

Talwalkars Healthclubs Ltd.

No. of shares (m)	31.01
Mkt cap (Rs crs/\$m)	364/53.1
Current price (Rs/\$)	118/1.7
Price target (Rs/\$)	150/2.2
52 W H/L (Rs.)	173/101
Book Value (Rs/\$)	158/2.3
Beta	0.8
Daily NSE volume (avg. monthly)	39460
P/BV (FY19e/20e)	0.7/0.6
EV/EBITDA (FY19e/20e)	3.3/2.8
P/E (FY19e/20e)	4.9/3.9
EPS growth (FY18/19e/20e)	15.1/6.6/26.3
OPM (FY18/19e/20e)	56.3/60.4/62.6
ROE (FY18/19e/20e)	18.7/16.2/17.4
ROCE(FY18/19e/20e)	11.1/11.0/11.8
D/E ratio (FY18/19e/20e)	0.9/0.7/0.6
BSE Code	541545
NSE Code	TALWGYM
Bloomberg	TALWGYM IN

Shareholding pattern

	%
Promoters	37.5
MFs / Banks / FIs	0.6
Foreign Portfolio Investors	1.5
Govt. Holding	-
Public & Others	60.4
Total	100.0

As on Dec 31, 2018

Recommendation

BUY

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Demerger

Talwalkars Better Value Fitness Limited (TBVFL) – the old entity – has demerged its business to two companies- a gym company and a lifestyle company. The gym company, earlier known as ‘Talwalkars Lifestyle Ltd.’ has now been renamed as ‘Talwalkars Healthclubs Ltd.’

Quarterly Highlights

- Talwalkars posted an impressive 35.3% (yoy) growth in its topline in Q3FY19 (contributing to 27.0% of revenue in 9MFY19 vs 23.9% of revenue in the same period last year), thanks to increased revenues from personal training and PWG (Power World Gyms) centres (60 in India at the end of 9MFY19 vs 40 in the same period last year. It has further signed 18-20 agreements under the PWG model last quarter to increase its share in topline going forward.
- Operating margins improved by 184 bps to 41.1% in Q3FY19, due to sturdy growth in revenue and check on operating expenditure. However, de-growth in other income (Rs 0.63 crs/\$0.1m vs Rs 4.57 crs/\$0.7m in Q3FY18), with marginal increase in depreciation and finance cost restricted PBT growth to only 2.0% (yoy). Had it not been for lower taxes, post tax earnings would have failed to post an uptick of 15.9% (yoy) to Rs 4.79 crs (\$0.7m).
- The stock currently trades at 4.9x FY19e EPS of Rs 23.80 and 3.9x FY20e EPS of Rs 30.06. Multi-ownership format of diversified gym business (Talwalkars gym, premium format gyms, HiFi, PWG, Snap Franchise gyms) with a strong presence – 252 gyms across 84 cities as on Dec 31st, 2018 - would help it post topline growth of CAGR 12.8% during FY18-20 period. Favorable long term prospects of the industry aided by low levels of gym penetration, rising disposable income levels and growing awareness about lifestyle diseases among the adult age group bodes well for Talwalkars, which would drive earnings growth at a CAGR of 16.0% over the next two fiscals. Yet, increase in competition and rise in debt due to aggressive expansion strategy – plans are afoot to add 25-30 centres per year and enhance presence in top 10-12 cities- cannot be overlooked. On balance, we recommend ‘buying’ the stock with target price of Rs 150 (previous target Rs 165) based on 5.0x FY20e EPS of Rs 30.06 over a period of 9-12 months.

Consolidated (Rs crs)	FY17	FY18	FY19e	FY20e
Income from operations	225.27	247.09	278.09	314.32
Other Income	1.93	12.16	2.50	2.59
EBITDA (other income included)	127.77	151.39	170.42	199.31
PAT after MI and Associate Profit	57.62	69.21	73.80	93.19
EPS (Rs)	19.40	22.32	23.80	30.06
EPS growth (%)	-	15.1	6.6	26.3

Outlook & Recommendation

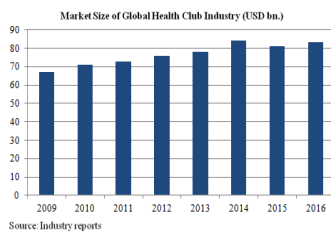
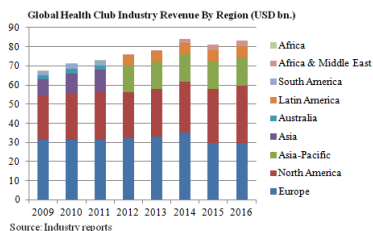
Industry Overview

India's wellness market, pegged at \$13 bn in 2015, is expected to witness CAGR growth of ~12% over the next five years, according to a Deloitte report. Although the industry is largely unorganized, but with global players entering the market and with fitness start-ups and online apps playing a catalytic role- unique combination of fitness and digitization is allowing consumers to enjoy easier access to convenient tech-driven services and products- the industry is likely to post unprecedented growth in the years ahead.

According to the International Health, Racquet & Sportsclub Association (IHRSA), fourteen markets in the Asia-Pacific region attract 22 million members at more than 25,000 clubs. In fitness market rapid growth and professionalism has been observed in Hong Kong, Singapore and Japan. New opportunities have also come to fore in Philippines, Thailand and India. Reflecting an increasing awareness of health and club memberships, the overall fitness market penetration in Asia-Pacific is on an upward trajectory.

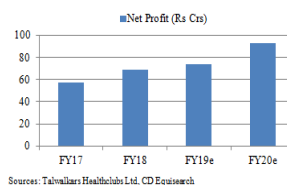
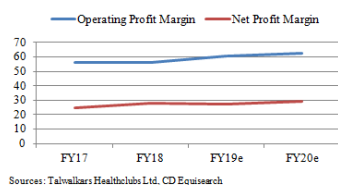
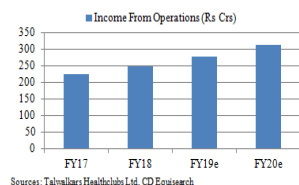
Prompted by trend of greater demand for fitness amenities and gyms, health clubs have become a standard feature at new residential complexes that are being built, not only in metros and tier I cities, but in tier II cities as well. A new corporate culture wherein companies provide fully-equipped gyms and health clubs to employees in the office is enabling many people to look at fitness in a new light- as a fun way to distress after a long day at work rather than a task that must be completed.

Number of upscale fitness centres is burgeoning with rapid rise in disposable income with consumers aged between 20 to 45 years old. Increasing cases of obesity, diabetes and heart disease is one of the key reasons behind surge in health club and gym memberships and also rise in the number of weight loss products available in the market. Furthermore, there is an uptick in number of people in tier-II and tier-III cities opting for wellness and fitness solutions. As a part of the bigger wellness movement being championed by the Indian government, the fitness industry is not only poised to garner more attention, but is also likely to experience unprecedented growth.

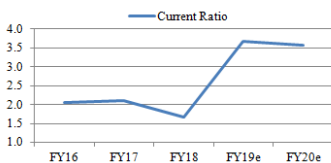


Financials & Valuations

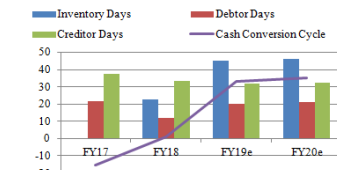
From offering a standard gym experience under a single brand few years ago to offering diverse gym formats across five brands today, Talwalkars has made itself a niche player in the Indian fitness industry. Its revenue increased by 9.7% last fiscal following a large rollout of centres (251 in FY18 vs 211 in FY17) and its ability to understand and service market needs. Although numbers of fitness centres have remained muted at 252 in 9MFY19, increased revenues from personal training and from PWG centres have augmented topline growth to 19.8% (yoy) in 9MFY19.



Post demerger, focus on single line of business is expected to translate into economies of scale and higher profitability. In 9MFY19, operating profit witnessed an uptick of 24.9% (yoy), improving operating margins to 55.0% vs 52.8% in the same period last year. However, PBT growth was restricted to only 8.1% (yoy) because of lower other income (down by 83.8% yoy). Lower taxes allowed post tax profits to increase by 17.1% (yoy). With Talwalkars' expansion plans on cards- we expect it to add a total of 51 gyms in current and next fiscal respectively- it would witness revenue growth of 12.5% and 13.0% in FY19 and FY20 respectively, with net profits up by 6.6% in current fiscal and 26.3% in next fiscal.

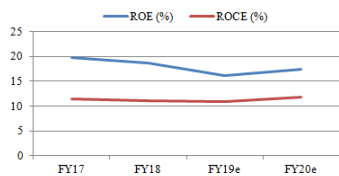


Sources: Talwalkars Healthclubs Ltd, CD Equisearch

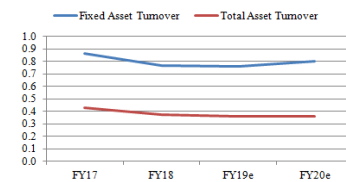


Sources: Talwalkars Healthclubs Ltd, CD Equisearch

Talwalkars enjoys first mover advantage as it is the first within its sector to be professionally organized. Going forward, along with opening new fitness centres (we expect total no of centres to be 273 in FY19 and 302 in FY20), it will focus on escalating same-stores sales growth through higher penetration and increased personal training. It is accelerating expansion via asset-light franchise driven business models and low capex models such as PWG, which would help in reducing capex, thereby containing debt accretion (we expect net D/E to stand at 0.6 and 0.5 in current and next fiscal respectively).

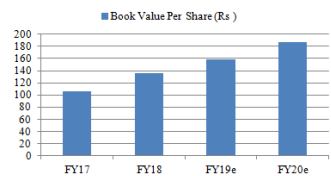


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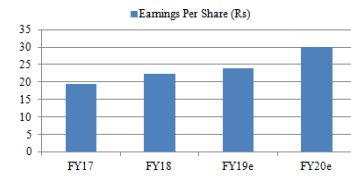


Sources: Talwalkars Healthclubs Ltd, CD Equisearch

On the strategic front, Talwalkars has invested in online app and portals like Growfitter (India's largest health and fitness discovery portal) and Fitternity (India's largest fitness discovery and booking platform) to strengthen its presence in large and growing online market. It introduced 'FitKit', an incentivized wellness mobile app with Growfitter, that tracks individual fitness consistency and maps their performance to generate an incentive oriented and reward based fitness solution. Talwalkars also enhanced its Facebook visibility through digital advertisements and posts.



Sources: Talwalkars Healthclubs Ltd, CD Equisearch



Sources: Talwalkars Healthclubs Ltd, CD Equisearch

The stock currently trades at 4.9x FY19e EPS of Rs 23.80 and 3.9x FY20e EPS of Rs 30.06. Talwalkars is in a sweet spot, marked by strong brand visibility in a growing market. Being the market leader in Indian fitness industry enables it to acquire competing local fitness brands, while retaining their identities and making it possible to sustain their growth, thereby allowing Talwalkars to fast-track its presence in various markets. Its focus on expanding its footprint through alliances and low cost PWG would help it enjoy improved margins – NPM of 27.1% and 29.5% in FY19 and FY20 respectively. In view of its recent performance, we have marginally changed our EPS estimates (Rs 23.80 vs earlier estimate of Rs 25.18 for FY19 and EPS of Rs 30.06 vs earlier estimate of Rs 32.94 for FY20). On balance, we recommend 'buying' the stock with target price of Rs 150 (previous target Rs 165) based on 5.0x FY20e EPS of Rs 30.06 over a period of 9-12 months. For more information, refer to our October 2018 report.

Financials

Standalone Quarterly Results

Figures in Rs crs

	Q3FY19	Q3FY18	% chg	9MFY19	9MFY18	% chg
Revenue From Operations	50.42	37.27	35.3	186.47	155.62	19.8
Other Income	0.63	4.67	-86.4	1.78	11.00	-83.9
Total Income	51.05	41.93	21.7	188.25	166.62	13.0
Total Expenditure	29.69	22.63	31.2	83.84	73.45	14.1
EBITDA (other income incl.)	21.37	19.31	10.7	104.41	93.16	12.1
Interest*	5.90	5.58	5.7	15.39	12.25	25.7
Depreciation	8.85	7.13	24.1	25.12	21.74	15.5
PBT	6.62	6.60	0.4	63.90	59.17	8.0
Tax	1.84	2.40	-23.6	14.41	16.86	-14.5
PAT	4.79	4.20	14.1	49.49	42.31	17.0
Extraordinary Item	-	0.06	-100.0	-	0.04	-100.0
Adjusted Net Profit	4.79	4.13	15.9	49.49	42.27	17.1
EPS (Rs)	1.54	1.33	15.9	15.96	13.63	17.1

Consolidated Income Statement

Figures in Rs crs

	FY17	FY18	FY19e	FY20e
Revenue From Operations	225.27	247.09	278.09	314.32
Other Income	1.93	12.16	2.50	2.59
Total Income	227.20	259.25	280.58	316.92
Total Expenditure	99.43	107.86	110.16	117.61
EBITDA (other income incl.)	127.77	151.39	170.42	199.31
Interest*	11.37	16.68	22.20	21.02
Depreciation	30.23	30.25	34.13	37.84
PBT	86.18	104.45	114.10	140.44
Tax	30.58	35.65	38.79	47.75
PAT	55.60	68.80	75.30	92.69
Profit from Associate	2.89	1.34	2.50	2.50
Minority Interest	1.11	0.87	4.00	2.00
Net Profit after MI & Associate Profit	57.37	69.27	73.80	93.19
Extraordinary Item	-0.25	0.06	-	-
Adjusted Net Profit	57.62	69.21	73.80	93.19
EPS (Rs)	19.40	22.32	23.80	30.06

*Net of interest income from loans/investments

Consolidated Balance Sheet

Figures in Rs crs

	FY17	FY18	FY19e	FY20e
Sources of Funds				
Share Capital	29.71	31.01	31.01	31.01
Reserves & Surplus	300.58	403.21	473.28	562.73
Total Shareholders Funds	330.29	434.22	504.28	593.74
Minority Interest	3.64	2.47	6.47	8.47
Long Term Debt	279.89	300.65	323.96	326.86
Total Liabilities	613.82	737.33	834.71	929.07
Application of Funds				
Gross Block	332.64	418.87	485.60	543.95
Less: Accumulated Depreciation	30.09	59.10	93.22	131.07
Net Block	302.56	359.77	392.37	412.88
Capital Work in Progress	31.32	54.23	40.00	50.00
Investments	57.99	104.22	100.26	102.76
Current Assets, Loans & Advances				
Inventory	-	13.26	13.90	15.72
Trade Receivables	2.24	13.88	16.65	19.98
Cash and Bank	42.72	44.76	46.49	91.96
Other Assets	73.86	83.49	96.07	106.26
Total CA & LA	118.83	155.39	173.11	233.92
Current Liabilities	49.78	88.76	42.86	61.15
Provisions-Short term	1.00	0.01	0.65	0.71
Total Current Liabilities	50.79	88.76	43.51	61.86
Net Current Assets	68.04	66.62	129.60	172.05
Net Deferred Tax	-5.10	-12.28	-9.51	-10.68
Net long term assets	159.00	164.77	181.99	202.06
Total Assets	613.82	737.33	834.71	929.07

Key Financial Ratios

	FY17	FY18	FY19e	FY20e
Growth Ratios (%)				
Revenue	-	9.7	12.5	13.0
EBITDA	-	18.1	12.6	16.9
Net Profit	-	20.1	6.6	26.3
EPS	-	15.1	6.6	26.3
Margins (%)				
Operating Profit Margin	56.0	56.3	60.4	62.6
Gross profit Margin	51.8	54.5	53.3	56.7
Net Profit Margin	24.8	27.8	27.1	29.5
Return (%)				
ROCE	11.5	11.1	11.0	11.8
ROE	19.7	18.7	16.2	17.4
Valuations				
Market Cap/ Sales	-	-	1.3	1.2
EV/EBITDA	-	-	3.3	2.8
P/E	-	-	4.9	3.9
P/BV	-	-	0.7	0.6
Other Ratios				
Interest Coverage	8.6	7.3	6.1	7.7
Debt Equity	1.0	0.9	0.7	0.6
Net Debt Equity	0.9	0.8	0.6	0.5
Current Ratio	2.1	1.7	3.7	3.6
Turnover Ratios				
Fixed Asset Turnover	0.9	0.8	0.8	0.8
Total Asset Turnover	0.4	0.4	0.4	0.4
Debtors Turnover	16.8	30.7	18.2	17.2
Inventory Turnover	-	16.3	8.1	7.9
Creditor Turnover	9.8	10.9	11.5	11.3
WC Ratios				
Debtor Days	21.7	11.9	20.0	21.3
Inventory Days	-	22.4	45.0	46.0
Creditor Days	37.3	33.4	31.8	32.2
Cash Conversion Cycle	-15.5	0.9	33.2	35.1

Cumulative Financial Data

Figures in Rs crs	FY17-18	FY19-20e
Income from operations	472	592
Operating profit	265	365
EBIT	219	298
PBT	191	255
PAT after MI and AP	127	167
Dividends	9	7
OPM (%)	56.2	61.6
NPM (%)	26.4	28.4
Interest coverage	7.8	6.9
ROE (%)	18.4	16.7
ROCE (%)	11.3	11.2
Debt Equity	0.9	0.6
Fixed asset turnover	0.8	0.8
Debtors turnover	12.3	17.5
Inventory turnover	15.6	7.9
Creditors turnover	10.7	11.1
Debtor days	29.7	20.9
Inventory days	23.4	46.4
Creditor days	34.3	32.8
Cash conversion	18.9	34.5
Dividend payout ratio (%)	7.4	4.6

FY17-18 implies two year period ending fiscal 18.

Talwalkars, one of India's leading fitness providers, has continued its expansion strategy to tap the growing and underpenetrated fitness market in the country. With 251 gyms in FY18, it plans to increase the rollout of gyms (we expect 306 gyms by FY20) and widen its customer base, which would garner topline growth of 1.3x in FY19-20 period. To sustain its strong foothold in the industry and consolidate its leadership position across South East Asia, it plans to expand both organically and inorganically.

As it capitalizes on franchise opportunity and the right mix of low capex and opex models (like PWG), we expect it to sustain accretion in margins- OPM and NPM of 61.6% and 28.4% respectively in the projected period. Higher profitability – up by 1.3x - would keep ROCE unchanged (see table). Due to check on debt acceleration and expansion of net worth, debt equity ratio would moderate to 0.6.

Financial Summary- US Dollar denominated

million \$	FY17	FY18	FY19e	FY20e
Equity capital	4.6	4.8	4.5	4.5
Shareholders funds	48.9	65.0	71.4	84.4
Total debt	48.2	57.3	50.7	53.4
Net fixed assets (including CWIP)	50.3	62.4	61.5	65.9
Investments	8.9	16.0	14.6	15.0
Net current assets	9.7	9.7	18.3	24.5
Total assets	92.6	111.6	119.5	133.3
Revenues	33.6	38.3	40.5	45.8
EBITDA	19.1	23.5	24.8	29.0
EBDT	17.4	20.9	21.6	26.0
PBT	12.9	16.2	16.6	20.5
Profit after MI & EO	8.6	10.7	10.7	13.6
EPS(\$)	0.29	0.35	0.35	0.44
Book value (\$)	1.65	2.10	2.30	2.72

Income statement figures translated at average rates; balance sheet at year end rates; projections at current rates (Rs 68.66/\$).
All dollar denominated figures are adjusted for extraordinary items.

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buy: >20% accumulate: >10% to ≤20% hold: ≥-10% to ≤10% reduce: ≥-20% to <-10% sell: <-20%

Exchange Rates Used- Indicative

Rs/\$	FY17	FY18
Average	67.09	64.45
Year end	64.84	65.04

All \$ values mentioned in the write-up translated at the average rate of the respective quarter/ year as applicable. Projections converted at current exchange rate. Cumulative dollar figure is the sum of respective yearly dollar value.