

22 June 2016

Robust Growth Story

CMP: Rs 220

Strong Buy

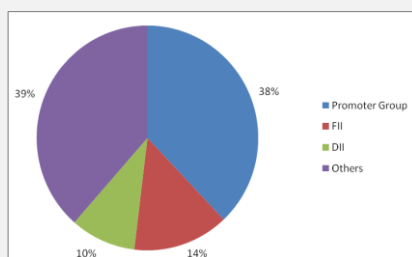
Target Price: Rs 332

Sector	Lifestyle
Market Cap	INR 651 Cr
52 Weeks High	INR 315.50
52 Weeks Low	INR 182.00
Target Time Period	12-14 months
Face Value	INR 10 each
Beta	1.28
Pledged Shares	0.00%
BSE Scrip Code	533200
NSE Scrip Code	TALWALKARS

Share Performance



Share Holding Pattern



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Company Background

Talwalkars Better Value Fitness Ltd (TBVF) is one of the biggest fitness chains across India. Talwalkars is a well known brand in fitness club which started its first gym in Mumbai in 1932. Over the years, the company has built its brand name "Talwalkars" and has become the largest fitness club in India, by adding a large number of gyms and value added services. In 2010, TBVF got listed in the both the major Stock Exchanges of India; NSE and BSE. Presently, the company has the highest number of fitness chains with 176 centres in 85 cities across India and Sri Lanka.

Investment Rationale:

Robust Growth in top line and bottom line:

Over the last 3 years, the company has grown its revenue at a CAGR of 20% and EBITDA and PAT margins have grown at a CAGR of 27% and 22%, respectively.

In FY 2016, the company has reported revenue, EBITDA and PAT of INR 258.13 Cr, INR 150.22 Cr and 55.02 Cr respectively with robust growth in revenue, EBITDA and PAT of 14%, 20% and 19% respectively, compares to FY2015.

EBITDA margin has improved from 55% in FY2015 to 57% in FY2016, due to higher operating efficiency and increase in contribution from value added services. Going forward, the above factors are expected to help the company in further expanding its margins.

Strong brand, pan-India presence and Increase in contribution from value added services will help to increase margins:

TBVF has presence across India. In FY2016, the company has extended its presence in Sri Lanka by acquiring 49.5% stake in PWG. PWG is the one of the biggest health and fitness players in Sri Lanka, operating 10 gyms. The company has planned to continue its expansion steak by increasing number of centres, organically and inorganically, with major focus on organic growth. TBVF is planning to take PWG upto 100 centres in Sri Lanka in next 3 years. Moreover, TBVF's management is looking to expand its footprint in India by opening 25 owned gyms and 10 HIFI gyms in FY2017.

Lucrative acquisition of better margin and ROC business: In FY2016, the company has acquired PWG, Inshape, Zorba and Gymtrekker to achieve significant scale and size and become a leader in all the major cities across India. All the acquisitions are high margin and ROC businesses, with lower capex, enabling the company to enhance its bottom-line and cash flows.

Increasing contribution of value added services with optimum utilization of gyms free space:

TBVF has introduced new value added services Transform, Reduce, Nuform, Zorba, Zumba, Group X Activities, TRX Spa and Massage in their existing gyms, both organically and inorganically. Reduce is a diet program which will help members to get the desired results along with working out at the gym. This program is managed by a well experienced nutritionist. Nuform is the electrical muscle stimulation training exercise, with proven German technology, which will help reduce inches and tone muscles in just 20 minutes. Transform is the combination of Reduce and Nuform. Zorba is a Chennai-based yoga studios chain which operates at 3 centres in Chennai. TBVF has acquired Zorba by

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acquiring 50% stake in the company. Zorba can be the game changer for the company. In FY2017, the company has planned to open 33 zorba studios at existing centres, which will help the company to increase revenue through optimal utilization of free spaces at existing centres. Zorba is very low capex business which will enhance ROC and free cash flows for the company. In addition to the above services, the company has planned to increase contribution from other services by offering these services at untouched centres.

Business Model

- **Talwalkars Gym:** The Company mainly operates Talwalkars gyms in 122 centres all over India, either under owned or franchise model. These gyms are equipped with latest technology equipments and value added services. Talwalkars Gyms have average space of 5000-6000 sq ft per gym with average number of members in the range of 1000-1300 per gym. These gyms mainly operate in Tier 1 and Tier 2 cities. TBVF's management is focused toward further enhancing profitability by increasing contribution from value added services.
- **Premium/ Large Format Gym:** Premium Gyms are big sized gyms having larger space (6000-12000 sq ft), higher capacity and additional value added services, compared to other class of gyms. Currently, the company operates 8 premium/large format gyms in the hub of metro cities. These gyms are more productive in terms of higher membership fees, larger contribution from value added services and higher margins; however, capex cost is 1.8x times higher compared to Talwalkars Gym class.
- **Power World Gym (PWG):** The Company has added PWG centres in its portfolio with the acquisition of 49.5% stake in PWG, which is a Sri Lanka-based health and fitness centre. Currently, PWG runs 20 centres in Sri Lanka. At the time of acquisition, PWG was operating 10 gyms, however, post acquisition it has added another 10 gyms. These gyms have average space of 3750-4000 sq ft per gym with average number of members in range of 800-1000 per gym. They generate higher margins and ROC with lower capex compared to other gyms in India. These gyms mainly operate in lower income areas in metros/ mini metros.
- **HIFI Gym:** HIFI Gyms operate in 23 centres, targeting Tier 2, 3 and 4 cities. HIFI Gyms entail a low capex model with average space of 2500-2800 sq ft per gym and average number of member in range of 550-650 per gym. These types of gyms mainly cater to meet fitness demands of people in lower Tier cities. HIFI Gyms are equipped with all the latest technology equipments same as other centres in India; however, without value added services. HIFI Gyms are higher margin gym class compared to Talwalkars Gyms. TBVF's management is looking to increase number of centres in HIFI model to enhance overall profitability and ROC of the company.

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Concerns of Free cash flow:

Being in the growth phase, the company is facing major challenges in terms of free cash flow. However, the company has reported positive free cash flow in FY2016. TBVF's management is now focused at increasing free cash flows with its robust growth plans. The management is confident of achieving positive free cash flows with increase in contribution from value added services, optimum utilization of free space at existing gyms and the acquisition of higher margin and ROC businesses.

Valuation Compelling:

We expect Talwalkars's revenue (without PWG) to grow at a CAGR of ~12% and 13% in FY2017 and FY2018 respectively while EBITDA is expected to grow at a CAGR of ~5% and ~13% during the same period. We expect an EPS of Rs 19 and Rs 23 in FY2017 and FY2018 respectively.

In our DCF model, we have assumed a weighted average cost of capital (WACC) of 13.5% and a long term growth rate of 3%, following explicit free cash flow forecasts through FY 2021. We arrive at a target price of Rs 332, which generates a 51% upside potential from current levels. Therefore, we initiate coverage on Talwalkars with a 'Strong Buy' rating.

Financial Statements**Exhibit 1:****Financial Summary (Consolidated)**

Y/E March	2013	2014	2015	2016E	2017E	2018E
Sales (INR Cr)	150.9	187.3	225.7	251.6	282.4	319.8
PAT (INR Cr)	30.1	36.6	46.1	53.8	55.1	67.4
EPS (INR)	11.5	14.0	17.6	18.1	18.5	22.7
P/E (x)	12.5	12.1	21.3	12.2	11.9	9.7
RoE (%)	14%	15%	17%	12%	11%	12%
RoCE (%)	16%	16%	15%	13%	13%	14%
EV/E (x)	3.2	2.7	5.9	3.4	3.2	2.8
DPS (Rs)	1.5	1.5	1.5	1.5	1.5	1.5

Exhibit 2:**Income Statement (Consolidated)**

Figures in INR crores	2013	2014	2015	2016	2017E	2018E
Revenue from Operation	151	187	226	258	282	320
Other Income	1	1	1	-	7	6
Total Income	152	188	227	258	289	326
Total Expenditure	78	95	101	108	139	155
EBITDA	74	94	125	150	151	171
Depreciation	15	24	40	47	45	50
EBIT and exceptional Items	59	70	86	103	105	120
Interest	11	12	13	18	18	16
EBT and exceptional Items	48	58	73	86	87	105
Less: Exceptional Items	-	0	-	-	-	-
EBT	48	58	73	86	87	105
Less: Tax Expenses	16	18	24	30	30	35
Earning before Minority Interest	33	40	48	55	58	70
Less: Minority Interest	3	3	2	0	3	3
Profit for the year	30	37	46	55	55	67

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Exhibit 3:

Assets and Liabilities Statement (Consolidated)

Figures in INR crores	2013	2014	2015	2016E	2017E	2018E
EQUITY AND LIABILITIES						
Share capital	26	26	26	30	30	30
Reserves and surplus	182	214	251	403	453	515
	208	240	277	433	482	545
Minority interests	8	11	14	16	18	21
NON-CURRENT LIABILITIES						
Long-term borrowings	135	137	278	308	282	241
Deferred tax liabilities (net)	19	24	25	25	25	25
Other Long-term liabilities	17	13	1	1	1	1
	171	174	304	334	309	267
CURRENT LIABILITIES						
Short-term borrowings	5	31	1	-	-	-
Trade payables	8	10	15	13	15	17
Other current liabilities	35	41	40	61	37	54
Short-term provisions	15	18	16	17	17	17
	63	100	72	91	68	87
Total	451	526	666	873	878	920
ASSETS						
NON-CURRENT ASSETS						
Fixed assets	358	451	521	552	610	660
Non-current investments	23	9	5	45	45	45
Long-term loans and advances	25	24	30	33	37	42
Other Non Current Assets	0	0	0	0	0	0
	48	33	35	79	83	88
CURRENT ASSETS						
Current investments	0	0	0	0	0	0
Inventories	0	0	0	0	0	0
Trade receivables	18	32	34	31	35	39
Cash and bank balances	23	6	47	181	118	99
Short-term loans and advances	4	4	29	31	32	34
	45	42	110	242	185	173
Total	451	526	666	873	878	920

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Exhibit 4:

Cash Flow Statement (Consolidated)

Figures in INR crores	2013	2014	2015	2016E	2017E	2018E
Net Profit before Tax & after Extraordinary Items	48	58	73	85	87	105
Op. Profit before Working Capital Changes	74	94	125	136	143	165
Adj for Working Capital Changes	2	(11)	(34)	(10)	(7)	(9)
Cash Generated from/(used in) Operations	75	83	91	126	136	156
Direct Taxes Paid	(6)	(10)	(22)	(29)	(30)	(35)
Share of minority Interest	(6)	(7)	(5)	-	-	-
Net cash from operating activities	63	66	64	97	107	121
Net Cash Used in Investing Activities	(99)	(87)	(98)	(91)	(81)	(81)
Net Cash Used in Financing Activities	38	5	75	127	(88)	(59)
Cash generated during the year	2	(16)	40	134	(62)	(19)
Cash and Cash Equivalents at Beginning of the year	21	22	6	47	181	118
Cash and Cash Equivalents at End of the year	23	6	47	181	118	99

Guide to Moneyore's research approach

Valuation methodologies

We apply one absolute valuation methodology and two relative valuation methodologies to triangulate the 'fair value' for the stock assessed fundamentally. The following are the most frequently used valuation methodologies in our research:

DCF: The Discounted Cash Flow (DCF) method values an estimated stream of future free cash flows discounted to the present day, using a company's WACC or cost of equity. This method is used to estimate the attractiveness of an investment opportunity and as such provides a good measure of the company's value in absolute terms. There are several approaches to discounted cash flow analysis, including Free Cash Flow to Firm (FCFF), Free Cash Flow to Equity (FCFE) and the Dividend Discount Model (DDM). The selection of a particular approach depends on the particular company being researched and valued.

Relative valuation: In relative valuation, various comparative multiples or ratios including Price/Earnings, Price/Sales, EV/Sales, EV/EBITDA, Price/Book Value are used to assess the relative worth of companies which operate in the same industry/industries and are thereby in the same peer group. Generally our approach involves the use of two multiples to estimate the relative valuation of a stock.

Other methodologies such as DuPont Analysis and Sum-of-the-Parts (SOTP) are applied where appropriate.

Stock ratings

"Strong Buy" recommendations are expected to improve based on consideration of the fundamental view by at least 15%.

Market-perform recommendations are expected to improve based on consideration of the fundamental view between 5% - 15%.

Underperform recommendations are expected to improve up to 5% or deteriorate, based on consideration of the fundamental view.

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