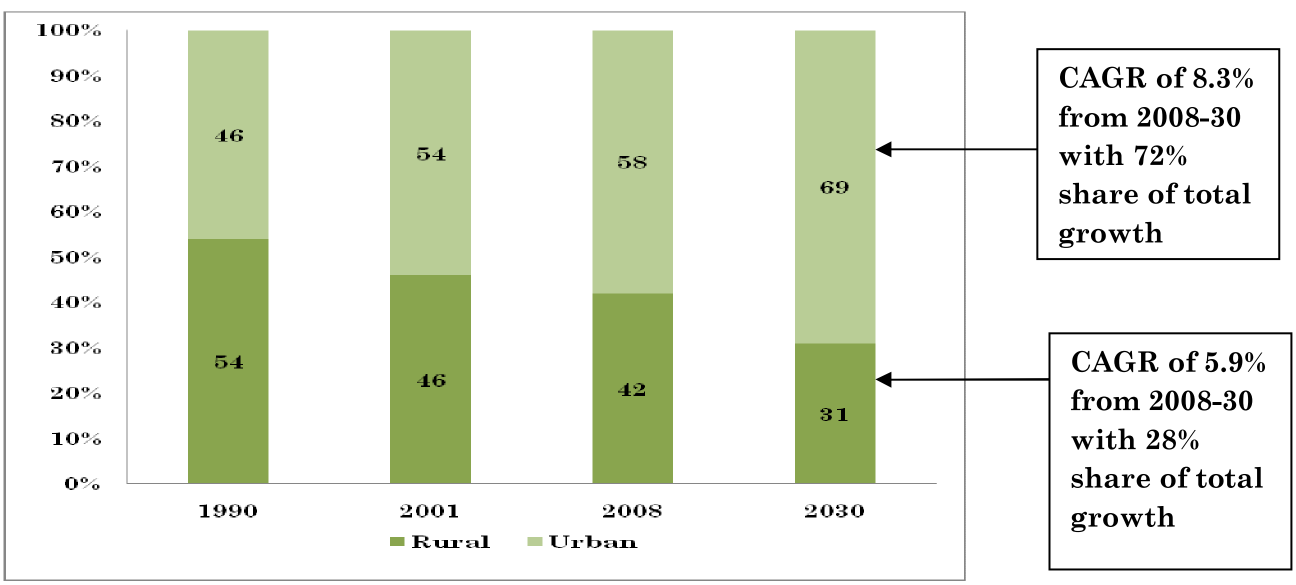
Source: MGI

According to McKinsey Global Institute (MGI), the average household disposable income in India is expected to grow at a 5% CAGR to ₹319,518 in 2010-25E on the back of ~10 times rise in middle class households in 2025E (128 million vs. 13 million households in 2005).
In addition, India is blessed with favourable demographics as the share of working population in the total population is expected to reach ~68% in 2025E (vs. 63% in 2005)



Source: MGI

Cities will account for ~70% of India's GDP by 2030 (₹ Bn)



Source: MGI

We believe Titan is well placed to capitalize on the rising discretionary spends and urbanization levels in India with its strong brand equity, dominant leadership position in the watches, jewellery and eyewear segments and improving geographical reach in Tier II and Tier III cities. Titan also caters to different income groups in the low end to premium end market with its organized retail format stores and could be a significant beneficiary of the rising per capita income of the population in India.
In addition to the in-house brands, Titan stores provide access to popular international brands to its customers in the watches and eyewear segments. These products have higher-than-average margin profile and are typically targeted at premium consumers. We believe Titan will remain the key supplier of these international brands given its large reach in the speciality retail market and strong brand equity. We believe, it will be difficult for any international retailer to replicate the distribution reach and create brand awareness on par with Titan in the near future.

Favourable Product Mix in SBU's to help push up margins going ahead

The Titan management has set itself a target of increasing its share of studded jewellery to 40% in next three years in total jewellery sales. Presently the share of studded jewellery in total jewellery sales is in the range of ~27-29% as against 25% in FY10. This has also elevated the margins to all time high levels of 9% in Q3FY11 and 8.7% in Q4FY11. Margin improvement in watches segment was led by the launch of new collections at higher price points (above ₹5000-₹2.5-3.0 lakhs comprising 65% of the market), a richer sales mix and fewer store additions. The management has stated that 15 to 17 new collections will be launched every year to attract renewed consumer interest which would be instrumental in improving the realizations. The robust business model followed by the company in the Eyewear segment would help it break-even by FY13. The company ended the year FY11 with EBIT margins of 14.7% and 8.5% in the watches and jewellery segments respectively. We expect the company to report EBIT margins of 14.3% and 15.9% in FY12E and FY13E respectively in the watches segment and stable margins of 8.7% and 9.0% in FY12E and FY13E respectively in the jewellery segment.

Segments (₹ Mn)	FY 09	FY 10	FY 11	FY12E	FY13E
Watches	9084.9	10267.8	12664.6	15337.25	17016.23
% of Total	23.9%	21.9%	19.3%	18.4%	17.1%
Watches EBIT	1378.6	1447.3	1862.3	2192.9	2708.4
EBIT Margin (%)	15.2%	14.1%	14.7%	14.3%	15.9%
Jewellery	27632	35041.9	50272	65504	79625
% of Total	72.6%	74.8%	76.4%	78.5%	79.9%
Jewellery EBIT	1644	2546.8	4291	5673.2	7122.2
EBIT Margin (%)	5.9%	7.3%	8.5%	8.7%	9.0%

Source: Company and Vantage Securities

Vast distribution reach supplementing other key strengths

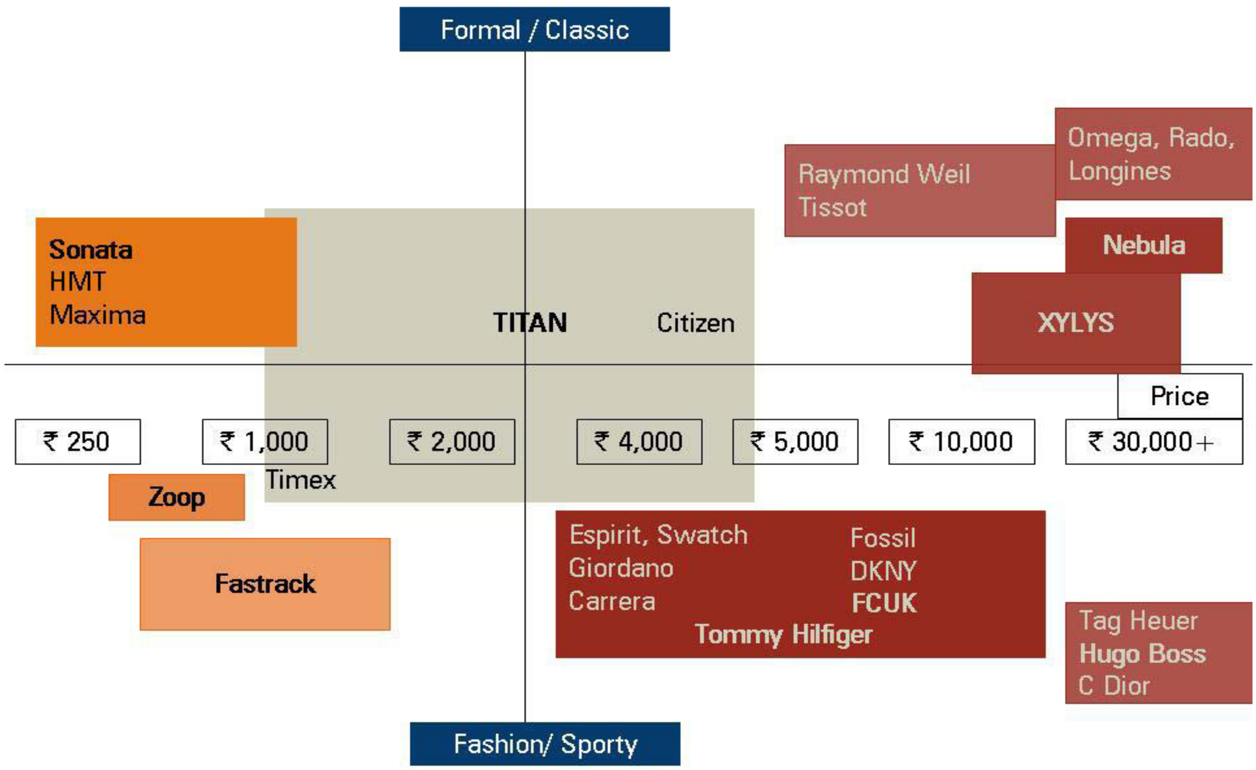
Titan's market and brand leadership of >50% uses the muscle of the vast distribution network of 11,000 dealers across India spanning 2500 towns. The depth of this vast distribution network has placed Titan amongst India's Top 5 watch brands by value, India's largest Eyewear retailer and India's largest jeweller. International brands like Hugo Boss, Tommy Hilfiger, Fcuk have also leveraged Titan's distribution strength to introduce its premium products in the rapidly growing Indian market. We believe Titan's capabilities of brand building, retailing, design, engineering, supply chain have been very well upheld by the 10,000+ multi brand outlets and the strong distribution reach.

Under penetration in the Watches market in India with varied layers or price points

The domestic Watch market is under penetrated with only 27% of the Indian population owning a watch. The total estimated market in FY2010 was estimated at ₹ 31bn at the retail level. In volume terms the organized players command ~40% of the industry share with the rest being with the unorganized players. However, in value terms ~60% of the total watch market in India is controlled by domestic brands like Titan. According to a report by the All India Federation of Horological Industries (AIFHI) and Technopak Advisors the current market size of the watch industry is ~₹ 4.5bn to ₹ 5.0 bn and is expected to grow at a rate of 10-15% annually and touch ₹ 8.5 bn in the next five years. Among premium watches, the per capita annual spend ranges between ₹25,000 and ₹40,000. Customers are not very price-sensitive as far as quality watches are concerned. Most watch buyers (almost 80 per cent) in India are in the age bracket of 21-30 years. The premium segment is expected to grow at a brisk pace in the coming years due to the influx of international premium brands. The trend of consumers easily migrating to higher priced products for watches and sunglasses is there because of the longevity associated with these products. We believe this under-penetration could expand the watches volumes going forward with Titan being an significant beneficiary. Titan has garnered ~25% of the volume share and ~45% of the value share of the organized retail market. The majority of the Indian watch market is below the ₹ 500 price level with ~65% of the total volumes and 24% of the total value falling in this category. Titan has positioned startegically with its offerings in every segment of the total Indian watches space. In FY2009 the company introduced the 'Sonata Super Fibre' in the mass segment to strengthen its presence in the less penetrated mass segment. TIL is the largest player in the branded low-end segment and its Sonata brand has highest volume sales of over 5 million watches per year. We believe, the strong brand positioning in the high volume mass and low-end segment will drive volume growth for the company in the next two or three years.

Titan is targeting the middle income consumer group with its flagship brand of Titan. The company presents diverse choices to consumers in this segment in order to raise its share in the high discretionary purchases of this consumer group. Some of the Titan sub-brands introduced recently are Titan Raga Flora, Titan Purple, Titan Edge and Titan Zoop (sub-brand for children). In our view, the middle income consumer segment presents strong growth opportunities for TIL due to high disposable income and rising aspiration level of this group, which drives multiple watch ownership and could increase it substantially from the current level of 3.5% of the country's total population.

Titan's Offerings in the Watches segment across different consumer segments



Source: Company

Titan is also licensed provider for some premium foreign brands like Hugo Boss, Fcuk etc in India. These brands can leverage the logistics and infrastructure strength of Titan which could take years for them to replicate. We have projected the EBIT margins for the watches segment to grow from 14.7% in FY11 to 15.9% by FY13E which would be led by the launch of new collections at higher price points, a richer sales mix and fewer store additions.

Aggressive but necessary expansion plans in the offing

At the end of February Titan has 650 stores under operation across several locations in India. Of these less than 15% of the stores are company owned and rest are franchisees. The company is planning to open 40 new stores of Titan in FY12 but the aim is to scale up the expansion of other newer formats like Eyeplus, Fastrack and Helios. Titan currently has 3 stores of Helios which by the end of the fiscal FY12 has been planned to touch 33 operational stores. The company also plans to open 100 stores of Fastrack which sells casual range of watches and accessories and ~20 stores of retail jewellery chain Tanishq. Titan is also planning to open 6-7 stores of its mass jewellery brand GoldPlus in Tier II and Tier III towns mainly in Andhra Pradesh and Karnataka. The company has gone slow on its GoldPlus after its launch in 2005 because it wanted to perfect its business model for this particular service offerings. The company also plans to add another 100 stores in the Titan Eye+ segment in FY12.

Huge Potential in the Jewellery segment of the Indian market

The opportunity in the Indian Indian Jewellery is estimated to be to the tune of ₹ 10,00,000 mn, with the semi urban and rural markets estimated to be ~40% of the total. The two major segments of the sector in India are gold jewellery and diamonds. Gold jewellery forms around 80 per cent of the Indian jewellery market. Besides, India has the world's largest cutting and polishing diamond industry. The Indian jewellery market is characterized by value conscious consumers buying traditional jewellery. It is also a fragmented industry with under karatage still prevalent in many parts of the country. According to the Bureau of Indian Standards, over 80% of the jewellers sell gold of lower purity than stated. The domestic jewellery market is dominated by the unorganised or unbranded players with the branded players constituting just 3% of the total market size. The gold jewellery market is presently growing at 15% p.a.and the diamond jewellery market at 27% p.a.

The World Gold Council estimates that 60% to 65% of the overall gold demand in India will come from the rural and semi-urban markets presenting a sizeable opportunity to the branded jewellery players like Gold Plus in the branded retail space.

TIL launched its Gold Plus stores to cater to the semi-urban and rural areas which currently stands at 29 stores. It has managed to increase its turnover five fold since 2007. The sales from GoldPlus stood at ₹4.4bn in FY10, comprising 13% of the jewellery sales. Since there is no diamond studded jewellery involved in GoldPlus sales with only plain gold sales the operating margins are at a lower level. TIL is therefore not going for aggressive expansion in this format of stores. TIL would scale up this segment of the business once GoldPlus is able to generate better margins on a consistent basis.

TIL has recently opened its luxury jewellery boutique Zoya in Delhi and Mumbai to cater to the fast growing ₹25bn luxury jewellery segment. The Zoya product portfolio is available in the price range of ₹0.2-2.5mn. TIL plans to open atleast six Zoya store boutiques by FY13.

Strong Design Capabilities

Tanishq Design studio's strong and diverse designing team has helped Titan win many awards. Apart from the 'trust' factor, Tanishq's unique and diverse designs have become its key USP. TIL's focus on developing and strenthening a capable design design team has enabled it to introduce contemporary designs based on various themes. These new innovative designs are in tune with the consumers changing preferences and present an opportunity to them to buy an extra piece of jewellery or additional watch which thereby bolstering TIL's brand equity.

Innovative Schemes

TIL has come up with an innovative instalment based jewellery buying initiative 'Golden Harvest Scheme' (GHS). This scheme witnessed record enrollments and contributed 15% of its retail sales in FY10. According to management, new enrollments are expected to increase the sales contribution of GHS to 25% of FY11E retail sales. We observe GHS scheme not only locks in a consumer for future purchases, it also is a highly effective way to lower working capital – capital employed in jewellery would have been twice the current capital employed if there were no advances from customers (Jewellery segment capital employed is negative currently). Member base of its Anuttara loyalty program also increased to over 450,000 members in FY10 since launch in July 2007.

Strong Same Store Sales (SSS) growth is correaleted to economic growth

SSS growth in jewellery has been strong and is closely linked to the level of economic growth in India. Slowdown in '00-01 due to IT meltdown led to SSS declining 4% in FY01. Economic improvement post the IT slowdown led to SSS growth ranging within 7-15% over FY02-05. Strong GDP growth in the following years of FY06-08 helped Titan post >25% growth in SSS growth. With the economic crisis in 2H FY09, SSS growth was lower at 11.7% in FY09. However, revival post 1H FY10 aided strong SSS growth of 18% in FY10.
Titan's current strategy of expanding the size of successful stores or opening bigger destination stores in major cities (two large format stores of Tanshiq opened in Mumbai and Pune) will help it to tap the higher end of the wedding market (consumers in this segment typically demand more choices/ inventory). Tanishq traditionally has not been a destination store for wedding jewellery – however, large stores in each city with more inventory and options, along with appropriate marketing campaigns will help it to tap this highly lucrative market. This will help to drive strong SSS growth going forward.

Dominant market leader with strong brand equity

TIL is the market leader in the domestic watches with an overall share of 40% by value and 22% by volume. Among the organized players, TIL has a market share of over 60%. TIL has been consistently voted as one of India's most admired brands in the consumer durables category – a position it has achieved through creativity (collections such as the Aviator series, use of Mozart's 25th symphony as its signature tune), innovation (collections such as the Edge series), trust (through the TATA brand and consistent product delivery), distribution (through the wide reach of 'World of Titan' chain) and impeccable service (via its innumerable watch care centres). We believe that 'emotional connect' and 'trust' associated with the brand is unparalleled and is a significant competitive advantage for Titan.

Investment Concerns

Volatility in gold and diamond prices

Jewellery demand is highly dependent on the movement in gold prices with stable/falling prices leading to an improvement in jewellery demand and vice versa. The significant jump in gold prices can lead to a significant slowdown in jewellery volume demand in the domestic market and negatively impact the volume demand on the downside. Though, a typical upper middle class customer of Tanishq buys gold based on a specific budget rather than monitoring the weight of the gold. This is unlikely to hurt the profitability factor much. The rise in diamond prices in the last 4-5 months has been quite steep and the management has indicated that this could have a negative bearing on the growth rates in the jewellery segment going ahead. The gap between the plain gold prices and jewellery prices which had broadened has narrowed to a considerable extent which could derail the high volume growth seen in the segment.

Increasing competition from international watch manufactures

Several international watch majors such as Tissot, Omega, Rolex Fossil, Calvin Klein, Giordano, Esprit and Tommy Hilfiger compete directly with TIL primarily in the premium watch category. With growing disposable income and rising aspirations levels, India presents an attractive market to the foreign premium watch manufacturers. TIL is highly susceptible to an increase in competition from foreign brands, which can negatively impact TIL's revenues and margin forecast in the watches segment.

Higher rentals in short-term

With robust expansion plans in FY12E (150-200 new stores), TIL is exposed to rising rental expenses on new stores as well as existing stores that are on lease. A higher than expected increase in rental expenses can negatively impact the company's expansion plans, leading to reduced profitability and added pressure to gain higher profit from existing stores.

Slower than expected recovery from economic slowdown

TIL's products fall under the discretionary category, which has high delta with the growth in disposable income and is highly dependent on the healthy growth of the economy. A slower than expected recovery in the economy can lead to lower spending on discretionary items (and more on necessities) leading to reduced volume growth for the company. Also, middle class consumers are highly likely to delay upgrading to premium products in the event of a delay in economic recovery. This, in turn, can negatively impact our revenues and margin forecasts.

Continued dominance of unbranded jewellery

The jewellery market in India is dominated by unorganised players with over 90% of the market share. In the recent past, TIL has been able to increase its market share by targeting young and educated customers in metros and Tier I cities with the guarantee on purity of gold and presenting contemporary designs. However, TIL's incremental growth is dependent on its ability to attract a large consumer base in Tier II and Tier III cities who still rely on family jewellers.

Design Team's Capabilities

The changing consumer perception towards watches and jewellery from its investment and functional uses to them being fashion accessories necessitates regular launch of new, trendy and diverse designs. If TIL is unable to come up with new, trendy and diverse designs on a regular basis this could pose significant risks to its two revenue earning divisions.

P & L Account -

Standalone Results (₹ mn)	FY 09	FY 10	FY 11	FY 12E	FY 13E
Gross Sales	38477.2	47031.2	65709	83483	99256
Less: Excise Duty	443.4	287	499.7	584.4	694.8
Net sales	38033.8	46744.2	65208.9	82898.8	98560.9
Other operating income	9.0	5.8	7.5	0.0	0.0
Total Sales	38042.8	46750	65216.4	82898.8	98560.9
Total Raw material costs	27621.9	34493.9	48039.6	61237.6	72610.2
Employee Cost	2334	2744.9	3929.6	4995.6	5939.5
Advertising	1813.6	2111.5	3032.7	3979.8	4731.7
Other Expenditure	3299.4	3444.3	4350.9	4808.1	5470.1
Total Expenditure	35068.9	42794.6	59352.8	75021.1	88751.4
Other Income	43.6	112.8	553.3	662.0	787.0
EBIT	2599.9	3467.4	6072.1	8047.2	10031.3
PBT	2305.6	3213.2	5990.0	7960.0	9944.1
PAT	1698.8	2532.4	4336.4	5730.7	7159.1
Less: Income tax of earlier years	109.2	29.2	32.2	0.0	0.0
Net profit for the period	1589.6	2503.2	4304.2	5730.7	7159.1
Exceptional Items	0.0	0.0	0.0	0.0	0.0
Adjusted Net profit	1589.6	2503.2	4304.2	5730.7	7159.1
EPS (₹)	1.8	2.8	4.8	6.5	8.1

Source: Company

Balance Sheet -

Standalone Balance Sheet					
Particulars (₹ Mn)	**FY 09**	**FY 10**	**FY11E**	**FY12E**	**FY13E**
SOURCES OF FUNDS					
Shareholders' funds					
Share capital	444	444	444	888	888
Reserves and surplus	5069	6800	9810	13374	18825
	5512	7244	10254	14262	19712
Loan funds					
Secured loans	1168	728	0	0	0
Unsecured loans	587	0	0	0	0
Total Debt	1754	728	728	728	728
Deferred tax liability (Net)	182	48	48	48	48
TOTAL LIABILITIES	7448	8019	11029	15037	19600
APPLICATION OF FUNDS					
Fixed assets					
Gross block, at cost	5930	6243	7743	9243	11243
Less : Depreciation	3186	3617	3962	4454	5020
Net block	2745	2626	3292	3929	4559
Advances on capital account and capital WIP, at cost	195	123	123	123	123
Investments	77	76	76	76	76
Deferred tax asset (Net)	0	0	0	0	0
Current assets, loans and advances					
Cash and bank balances	547	1867	3165	5753	9400
	14777	18037	26157	34956	43413
Less :					
Current liabilities and provisions					
	10346	12843	18619	24048	28571
Net current assets	4432	5194	7538	10909	14842
TOTAL ASSETS	7448	8019	11029	15037	19600

Source: Company

Cash Flow Statement –

Standalone Cash Flow Statement	FY 09	FY 10	FY11E	FY12E	FY13E
Particulars (₹ Mn)					
[A]CASH FLOWS FROM OPERATING ACTIVITIES					
Net profit before taxes and exceptional items (PBT)	2306	3213	5990	7960	9944
Adjustments for :					
Depreciation / Amortisation	418	601	345	492	565
Interest income	(39.4)	(106.3)	(560.8)	(662.0)	(787.0)
Dividend income	0.0	0.0	0.0	0.0	0.0
Interest expense	294	254	82	87	87
Operating profit before working capital changes	3098	3979	5856	7878	9810
Adjustments for:					
(Increase)/Decrease in trade and other receivables	(95.4)	117	(314.5)	(271.1)	(287.5)
(Increase)/Decrease in inventories	(1,816.0)	(1,376.4)	(5,784.7)	(5,579.2)	(4,168.1)
(Increase)/Decrease in loans and advances	(314.1)	(190.6)	(723.1)	(361.2)	(353.6)
(Increase/(Decrease) in current liabilities and provisions	1316	2230	5776	5429	4523
Cash generated from operations	2189	4760	4809	7095	9523
Direct taxes paid	(592.7)	(1,340.5)	(1,718.0)	(2,229.3)	(2,784.9)
CASH GENERATED FROM / (USED IN) OPERATIONS	**1596**	**3419**	**3091**	4866	6738
[B]CASH FLOW FROM INVESTING ACTIVITIES					
Additions to fixed assets(including capital WIP and advances on capital acc)	(680.9)	(441.6)	(1,500.0)	(1,500.0)	(2,000.0)
Interest received	76	105	561	662	787
NET CASH (USED IN) / FROM INVESTING ACTIVITIES	**(572.7)**	**(316.4)**	**(939.2)**	**(838.0)**	**(1,213.0)**
[C]CASH FLOW FROM FINANCING ACTIVITIES					
Proceeds from new borrowings	2492	104	0.0	0.0	0.0
Repayment of borrowings	(2,875.5)	(1,104.7)	0.0	0.0	0.0
Dividends paid	(352.9)	(441.5)	(665.8)	(1,109.7)	(1,477.5)
Tax on dividends paid	(60.4)	(75.4)	(110.6)	(184.3)	(245.4)
Interest paid	(200.8)	(262.1)	(82.1)	(87.2)	(87.2)
Others	0.0	0.0	0.0	(59.0)	(68.0)
CASH GENERATED FROM / (USED IN) FINANCING ACTIVITIES	**(997.5)**	**(1,779.5)**	**(858.5)**	**(1,440.2)**	**(1,878.1)**
NET CHANGES IN CASH AND CASH EQUIVALENT(A+B+C)	**26**	**1323**	**1294**	**2588**	**3647**
Cash and cash equivalents at beginning of the year	519	547	1871	3165	5753
Cash and cash equivalents at end of the year	**548**	**1871**	**3165**	**5753**	**9400**

Source: Company

Ratios –

	FY 09	FY 10	FY 11E	FY 12E	FY 13E
Standalone Ratios					
Particulars					
Growth (In %)					
Net Sales	27.0%	22.9%	39.5%	27.1%	18.9%
Adjusted Net Profit	5.8%	57.5%	71.9%	33.1%	24.9%
EBITDA (Operating EBITDA)	18.4%	33.2%	48.3%	34.5%	24.5%
EPS	5.8%	57.5%	81.8%	30.8%	27.3%
CEPS	20.0%	56.2%	44.6%	32.9%	24.1%
Gross Fixed Assets	6.3%	5.3%	24.0%	19.4%	21.6%
Capital Employed	3.7%	7.7%	37.5%	36.3%	30.3%
Valuation					
EPS (₹)	1.8	2.8	4.8	6.5	8.1
CEPS (₹)	2.3	3.6	5.3	7.0	8.7
BVPS (₹)	6.2	8.2	11.5	16.1	22.2
PER (x)	125.1	79.5	46.2	34.7	27.8
PEG (x)	21.6	1.4	0.6	1.1	1.0
P/CEPS (x)	96.0	61.4	42.5	32.0	25.7
P/BV (x)	36.1	27.5	19.4	13.9	10.1
EV/EBITDA (x)	3.7	2.2	1.3	1.9	1.1
EV/Net Sales (x)	0.3	0.2	0.1	0.2	0.1
EV/Cash Profit (x)	5.3	2.7	1.6	2.4	1.4
Mkt Cap/Sales (x)	0.3	0.2	0.2	0.2	0.2
Debt/Equity (x)	0.3	0.1	0.1	0.1	0.0
Profitability					
ROCE (%)	35.5%	44.8%	63.8%	61.7%	57.9%
ROE (%)	32.2%	39.2%	49.2%	46.8%	42.1%
(Operating EBITDA) EBIDTA Margin	7.8%	8.4%	9.0%	9.5%	10.0%
EBIT Margin (%)	6.8%	7.4%	9.3%	9.7%	10.2%
Net Profit Margin (%)	4.2%	5.4%	6.6%	6.9%	7.3%
Tax/PBT (%)	31.1%	22.1%	28.1%	28.0%	28.0%
Turnover					
Avg. Collection Period (Days)	10.2	7.3	7.0	6.7	6.7
Avg. Inventory Period (Days)	158.9	141.8	145.8	147.6	145.5
Avg. Payment Period (Days)	98.0	98.0	100.0	105.0	105.5
Net working capital (Days)	37.3	26.0	24.5	22.7	20.2
Net Fixed Assets (x)	12.9	17.0	19.1	20.5	21.1
Total Assets (x)	5.1	5.8	5.9	5.5	5.0
Cash on B/S	546.9	1867.2	3165.1	5752.7	9399.8
Cash per share (₹)	0.6	2.1	3.6	6.5	10.6

Source: Company

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