

Strong momentum drives earnings upgrade

Earnings momentum and reasonable valuation; reiterate Buy with TP of INR1,090

July 29, 2013

Rating	Buy
Remains	
Target price	INR 1090
Increased from 990	
Closing price	INR 908
July 26, 2013	
Potential upside	+20%

Action: Reiterate Buy on strong confidence into 2HCY13

Post strong 2QCY13 results, we have revisited our assumptions for Bata and believe the company will outperform our previous expectations over the next year or so. This confidence is backed by positive management commentary on the growth outlook, both near term and medium term. Our previous margins assumptions were conservative, thus we have made revisions to build in a 40bp improvement for both CY13F and CY14F. Our TP moves from INR990 to INR1,090 on our earnings revisions of 3-5% for CY13-15F and the rolling forward of our valuation by one quarter.

Catalysts: Strong volume growth and pick-up in margins

There is some apprehension that footwear, being a discretionary category, will see a sharp deceleration in growth in the current weak macro environment. However, as the 1HCY13 results indicate, Bata has been successful in maintaining growth in the tough market environment. Commentary suggests a pick-up in 2HCY13, which would be a key catalyst for stock price performance over the next year.

Valuation: Bata trades at 24x CY14F P/E

Bata trades at 24x CY14F P/E, vs the consumer sector which trades at a ~29.6x FY15F. We estimate Bata will deliver ~20% pa earnings growth over the next couple of years, driven by strong top-line growth of 17-18% pa and margin expansion of 40bps pa over CY13-14F. Given the reasonable valuations, strong commentary from management and potential for margins to surprise on the upside, we believe investors should own Bata at these levels.

Anchor themes

Bata is the market leader in India's organised footwear market, as per the company. The company has the widest portfolio of products across segments and price points, which gives it a strong competitive edge vs smaller domestic players as well as MNCs.

Nomura vs consensus

We are largely in line with consensus for CY14/15F on EPS. However, improvement in realisations could surprise on the upside.

Research analysts

India Consumer Related

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31 Dec	FY12	FY13F		FY14F		FY15F	
Currency (INR)	Actual	Old	New	Old	New	Old	New
Revenue (mn)	18,412	21,477	21,697	25,270	25,525	29,762	30,059
Reported net profit (mn)	1,715	1,946	2,004	2,307	2,427	2,784	2,927
Normalised net profit (mn)	1,690	1,946	2,004	2,307	2,427	2,784	2,927
FD normalised EPS	26.30	30.28	31.19	35.89	37.77	43.31	45.54
FD norm. EPS growth (%)	45.7	15.1	18.6	18.5	21.1	20.7	20.6
FD normalised P/E (x)	34.5	N/A	29.1	N/A	24.0	N/A	19.9
EV/EBITDA (x)	20.6	N/A	16.8	N/A	13.7	N/A	11.3
Price/book (x)	8.3	N/A	7.0	N/A	5.9	N/A	4.9
Dividend yield (%)	0.8	N/A	1.2	N/A	1.5	N/A	1.7
ROE (%)	26.9	25.5	26.2	25.7	26.7	26.3	27.0
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash	net cash	net cash

Key company data: See page 2 for company data and detailed price/index chart.

See Appendix A-1 for analyst certification, important disclosures and the status of non-US analysts.

Key data on Bata India

Income statement (INRmn)

Year-end 31 Dec	FY11	FY12	FY13F	FY14F	FY15F
Revenue	15,409	18,412	21,697	25,525	30,059
Cost of goods sold	-7,265	-8,680	-10,197	-11,920	-14,037
Gross profit	8,143	9,731	11,499	13,605	16,021
SG&A	-4,408	-5,541	-6,707	-7,978	-9,475
Employee share expense	-1,859	-1,959	-2,155	-2,371	-2,608
Operating profit	1,877	2,231	2,636	3,257	3,939
EBITDA	2,288	2,744	3,323	4,020	4,796
Depreciation	-411	-514	-686	-764	-858
Amortisation	0	0	0	0	0
EBIT	1,877	2,231	2,636	3,257	3,939
Net interest expense	-9	-10	-10	-10	-10
Associates & JCEs	0	0	0	0	0
Other income	227	274	321	323	375
Earnings before tax	2,096	2,494	2,948	3,569	4,304
Income tax	-936	-804	-943	-1,142	-1,377
Net profit after tax	1,160	1,690	2,004	2,427	2,927
Minority interests	0	0	0	0	0
Other items	0	0	0	0	0
Preferred dividends	0	0	0	0	0
Normalised NPAT	1,160	1,690	2,004	2,427	2,927
Extraordinary items	1,098	25	0	0	0
Reported NPAT	2,258	1,715	2,004	2,427	2,927
Dividends	-447	-448	-694	-849	-1,003
Transfer to reserves	1,811	1,267	1,310	1,578	1,924

Valuation and ratio analysis

Reported P/E (x)	25.8	34.0	29.1	24.0	19.9
Normalised P/E (x)	50.3	34.5	29.1	24.0	19.9
FD normalised P/E (x)	50.3	34.5	29.1	24.0	19.9
FD normalised P/E at price target (x)	54.8	37.6	31.7	26.2	21.7
Dividend yield (%)	0.8	0.8	1.2	1.5	1.7
Price/cashflow (x)	81.7	24.7	26.9	20.5	18.8
Price/book (x)	10.2	8.3	7.0	5.9	4.9
EV/EBITDA (x)	25.0	20.6	16.8	13.7	11.3
EV/EBIT (x)	30.4	25.3	21.2	16.9	13.7
Gross margin (%)	52.8	52.9	53.0	53.3	53.3
EBITDA margin (%)	14.8	14.9	15.3	15.7	16.0
EBIT margin (%)	12.2	12.1	12.2	12.8	13.1
Net margin (%)	14.7	9.3	9.2	9.5	9.7
Effective tax rate (%)	44.6	32.2	32.0	32.0	32.0
Dividend payout (%)	19.8	26.1	34.6	35.0	34.3
Capex to sales (%)	2.8	4.9	4.5	3.7	3.3
Capex to depreciation (x)	1.0	1.8	1.4	1.2	1.1
ROE (%)	na	26.9	26.2	26.7	27.0
ROA (pretax %)	26.6	26.8	27.0	28.9	30.6

Growth (%)

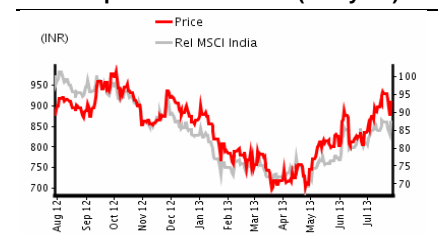
Revenue	22.6	19.5	17.8	17.6	17.8
EBITDA	36.1	19.9	21.1	21.0	19.3
EBIT	38.4	18.8	18.2	23.5	20.9
Normalised EPS	21.1	45.7	18.6	21.1	20.6
Normalised FDEPS	21.1	45.7	18.6	21.1	20.6

Per share

Reported EPS (INR)	35.13	26.69	31.19	37.77	45.54
Norm EPS (INR)	18.05	26.30	31.19	37.77	45.54
Fully diluted norm EPS (INR)	18.05	26.30	31.19	37.77	45.54
Book value per share (INR)	89.37	108.98	129.36	153.92	183.86
DPS (INR)	6.96	6.97	10.81	13.21	15.61

Source: Company data, Nomura estimates

Relative performance chart (one year)



Source: ThomsonReuters, Nomura research

(%)	1M	3M	12M
Absolute (INR)	12.7	27.1	1.3
Absolute (USD)	15.3	16.6	-3.8
Relative to index	6.5	25.2	-17.5
Market cap (USDmn)	989.0		
Estimated free float (%)	48.0		
52-week range (INR)	989.5/686.85		
3-mth avg daily turnover (USDmn)	5.15		
Major shareholders (%)			
Bata BNBV	52.0		
FID Funds	4.1		

Source: Thomson Reuters, Nomura research

Notes

Cashflow (INRmn)

Year-end 31 Dec	FY11	FY12	FY13F	FY14F	FY15F	Notes
EBITDA	2,288	2,744	3,323	4,020	4,796	
Change in working capital	-1,449	-69	-256	-193	-529	
Other operating cashflow	-126	-317	-897	-984	-1,166	
Cashflow from operations	714	2,358	2,169	2,843	3,101	
Capital expenditure	-428	-906	-984	-952	-978	
Free cashflow	285	1,453	1,185	1,891	2,123	
Reduction in investments		0	0	0	0	
Net acquisitions						
Reduction in other LT assets		-125	-219	-252	-298	
Addition in other LT liabilities		-101	0	0	0	
Adjustments						
Cashflow after investing acts	285	1,227	967	1,639	1,825	
Cash dividends	-299	-447	-448	-694	-849	
Equity issue	0	0	0	0	0	
Debt issue	-113	-138	0	0	0	
Convertible debt issue	0	0	0	0	0	
Others						
Cashflow from financial acts	-412	-585	-448	-694	-849	
Net cashflow	-127	642	518	945	976	
Beginning cash	1,356	1,229	1,871	2,389	3,334	
Ending cash	1,229	1,871	2,389	3,334	4,311	
Ending net debt	-1,229	-1,871	-2,389	-3,334	-4,311	

Source: Company data, Nomura estimates

Balance sheet (INRmn)

As at 31 Dec	FY11	FY12	FY13F	FY14F	FY15F	Notes
Cash & equivalents	1,229	1,871	2,389	3,334	4,311	
Marketable securities	49	49	49	49	49	
Accounts receivable	355	518	594	699	824	
Inventories	3,913	4,621	5,528	6,504	7,659	
Other current assets	0	0	0	0	0	
Total current assets	5,546	7,058	8,561	10,586	12,841	
LT investments						
Fixed assets	2,271	2,595	2,911	3,100	3,220	
Goodwill	0	0	0	0	0	
Other intangible assets	0	0	0	0	0	
Other LT assets	1,083	1,208	1,427	1,678	1,976	
Total assets	8,900	10,861	12,899	15,364	18,038	
Short-term debt	0	0	0	0	0	
Accounts payable	2,782	3,506	4,161	4,895	5,765	
Other current liabilities	717	795	868	1,021	902	
Total current liabilities	3,499	4,301	5,029	5,916	6,666	
Long-term debt	0	0	0	0	0	
Convertible debt	0	0	0	0	0	
Other LT liabilities	-342	-444	-444	-444	-444	
Total liabilities	3,157	3,857	4,585	5,473	6,223	
Minority interest	0	0	0	0	0	
Preferred stock	0	0	0	0	0	
Common stock	643	643	643	643	643	
Retained earnings	5,100	6,361	7,671	9,249	11,173	
Proposed dividends	0	0	0	0	0	
Other equity and reserves						
Total shareholders' equity	5,743	7,003	8,313	9,892	11,815	
Total equity & liabilities	8,900	10,861	12,899	15,364	18,038	

Liquidity (x)

Current ratio	1.58	1.64	1.70	1.79	1.93
Interest cover	215.8	216.1	263.6	325.7	393.9

Leverage

Net debt/EBITDA (x)	net cash	net cash	net cash	net cash	net cash
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash

Activity (days)

Days receivable	7.8	8.7	9.4	9.3	9.2
Days inventory	173.5	179.9	181.6	184.2	184.1
Days payable	148.5	132.6	137.2	138.7	138.6
Cash cycle	32.7	56.0	53.8	54.8	54.8

Source: Company data, Nomura estimates

Strong 2QCY13 results

- Net sales increased 13% y-y to INR5.7bn, against our expectation of INR5.7bn.
- EBITDA came in at INR961mn, vs Nomura estimate of INR973bn.
- EBITDA margin came in at 16.8%, up 20bps y-y. We were expecting EBITDA margin at 17% (flat y-y).
- The key negative surprise was other overheads, up 18% y-y to 14.8% (Nomura estimate of 14.3%).
- PAT came in at INR619mn, against our expectation of INR603mn – a beat of ~3% to our and Street numbers.

Fig. 1: Key numbers from Q2CY13 results

(INR mn)	Quarter ended				
	Jun-13	Jun-12	% Chg	Mar-13	% Chg
Net Sales	5,725	5,065	13.0	4,539	26.1
EBIDTA	961	859	11.8	629	52.8
Other income	78	40	94.8	69	11.7
PBIDT	1,038	899	15.5	698	48.7
Depreciation	141	124	13.6	131	7.7
Interest	2	2	N.A	2	N.A
PBT	895	773	15.8	565	58.4
Tax	276	247	11.8	180	52.7
Adjusted PAT	619	527	17.6	385	61.0
Extra ordinary income/ (exp.)	0	0	N.A	0	N.A
Reported PAT	619	527	17.6	385	61.0
No. of shares (mn)	64	64		64	
EBIDTA margins (%)	16.8	17.0		13.9	
PBIDT margins (%)	18.1	17.7		15.4	
EPS (INR)	9.6	8.2	17.6	6.0	61.0
INR mn	Jun-13	Jun-12	% Chg	Mar-13	% Chg
Net Sales	5,725	5,065	13.0	4,539	26.1
EBIDTA	961	859	11.8	629	52.8
Other income	78	40	94.8	69	11.7
PBIDT	1,038	899	15.5	698	48.7
Depreciation	141	124	13.6	131	7.7
Interest	2	2	N.A	2	N.A
PBT	895	773	15.8	565	58.4
Tax	276	247	11.8	180	52.7
Adjusted PAT	619	527	17.6	385	61.0
Extra ordinary income/ (exp.)	0	0	N.A	0	N.A
Reported PAT	619	527	17.6	385	61.0
No. of shares (mn)	64	64		64	
EBIDTA margins (%)	16.8	17.0		13.9	
PBIDT margins (%)	18.1	17.7		15.4	
EPS (INR)	9.6	8.2	17.6	6.0	61.0

Source: Company data, Nomura Research

Management commentary

- Plans to add 100 new format stores in CY13F which will all be more than an average of 3,000 sq ft.

- So far in the current quarter, it has opened 15 new stores, all in major metro cities.
- To quote the management: **"We are confident our momentum will accelerate in line with our expectations as we move through the year."**

Confidence for delivery in 2HCY13

Management commentary indicated strong confidence that growth will pick up in 2HCY13, driven by:

- Management's execution capabilities, even in a tough market environment.
- Relatively low comps in 3QCY13 when looked at on a y-y basis.

While the market environment for consumer demand (discretionary as well as non-discretionary) remains weak, companies with better execution capabilities should outperform. We believe Bata certainly falls into that category with its proven management capabilities to steer the business through various cycles. This has clearly been demonstrated by company's performance during the past five years.

If we look at the comps from 3QCY12, revenue growth was +14.5% y-y but as a result of sharp deterioration in margins (average margin -150bps y-y in 2HCY12). This margin deterioration was driven by lower gross margin in 3QCY12 as well as a significant increase in rental cost.

We believe 3QCY13F will see more normalised trends and although we are building in an increase in rental costs as a percentage of sales, we do not expect the increase to be as sharp as in 3QCY12. Considering the trends since 3QCY12 when net profit grew by only 5.3% y-y and the company's strong commentary, we expect net income growth to be close to ~25% y-y in 3QCY13F.

Margins in 3QCY12 were 12%, which are a soft comp on a y-y basis. In 3QCY13F, we expect the company to report margins of 13.4%, with further upside risk to that number.

Fig. 2: Q3 comps are relatively soft both on margins and net income

INR mn	Q3CY12	Q3CY13F
Revenues	4,235	4,871
Growth (%)	14.5%	15.0%
EBITDA	510	653
EBITDA Margins (%)	12.0%	13.4%
Net Income	320	405
Growth (%)	5.3%	26.2%
INR mn	Q3CY12	Q3CY13F
Revenues	4,235	4,871
Growth (%)	14.5%	15.0%
EBITDA	510	653
EBITDA Margins (%)	12.0%	13.4%
Net Income	320	405
Growth (%)	5.3%	26.2%

Source: Company data, Nomura estimates

Change to our earnings estimates

Taking into account the robust 1HCY13 performance and the company's confidence on medium-term growth, we have made some changes to our assumptions. Key changes are:

- Revenue growth of 17.8% in CY13F, vs our earlier expectation of 16.6%, mainly on the strong sales growth in 1HCY13.
- EBITDA margin of 15.4% (+40bps y-y vs CY12), against our earlier expectation of 15%. We also assume the improvement in margins will continue into CY14F with a 40bps improvement against our earlier expectation of margins remaining flat. As detailed in

our 2 July 2013 initiation report, *Taking the right steps*, the company has a well established strategy to improve margins – 6% in CY06 to 15% in CY12.

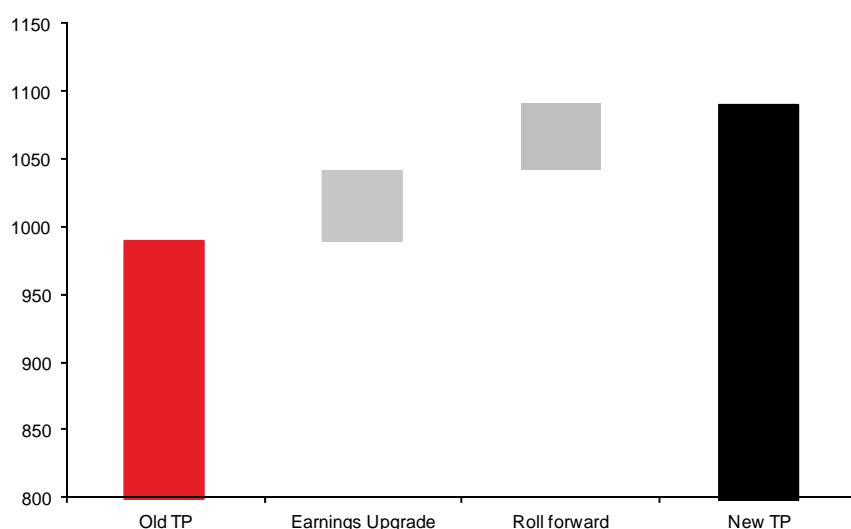
After a pause for a year where margins held stable, we believe the upward trajectory will resume with a steady but sustainable margin expansion. The key factors driving this will likely be an improvement in the mix (higher share of leather vs rubber shoes) as well as cost cutting initiatives, including outsourcing more production vs manufacturing in-house. The company is also investing significant money to increase its distribution which should widen the gap between Bata and its competitors in India.

- Our net income estimates move up by 3-5% for CY13-CY15F as a result of these changes. We now expect a ~20% earnings CAGR over CY13-15F, vs average earnings growth for the sector of close to 17-18%.

TP moves higher on earnings upgrade and roll forward

Our TP moves from INR990 to INR1,090, an upgrade of 10%. This is driven primarily by 5% earnings upgrades to our CY14F/15F numbers and rolling forward our valuation by one quarter. Our target P/E for Bata remains unchanged at 25x on one-year forward earnings.

Fig. 3: Change in TP driven both by earnings and rolling forward



Source: Nomura research

Valuation comfort adds to attractiveness

Together with solid business fundamentals over the next couple of years, valuation is another comforting factor, in our view, on Bata India. The company trades at 24x CY14F earnings, vs the market-cap weighted sector average of ~29.6x for FY15F. We believe within the context of expensive valuations in the sector, Bata offers a relatively cheap option of gaining exposure to the consumption story in India.

Fig. 4: Consumer sector valuation

Company	Ticker	Rating	Price INR	EPS growth FY14E %	EPS growth FY15E %	FY14E P/E	FY15E P/E	FY14E PEG	FY15E PEG
Nestle *	NEST IN	Neutral	5,450	22%	23%	35.7x	29.1x	1.6x	1.3x
GSK Consumer *	SKB IN	Reduce	5,013	20%	21%	41.1x	34.1x	2.0x	1.7x
Jubilant Foodworks	JUBI IN	Reduce	1,150	20%	27%	47.9x	37.6x	2.4x	1.4x
United Spirits	UNSP IN	Buy	2,587	139%	49%	53.7x	36.0x	0.4x	0.7x
F&B Average						42.8x	32.6x		
Colgate Palmolive	CLGT IN	Reduce	1,444	13%	14%	35.1x	30.8x	2.6x	2.2x
Dabur	DABUR IN	Buy	172	20%	18%	32.2x	27.3x	1.6x	1.5x
Godrej Consumer	GCPL IN	Buy	862	24%	24%	30.5x	24.6x	1.3x	1.0x
Hindustan Unilever	HUVR IN	Reduce	664	12%	10%	39.7x	36.0x	3.3x	3.5x
Marico	MRCO IN	Buy	217	39%	22%	27.8x	22.8x	0.7x	1.0x
Emami	HMN IN	Buy	497	25%	20%	28.1x	23.5x	1.1x	1.2x
HPC Average						36.1x	31.9x		
ITC	ITC IN	Buy	368	19%	19%	32.2x	27.1x	1.7x	1.5x
Asian Paints	APNT IN	Neutral	5,076	27%	19%	35.4x	29.6x	1.3x	1.5x
Titan Industries	TTAN IN	Neutral	261	10%	19%	27.4x	23.0x	2.7x	1.2x
Bata India	BATA IN	Buy	908	19%	21%	29.1x	24.0x	1.6x	1.1x
Retail Average						27.7x	23.2x		

Source: Company data, Nomura estimates. Note: * indicates calendar year based valuations. Pricing as on 26 July 2013

Appendix A-1

Analyst Certification

We, Manish Jain and Anup Sudhendranath, hereby certify (1) that the views expressed in this Research report accurately reflect our personal views about any or all of the subject securities or issuers referred to in this Research report, (2) no part of our compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this Research report and (3) no part of our compensation is tied to any specific investment banking transactions performed by Nomura Securities International, Inc., Nomura International plc or any other Nomura Group company.

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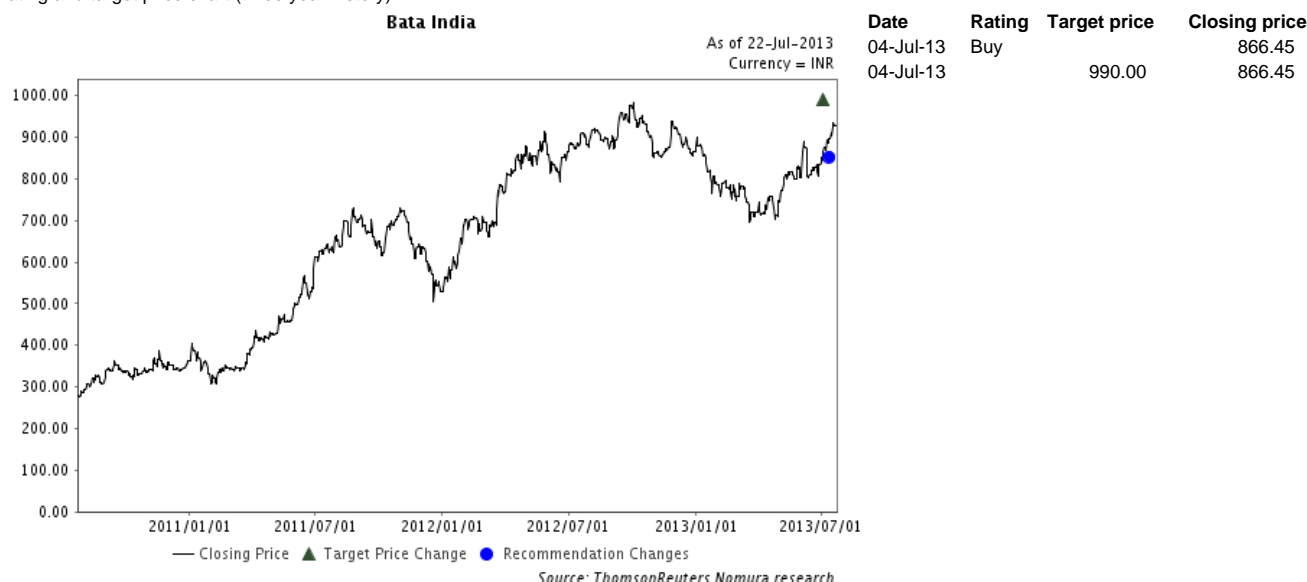
Materially mentioned issuers

Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Bata India	BATA IN	INR 908	26-Jul-2013	Buy	Not rated	

Bata India (BATA IN)

INR 908 (26-Jul-2013) Buy (Sector rating: Not rated)

Rating and target price chart (three year history)



For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology We value the company at 25x one-year forward EPS of INR43.6. The multiple we assign to Bata is similar to the multiples we assign to other mid-cap consumer companies. Our target price is INR1,090.

Risks that may impede the achievement of the target price Spending on footwear is highly leveraged to discretionary spend, which could be hit if GDP growth slows. High rental costs could mean margins taking a hit.

Important Disclosures

Online availability of research and conflict-of-interest disclosures

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Explanation of Nomura's equity research rating system in Europe, Middle East and Africa, US and Latin America

The rating system is a relative system indicating expected performance against a specific benchmark identified for each individual stock. Analysts may also indicate absolute upside to target price defined as (fair value - current price)/current price, subject to limited management discretion. In most cases, the fair value will equal the analyst's assessment of the current intrinsic fair value of the stock using an appropriate valuation methodology such as discounted cash flow or multiple analysis, etc.

STOCKS

A rating of '**Buy**', indicates that the analyst expects the stock to outperform the Benchmark over the next 12 months. A rating of '**Neutral**', indicates that the analyst expects the stock to perform in line with the Benchmark over the next 12 months. A rating of '**Reduce**', indicates that the analyst expects the stock to underperform the Benchmark over the next 12 months. A rating of '**Suspended**', indicates that the rating, target price and estimates have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including, but not limited to, when Nomura is acting in an advisory capacity in a merger or strategic transaction involving the company.

Benchmarks are as follows: **United States/Europe**: please see valuation methodologies for explanations of relevant benchmarks for stocks, which can be accessed at: <http://go.nomuranow.com/research/globalresearchportal/pages/disclosures/disclosures.aspx>; **Global Emerging Markets (ex-Asia)**: MSCI Emerging Markets ex-Asia, unless otherwise stated in the valuation methodology.

SECTORS

A '**Bullish**' stance, indicates that the analyst expects the sector to outperform the Benchmark during the next 12 months. A '**Neutral**' stance, indicates that the analyst expects the sector to perform in line with the Benchmark during the next 12 months. A '**Bearish**' stance, indicates that the analyst expects the sector to underperform the Benchmark during the next 12 months. Benchmarks are as follows: **United States**: S&P 500; **Europe**: Dow Jones STOXX 600; **Global Emerging Markets (ex-Asia)**: MSCI Emerging Markets ex-Asia.

Explanation of Nomura's equity research rating system in Japan and Asia ex-Japan

STOCKS

Stock recommendations are based on absolute valuation upside (downside), which is defined as (Target Price - Current Price) / Current Price, subject to limited management discretion. In most cases, the Target Price will equal the analyst's 12-month intrinsic valuation of the stock, based on an appropriate valuation methodology such as discounted cash flow, multiple analysis, etc. A '**Buy**' recommendation indicates that potential upside is 15% or more. A '**Neutral**' recommendation indicates that potential upside is less than 15% or downside is less than 5%. A '**Reduce**' recommendation indicates that potential downside is 5% or more. A rating of '**Suspended**' indicates that the rating and target price have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including when Nomura is acting in an advisory capacity in a merger or strategic transaction involving the subject company. Securities and/or companies that are labelled as '**Not rated**' or shown as '**No rating**' are not in regular research coverage of the Nomura entity identified in the top banner. Investors should not expect continuing or additional information from Nomura relating to such securities and/or companies.

SECTORS

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Target Price

A Target Price, if discussed, reflects in part the analyst's estimates for the company's earnings. The achievement of any target price may be impeded by general market and macroeconomic trends, and by other risks related to the company or the market, and may not occur if the company's earnings differ from estimates.

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