

## Entering Favorable Base Effects, Upgrade to 'HOLD'

February 1, 2010

### HOLD

Price	Target Price
<b>Rs1,499</b>	<b>Rs1,763</b>

<b>Sensex</b>	<b>16,358</b>
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#### Price Performance

(%)	1M	3M	6M	12M
Absolute	3	22	22	61
Rel. to Sensex	9	20	17	(9)

Source: Capitaline

#### Stock Details

Sector	Retail
Reuters	TITN.BO
Bloomberg	TTAN@IN
Equity Capital (Rs mn)	444
Face Value(Rs)	10
No of shares o/s (mn)	44
52 Week H/L	1,572/667
Market Cap (Rs bn/USD mn)	67/1,385
Daily Avg Volume (No of sh)	54958
Daily Avg Turnover (US\$m)	1.6

#### Shareholding Pattern (%)

	M'09	D'08	S'08
Promoters	53.1	53.1	53.1
FII/NRI	11.2	10.6	10.2
Institutions	8.7	8.8	9.0
Private Corp	3.3	3.9	4.3
Public	23.8	23.7	23.5

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Titan's Q310 performance exceeds expectation with (1) 30.3% YoY growth in revenues to Rs13.3 bn (2) 81.1% YoY growth in operating profit to Rs1.1 bn and (3) 233.1% yoy growth in adjusted in net profit to Rs784 mn. The revenue growth was led by 33.7% yoy growth in 'Jewellery' business to Rs10.5 bn and 24.8% yoy growth in 'Watch' business to Rs2.4 bn. Robust performance of Jewellery business and reduction of Ebit loss in Others business i.e. Eyewear & Precision Engineering was a positive surprise.

'Jewellery' business performance in Q310 signals for a period of favorable base effects in ensuing quarters. Hereon, expect sharp acceleration in volume growth in 'Jewellery' business considering better acceptability of gold prices and favorable base effects. Considering robust performance of 'Jewellery' business in 9MFY10 (especially EBIT margins) - we have upgraded the FY10E and FY11E earnings estimates by 14% (Rs48.1/Share) and 24% (Rs60.8/Share). Since, our initiating coverage on April 2008, Titan has remain under-performer with relative under-performance of 9% to Sensex. Also, where our consumer universe delivered absolute return of 72%, Titan was under-performer with absolute return of 61%. A favorable base effect scenario coupled with relative under-performance in consumer pack- we upgrade Titan from SELL to HOLD with price target of Rs1763/Share – valuing at PER of 29X FY11E earnings (Medium term-average multiple i.e. FY05-10E).

#### Q3FY10 results surpassed our estimates, led by better performance in Jewellery and Others business

Titan reported 30.3% yoy growth in net revenues to Rs13.3 bn – ahead of our estimates. The revenue growth was led by 33.7% yoy growth in 'Jewellery' business to Rs10.5 bn and 24.8% yoy growth in 'Watch' business to Rs2.4 bn. Titan reported 81.1% yoy growth in operating profit to Rs1.1 bn led by robust performance of Jewellery business and reduction of Ebit loss in Others business i.e. Eyewear & Precision Engineering. Consequently, operating margins jumped 230 bps yoy to 8.1% and operating profit grew 45.2% yoy to Rs862 mn - ahead of our estimates. Benefiting from strong operational performance and lower interest and depreciation charge, the adjusted net profit grew 233.1% yoy to Rs784 mn. The adjusted net profit exceeds our earnings estimates for Q310 – posting positive surprise.

#### 'Watch' business performance was ahead of our estimates, not out of woods as yet

The 'Watch' business reported 24.8% yoy growth in revenues to Rs2.4 bn –ahead of our estimates. New product launches, strong volume growth and favorable base effect augmented the performance in the quarter. The segment EBIT jumped 144.7% yoy to Rs354 mn – yet ahead of our estimates. The EBIT margins improved 720 bps yoy to 14.7% in the quarter – closer to average EBIT margins. Even, on annual basis, we expect the EBIT margins of 'Watch' business to remain at 13-15% levels. We continue maintain our view that, 'Watch' business is bracing for change- whereby volume growth momentum will slowdown along with downtrading.

YE-Mar	Net Sales	EBITDA (Core)	EBITDA (%)	AEPS APAT	EV/ (Rs)	EV/ EBITDA	P/BV	Div Yld (%)	RoE (%)	P/E (x)
FY2008	29,937	2,390	8.0	1,602	36.1	28.7	15.3	0.5	33.0	41.6
FY2009	38,034	3,371	8.9	2,100	47.3	20.1	12.1	0.7	41.6	31.7
FY2010E	46,463	3,674	7.9	2,134	48.1	18.5	9.0	0.7	38.0	31.2
FY2011E	53,747	4,524	8.4	2,701	60.8	14.7	6.9	0.7	37.5	24.7

**Approximate 13% YoY volume growth in 'Jewellery' business, gaining from base effects**

Jewellery has flagged its entry to favorable base effects season i.e. entering phase of robust volume growth. Thereby, Titan reported 33.7% yoy growth in 'Jewellery' business to Rs10.5 bn – approximately 19% yoy price-led growth and 13% yoy volume-led growth. Despite, Diwali season falling in Q210 –this year, volume growth of 13% yoy indicates benefits of favorable base effects and acceptance of higher gold prices. With robust volume and value growth, EBIT grew ahead of estimates by 46.5% yoy to Rs742 mn. We expect the trend to accentuate and strengthen in ensuing quarters - purely on favorable base effects and acceptance of high gold prices.

**Reduction in EBIT loss in 'Other' business- is a blip**

'Other' business i.e. eyewear and precision engineering posted revenue decline of 6.8% yoy to Rs403 mn – derailing the trend of continued growth momentum. Its 'Precision Engineering' that registered 25% yoy decline in revenues to Rs180 mn – on account of deferrals and cancellations. Whereas, 'Eyewear' business grew by 15.8% yoy to Rs220 mn – growth momentum is in line with our estimates. The EBIT Loss declined to Rs61 mn in Q310 compare to Rs69 mn in Q309 – yielding positive surprise. We believe that, reduction of EBIT loss (especially Eyewear business) is short-term blip and achieving break-even will remain long-haul process.

**'Jewellery' entering a phase of favorable base effects and acceptability of high gold prices**

We did analysis on gold prices and India consumption pattern – for 20-year data. The outcome is applicable in current time period of gradual fall in gold price after continuous rise. The data clearly indicates at 3-stage process for gold consumption (1) Phase - I growing skepticism with every rise in gold prices (2) Phase -2 better acceptability of gold prices especially after sharp and sustained rise – even though gold prices remain at historic high (3) Phase – III acceleration in demand on gradual decline in gold prices, especially after sharp rise. We believe that, gold consumption in India is at Phase-III – which implies sharp increase in demand in ensuing quarters. Thus, 'Jewellery' business of Titan is in a sweet spot – and initial signs are visible in Q310 performance.

**Entering favorable base effect, Upgrading from 'SELL' to 'HOLD'**

'Jewellery' business performance in Q310 signals for a period of favorable base effects. Hereon, expect sharp acceleration in volume growth in 'Jewellery' business considering better acceptability of gold prices and favorable base effects. Further, considering robust performance of 'Jewellery' business in 9MFY10 (especially EBIT margins) - we have upgraded the FY10E and FY11E earnings estimates by 14% (Rs48.1/Share) and 24% (Rs60.8/Share). Since, our initiating coverage on April 2008, Titan has remain under-performer with relative under-performance of 9% to Sensex. Also, where our consumer universe delivered absolute return of 72%, Titan was under-performer with absolute return of 61%. A favorable base effect scenario coupled with relative under-performance in consumer pack- we upgrade Titan from SELL to HOLD with price target of Rs1763/Share – valuing at PER of 29X FY11E earnings (Medium term-average multiple i.e. FY05-10E).

## Consolidated Quarterly Financials

(Rs Million)	Q3FY10	Q3FY09	YoY Gr(%)	Q2FY10	QoQ Gr(%)
Net Sales	13338.1	10240.3	30.3	11468.8	16.3
Expenditure	12263.5	9647.0	27.1	10386.8	18.1
Material Cost	10169.5	7823.4	30.0	8469.6	20.1
% of Sales	76.2	76.4	-20 bps	73.8	240 bps
Employee Expenses	678.8	757.0	-10.3	651.8	4.1
% of Sales	5.1	7.4	-230 bps	5.7	-60 bps
Selling & Marketing Expenses	604.7	496.9	21.7	515.6	17.3
% of Sales	4.5	4.9	-30 bps	4.5	0 bps
Other Expenses	810.5	569.7	42.3	749.8	8.1
% of Sales	6.1	5.6	50 bps	6.5	-50 bps
Operating Profit	1074.6	593.3	81.1	1082.0	-0.7
EBIDTA (%)	8.1	5.8	230 bps	9.4	-140 bps
Other Income	28.3	11.5	146.1	30.9	-8.4
Interest	29.0	115.8	-75.0	50.3	-42.3
Depreciation	91.1	78.9	15.5	89.0	2.4
PBT	982.8	410.1	139.6	973.6	0.9
Tax	199.3	174.9	14.0	197.6	0.9
APAT (Before Exceptional Items)	783.5	235.2	233.1	776.0	1.0
APAT (%)	5.9	2.3	360 bps	6.8	-90 bps
RPAT (After Exceptional Items)	783.5	59.4	1219.0	776.0	1.0
RPAT (%)	5.9	0.6	530 bps	6.8	-90 bps
EPS (Before Exceptional Items)	17.7	5.3	233.1	17.5	1.0
EPS (After Exceptional Items)	17.7	1.3	1219.0	17.5	1.0

## Segmental performance

(Rs Mn)	Q3FY10	Q3FY09	% YoY	Q2FY10	% QoQ
<b>Segment revenue</b>					
Watches	2409.4	1,931.1	24.8%	2955.2	-18.5%
Jewellery	10545.2	7,886.9	33.7%	8226.2	28.2%
Others	402.5	431.8	-6.8%	310.3	29.7%

(Rs Mn)	Q3FY10	Q3FY09	% YoY	Q2FY10	% QoQ
<b>Segment PBIT</b>					
Watches	353.9	144.6	144.7%	582.7	-39.3%
Jewellery	741.8	506.2	46.5%	577.2	28.5%
Others	-60.5	-69	12.3%	-110.7	45.3%

	Q3FY10	Q3FY09	% YoY	Q2FY10	% QoQ
<b>PBIT Margin (%)</b>					
Watches	14.7%	7.5%	720 bps	19.7	-500 bps
Jewellery	7.0%	6.4%	60 bps	7	0 bps
Others	-15.0%	-16.0%	90 bps	-35.7	2060 bps

(Rs Mn)	Q3FY10	Q3FY09	% YoY	Q2FY10	% QoQ
<b>Capital Employed</b>					
Watches	3,209.6	3,881.6	-17.3	2,858.0	12.3
Jewellery	2,485.0	2,516.3	-1.2	3,525.3	-29.5
Others	877.9	947.1	-7.3	902.5	-2.7
Corporate(Unallocated)	1,279.1	28.4	4403.9	393.0	225.5

## Financial

## Income Statement

Y/E, Mar (Rs. mn)	FY08	FY09	FY10E	FY11E
<b>Net Sales</b>	<b>29,937</b>	<b>38,034</b>	<b>46,463</b>	<b>53,747</b>
Growth	43.2	27.0	22.2	15.7
<b>Expenses</b>	<b>27,547</b>	<b>34,663</b>	<b>42,789</b>	<b>49,223</b>
Growth	46.2	25.8	23.4	15.0
Raw Materials	20,920	26,917	33,459	38,601
% Of Sales	69.9	70.8	72.0	71.8
Employee Cost	1,934	2,334	2,680	2,989
% Of Sales	6.5	6.1	5.8	5.6
Manufacturing Expenses	633	969	1,184	1,370
% Of Sales	2.1	2.5	2.5	2.5
Admin Expenses	714	1,039	1,039	1,143
% Of Sales	2.4	2.7	2.2	2.1
Selling & Distribn	2,806	3,623	4,426	5,120
% Of Sales	9.4	9.5	9.5	9.5
<b>Ebidta</b>	<b>2,390</b>	<b>3,371</b>	<b>3,674</b>	<b>4,524</b>
Growth	16.0	41.0	9.0	23.2
Ebidta%	0.1	0.1	0.1	0.1
Other Income	18	53	79	79
Interest	201	294	356	401
Depreciation	297	418	457	482
PBT	2,043	2,707	2,939	3,721
Tax	440	607	806	1,020
<b>PAT (Before EO Item)</b>	<b>1,602</b>	<b>2,100</b>	<b>2,134</b>	<b>2,701</b>
Growth	33.9	31.1	1.6	26.6
Net Margin%	0.1	0.1	0.0	0.1
E/O Item	100	511	-300	0
Reported PAT	1,503	1,590	2,434	2,701

## CashFlow Statement

Y/E, Mar (Rs. mn)	FY08	FY09	FY10E	FY11E
<b>Pre-Tax Profit</b>	<b>2,023</b>	<b>2,306</b>	<b>3,239</b>	<b>3,721</b>
Depreciation & Non Cash	334	426	457	482
Interest & others	210	1,372	356	401
Chg in W Cap	-936	-909	-2,019	-1,046
Tax Paid	-609	-593	-806	-1,020
<b>Operating CashFlow</b>	<b>1,022</b>	<b>2,601</b>	<b>1,228</b>	<b>2,538</b>
Capex	-467	-445	-461	-356
<b>Free Cash Flow</b>	<b>555</b>	<b>2,156</b>	<b>767</b>	<b>2,182</b>
Investments	-207	7	0	0
Equity Capital	0	0	0	0
Loans	102	-383	500	0
Dividend	-221	-353	-519	-519
Others	-211	217	-356	-401
<b>Net Change in Cash</b>	<b>19</b>	<b>1,644</b>	<b>391</b>	<b>1,262</b>
<b>Opening Cash Position</b>	<b>507</b>	<b>519</b>	<b>547</b>	<b>938</b>
<b>Closing Cash Position</b>	<b>519</b>	<b>547</b>	<b>938</b>	<b>2,200</b>

## Balance Sheet

Y/E, Mar (Rs. mn)	FY08	FY09	FY10E	FY11E
Equity Share Capital	444	444	444	444
Reserves	3,918	5,069	6,983	9,164
<b>Networth</b>	<b>4,362</b>	<b>5,512</b>	<b>7,427</b>	<b>9,608</b>
Secuured Loans	1,881	1,168	1,168	1,168
Unsecured Loans	698	587	1,087	1,087
<b>Loan Funds</b>	<b>2,579</b>	<b>1,754</b>	<b>2,254</b>	<b>2,254</b>
<b>Total Liabilities</b>	<b>6,941</b>	<b>7,266</b>	<b>9,681</b>	<b>11,862</b>
Gross Block	5,581	5,930	6,486	6,842
Acum Depreciation	2,856	3,186	3,642	4,124
<b>Net Block</b>	<b>2,724</b>	<b>2,745</b>	<b>2,844</b>	<b>2,718</b>
CWIP	100	195	100	100
<b>Investments</b>	<b>474</b>	<b>77</b>	<b>77</b>	<b>77</b>
<b>Current Assets</b>	<b>12,686</b>	<b>14,777</b>	<b>18,343</b>	<b>22,239</b>
Inventories	10,211	12,027	14,686	16,895
Debtors	965	1,062	1,325	1,532
Cash&Bank	519	547	938	2,200
Loans&Advances	992	1,141	1,394	1,613
<b>Cur Liab &amp; Prov</b>	<b>8,797</b>	<b>10,346</b>	<b>11,501</b>	<b>13,090</b>
<b>Net Current Assets</b>	<b>3,889</b>	<b>4,432</b>	<b>6,842</b>	<b>9,149</b>
Misc Expenditure	0	0	0	0
Deferred Tax	-247	-182	-182	-182
<b>Total Assets</b>	<b>6,941</b>	<b>7,266</b>	<b>9,681</b>	<b>11,862</b>

## Key Ratios

Y/E, Mar	FY08	FY09	FY10E	FY11E
<b>Profitability %</b>				
Ebidta Mgn	8.0	8.9	7.9	8.4
PAT Mgn	5.4	5.5	4.6	5.0
ROCE	33.0	41.6	38.0	37.5
ROE	42.0	42.5	33.0	31.7
<b>Per Share Data (Rs/share)</b>				
EPS	36.1	47.3	48.1	60.8
CEPS	42.8	56.7	58.4	71.7
BVPS	98.3	124.2	167.3	216.5
DVPS	8.0	10.0	10.0	10.0
<b>Valuations (X)</b>				
PER	41.6	31.7	31.2	24.7
CPER	35.1	26.4	25.7	20.9
P/BV	15.3	12.1	9.0	6.9
Ev/Sales	2.3	1.8	1.5	1.2
Ev/Ebidta	28.7	20.1	18.5	14.7
Dividend Yield	0.5	0.7	0.7	0.7
<b>Turnover (X Days)</b>				
Debtor TO	11.5	9.7	10.4	10.4
Inventory TO	112.5	117.1	125.3	125.3
<b>Gearing Ratio (X)</b>				
Net Debt/Equity	0.5	0.2	0.2	0.0
Total Debt/Equity	0.6	0.3	0.3	0.2

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