Talwalkars Better Value Fitness Limited	
No. of shares (m)	29.7
Mkt cap (Rs crs/$m)	798/118.9
Current price (Rs/$)	269/4.0
Price target (Rs/$)	338/5.0
52 W H/L (Rs.)	290/182
Book Value (Rs/$)	145/2.2
Beta	1.2
Daily volume (avg. monthly)	160910
P/BV (FY17e/18e)	1.6/1.4
P/E (FY17e/18e)	12.1/9.5
EPS growth (FY16/17e/18e)	8.5/16.6/26.6
ROE (FY16/17e/18e)	15.8/14.6/16.0
OPM(FY16/17e/18e)	57.1/56.0/57.0
Net D/E ratio (FY16/17e/18e)	.5/.4/.2
BSE Code	533200
NSE Code	TALWALKARS
Bloomberg	TALW IN
Reuters	TALW.BO

Shareholding pattern	%
Promoters	38.0
MFs / Banks / FIs	5.4
Foreign	14.4
Govt. holding	-
Public & others	42.2
Total	**100.0**

As on June 30, 2016

Recommendation

BUY

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Company Brief

Talwalkars is a leader in the Indian fitness industry with centers across India offering gymming and fitness. The company's fitness centers operate under three major formats- premium, Talwalkars and HiFi (budget format located in non-metros). It has continuously focused on generating greater same- store sales growth over the need to implement new fitness centers.

Quarterly Highlights

- Q1FY17 saw a muted addition of 3000-4000 members and 1 new gym only. The heat wave in India during the month of April-June hampered the growth of the business- revenues grew by a mere 11.9%.
- Over the last four-six quarters, franchisee has become an integral part of the company's operations. Out of the 177 gyms owned/ operated by it, almost 50-55 gyms are in the franchisee model. Going ahead, the company plans to add another 12-15 gyms under the same model which will be operational within the next three quarters.
- In the fiscal 2016, the company added 26 gyms, out of which 20 were from the associate company in Sri Lanka. Going forward the company expects the value added services to grow and contribute more to the total revenue.
- The GPMs went north of 50% for the first time since FY11 supported by a lesser increase in costs (6.6% y-o-y) in comparison with the increase in total revenue (11.4% y-o-y). The cash conversion cycle of 6 days in FY16 is expected to rise to 9 days this fiscal. ROE declined from 18.1% in FY15 to 15.8% in FY16.
- The stock currently trades at 12.1x FY17e EPS of Rs 22.27 and 9.5x FY18e EPS of Rs 28.20. The intention to forge a joint venture with David Lloyd Leisure (Europe's leading premium sports, health and leisure group) for the development of 7-10 clubs in India along with demerger - one focusing on gyms and the other focusing on properties and value added services- is symptomatic of renewed business focus. Transformation into a wellness company (better services and infrastructure) will further make its offerings more eclectic. Growing disposable income and awareness regarding fitness augurs well for the business expansion. Average earnings growth of 21.5% over the next two years is doubtless worthy of notice. We retain 'buy' rating on the stock with a revised target of Rs. 338 (previous target Rs 319) implying a 12x FY18e EPS over a period of 9-12 months. (PEG ratio: 0.6)

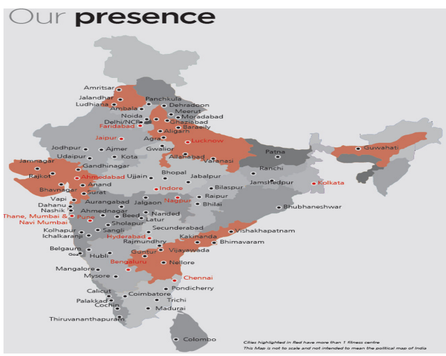
Figures (Rs crs)	FY14	FY15	FY16	FY17e	FY18e
Income from operations	187.27	225.66	251.37	302.29	356.34
Other Income	1.08	0.85	6.76	6.79	8.88
EBIDTA (other income included)	93.76	125.38	150.27	176.07	212.00
PAT after MI & Associate profit	36.60	46.07	55.04	66.15	83.76
EPS (Rs.)	13.98	17.60	19.09	22.27	28.20
EPS growth (%)	14.6	25.9	8.5	16.6	26.6

Outlook & Recommendation

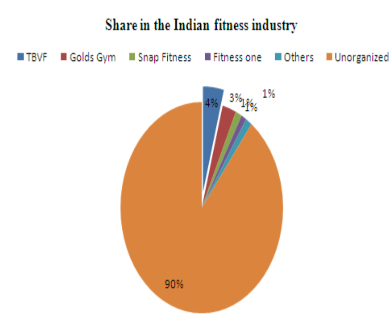
Outlook of Fitness Industry

The fitness and slimming market in India has witnessed a remarkable transformation over the years probably due to the change in the lifestyle of the urban middle class. Desk-bound lifestyles, rising disposable incomes and rising awareness pertaining to 'healthy' lifestyles are major factors driving the fitness industry. Analysts predict that the entire sector is set to grow annually by 20-30% y-o-y. Along with fitness, a new trend of complete wellness is gaining ground within the age group of 20-44. These people are trying out various ways to stay fit such as Zumba, aerial yoga, pilates, mixed martial arts and kickboxing, among others. All across India, various startups are trying to consolidate this disintegrated industry to offer exclusive solutions to people wanting to stay fit. The Central Government has established a separate Ministry called AYUSH to propagate natural healthcare and yoga among the masses. In the wake of this there has been a 30% rise in memberships across fitness centers in metro cities. Currently, there are ~3,800 fitness and health clubs in India. New fitness centre chains and fitness clubs are deepening their footprints across metros. (Sources: Statistia, Economic Times, The Hindu Business Line, IHSRA Global Report, 2016)

India ranks third globally when it comes to obesity. Cardiovascular diseases, hypertension and stress afflict vast percentage of the population. India also has the highest number of diabetics in the world. There is an urgent need to raise awareness about the need for staying fit. A lack of awareness regarding the long-term economic benefits of joining a fitness centre and a penchant for laziness has held back most from getting into shape. However, this is likely to change.



Countries	Total Industry Revenue (USD in Mn)	Total #Clubs	Total # of member (mn)
China (Mainland),Taiwan, Hongkong	2,820	3,193	4.76
Brazil	2,442	31,809	7.95
India	669	3,800	0.95
Poland	492	2,500	1.00
Portugual	391	1,200	0.65
Egypt	210	936	0.50
Vietnam	27	2,325	0.14



Source: Talwalkars Source: IHRSA Global Report, 2015, Talkwalkars Source: Talwalkars

A significant chunk of the Indian population falls within the age group of 20-30. They are far more focused on staying fit than their predecessors, thanks to the rising levels of disposable incomes. The long-held notion that fitness means bulging muscles and food supplements are slowly giving way as more people are turning to alternative means such as kickboxing, mixed martial arts, yoga and dance, among others, to get in shape and stay fit.

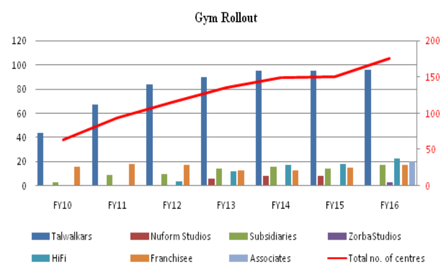
The rise in the number of lifestyle diseases has reaffirmed the necessity for staying fit. The media (AV and web) have also played a major role in raising awareness. The Central Government's efforts towards promoting yoga and various celebrity endorsements have also made people aware regarding the benefits of a healthy lifestyle and a fit body. Companies have started leveraging social media platforms by publishing informative and interactive pages.

With cities promoting the culture of 'fitness' and becoming a breeding ground of state-of-the-art fitness centers and studios, the people migrating to cities are automatically adopting this culture. Currently, the major cities of India are home to approximately 300 mn people and the number is expected to double over the next 20 years, making urban centers a thriving market for fitness in India.

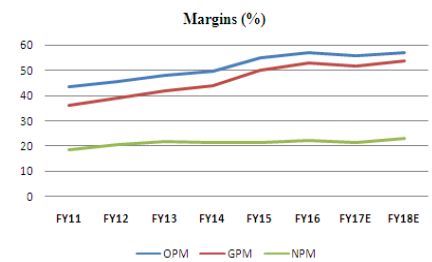
Financials and Valuations

Realizing the need to combine health with a fun-filled, exciting and energetic fitness regimen, Talwalkars is on the path to continuously reinvent the way people look at fitness. The scale and the reach at which Talwalkars operate will aid it in pursuing inorganic growth, give access to newer markets, strengthen its presence in the existing markets and help it achieve a larger scale within a short time frame.

Even though the entire India was reeling under the heat wave in April-June, the company showed better than expected operating margins. The attractive 'Beat the heat' plan contributed to the top line. Summers usually keep the operating margins south of 50% but it was not the case in Q1FY17. Quarterly operating costs reduced by 6.8% y-o-y due to slightly higher productivity and effective cost management.



Source: Talwalkars, CD Equisearch



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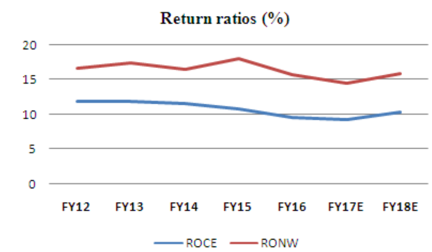
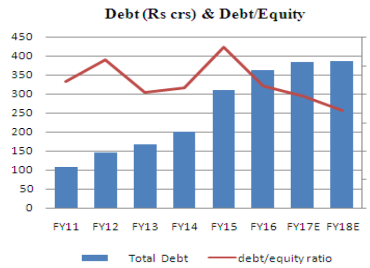


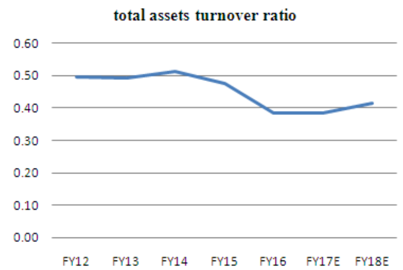
Source: Talwalkars, CD Equisearch

The company benefited from its alliance with PWG gym in Sri Lanka and this is reflected in the bottom line. Value added services like Zorba, Nuform, Reduce, Transform etc, provided impetus in the first quarter of FY17. To improve profitability and co-ordination, seven gyms which were earlier owned by subsidiaries were taken over by entering into MOUs with those subsidiaries. Zorba was offered across many centers, especially in Chennai, Bangalore, Mumbai and Hyderabad.

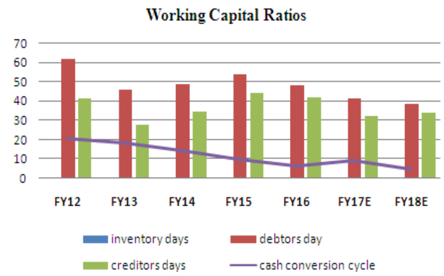
The various acquisitions undertaken by Talwalkars in FY16 will enable it to strengthen its wellness and fitness offerings. The acquisition of 49.5% stake in the PWG will enable the company to penetrate into the rapidly developing Sri Lankan economy. By transforming itself into a wellness company, it has made drastic changes to its products and services.



Source: Talwalkars, CD Equisearch



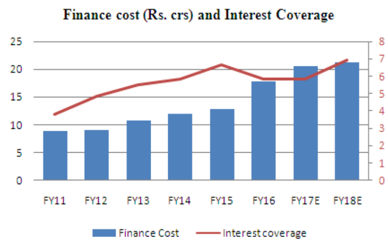
Source: Talwalkars, CD Equisearch



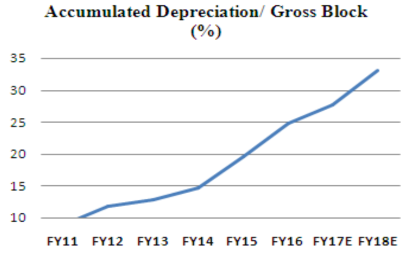
Source: Talwalkars, CD Equisearch

The increase in interest cost by almost 39% y-o-y last fiscal was mainly on account of increase in long term borrowings. The company has decided to keep significant cash balance for future expansion and potential acquisition.

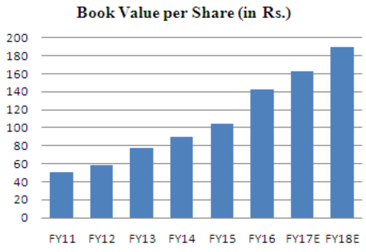
The company plans to reach 250 centers in a period of 24-36 months from the 177 gyms now by expanding through a combination of Talwalkars and PWG gyms both in India and Sri Lanka. Zorba will continue to expand in such a way that it will be available in the top-10 cities of the Talwalkars network by first half of the next calendar year. It has already aggressively initiated marketing activities for the pre-August scheme and the initial figures indicate an encouraging response to the scheme.



Source: Talwalkars, CD Equisearch



Source: Talwalkars, CD Equisearch



Source: Talwalkars, CD Equisearch

Given the leadership status of Talwalkars, it expects the number of members to increase by 7-8% in the upcoming quarters together with an increase in the average realization per member. Going forward the value added services are projected to contribute more to the total revenues. The contribution from gyms is expected to come down to 75% (currently it contributes almost 77%) whereas the remainder will be contributed by the value added services. The new gyms, both ownership and franchisees, will further strengthen the revenue which is expected to cross the 300 cr ($44.7 mn) mark in FY17 itself, with a growth of 20.3%. As was the case in FY16, the treasury income will aid in the margins for the next couple of years as well.

A capex of 85-90 crs ($12.7 m- $13.4 m) is planned for which will include the renovation of gyms – Rs. 15-18 crs ($2.2 m-$2.7 m) - and setting up of 20-25 new ownership gyms. This does not include the 10 HiFi gyms which the company is planning under the franchisee model.

The stock currently trades at 12.1x FY17e EPS of Rs 22.27 and 9.5x FY18e EPS of Rs 28.20. The intention to forge a joint venture with David Lloyd Leisure (Europe's leading premium sports, health and leisure group) for the development of 7-10 clubs in India along with demerger - one focusing on gyms and the other focusing on properties and value added services- is symptomatic of renewed business focus. Transformation into a wellness company (better services and infrastructure) will further make its offerings more eclectic. Growing disposable income and awareness regarding fitness augurs well for the business expansion. Average earnings growth of 21.5% over the next two years is doubtless worthy of notice. We retain 'buy' rating on the stock with a revised target of Rs. 338 (previous target Rs 319) implying a 12x FY18e EPS over a period of 9-12 months. (PEG ratio: 0.6). For more information refer to our October report.

Risks

Economic risk

An economic downturn would affect reduce spending on fitness on an individual level and thus impact company's profitability. Talwalkars offers a gamut of fitness services along with various value-added offerings to its customers. This diversity in customer base should cushion the Company in case of a slowdown in the economy.

Competition risk

Competition is a part of any business, and the potential of the fitness industry has attracted many players. However, with the market still remaining under-penetrated, the scope for growth is enormous, as the number of people focusing on fitness and health are rising steadily. The Company offers wide ranging services for different classes of people- Hi-fi fitness centers offer affordable fitness services while the premium fitness centers cater to the top-end of the market and the Talwalkars fitness centers address the large mid-end of the market. These initiatives adequately protect the Company from fledgling unorganized players.

Personnel risk

The lack of skilled instructors could weaken the quality of services offered at the fitness centers. The Company has a dedicated team to provide periodic training (online and onsite) to each fitness centre across its centers in South Asia. This facility has made training an ongoing feature in a sector where organized training is virtually non-existent.

*All $ values expressed in the write-up are translated at current exchange rates.

Financials

Quarterly results- consolidated

Figures in crores

	Q1FY17	Q1FY16	% chg.	FY16	FY15	% chg.
Income From Operations	**50.24**	**44.89**	**11.9**	**251.37**	**225.66**	**11.4**
Other Income	0.73	0.98	-25.5	6.76	0.85	697.6
Total Income	**50.97**	**45.87**	**11.1**	**258.13**	**226.50**	**14.0**
Total Expenditure	25.10	23.49	6.8	107.86	101.12	6.7
EBITDA (other income included)	**25.87**	**22.38**	**15.6**	**150.27**	**125.38**	**19.9**
Interest	3.77	3.16	19.6	17.74	12.78	38.9
Depreciation	13.61	13.14	3.5	47.00	39.73	18.3
PBT	**8.49**	**6.08**	**39.6**	**85.52**	**72.87**	**17.4**
Tax	2.79	1.10	152.5	30.16	24.50	23.1
PAT	**5.70**	**4.98**	**14.6**	**55.36**	**48.37**	**14.4**
Share of associate profit	0.27	-	-	-	-	-
Minority Interest	0.24	0.21	17.5	0.35	2.30	-85.0
PAT after MI	5.73	4.77	20.1	55.02	46.07	19.4
Extraordinary item	-	-	-	-0.02	0.00	-
Adjusted Net Profit	5.73	4.77	20.1	55.04	46.07	19.5
EPS(Rs)	**1.93**	**1.82**	**5.8**	**19.09**	**17.60**	**8.5**

Income Statement- consolidated

Figure in crores

	FY14	FY15	FY16	FY17e	FY18e
Income From Operations	**187.27**	**225.66**	**251.37**	**302.29**	**356.34**
Growth (%)	24.1	20.5	11.4	20.3	17.9
Other Income	1.08	0.85	6.76	6.79	8.88
Total Income	**188.35**	**226.50**	**258.13**	**309.08**	**365.22**
Total Expenditure	94.59	101.12	107.86	133.01	153.23
EBITDA (other income included)	**93.76**	**125.38**	**150.27**	**176.07**	**212.00**
Interest	11.96	12.78	17.74	20.60	21.23
Depreciation	24.18	39.73	47.00	56.02	64.30
PBT	**57.63**	**72.87**	**85.52**	**99.45**	**126.47**
Tax	17.84	24.50	30.16	34.81	44.26
PAT	**39.79**	**48.37**	**55.36**	**64.64**	**82.21**
Share of associate profit	-	-	-	1.98	2.08
Minority Interest	3.19	2.30	0.35	0.48	0.53
PAT after MI	36.60	46.07	55.02	66.15	83.76
Extraordinary item	-0.02	0.00	-0.02	-	-
Adjusted Net Profit	**36.61**	**46.07**	**55.04**	**66.15**	**83.76**
EPS (Rs)	13.99	17.60	19.09	22.27	28.20

Consolidated Balance Sheet

Figure in crores

	FY14	FY15	FY16	FY17e	FY18e
Sources of Funds					
Share Capital	26.18	26.18	29.70	29.70	29.70
Reserves	214.31	250.66	397.29	458.07	536.47
Total Shareholders' Funds	**240.49**	**276.84**	**426.99**	**487.78**	**566.17**
Minority Interest	11.25	13.56	13.90	14.38	14.91
Long Term Debt	137.32	277.86	307.30	325.00	325.00
Total Liabilities	**389.06**	**568.25**	**748.20**	**827.16**	**906.08**
Application of Funds					
Gross Block	474.08	549.97	638.32	773.38	845.38
Less: Accumulated Depreciation	68.89	106.95	156.83	212.84	277.14
Net Block	**405.19**	**443.03**	**481.49**	**560.53**	**568.24**
Capital Work in Progress	45.33	78.25	83.06	35.00	28.00
Investments	8.80	5.07	9.88	11.86	13.94
Current Assets, Loans & Advances					
Inventory	0.06	0.04	0.04	0.04	0.04
Trade receivables	32.05	34.10	31.68	36.27	39.20
Cash and Bank	6.00	46.56	140.76	187.39	264.63
Short term loans (inc. other current assets)	3.92	29.23	50.83	55.92	61.51
Total CA	**42.03**	**109.92**	**223.31**	**279.62**	**365.37**
Current Liabilities	81.98	55.65	88.34	93.54	97.43
Provisions-Short term	17.70	15.99	16.55	17.03	18.54
Total Current Liabilities	**99.69**	**71.64**	**104.89**	**110.58**	**115.96**
Net Current Assets	**-57.66**	**38.28**	**118.42**	**169.05**	**249.41**
Net Deferred Tax Asset	-23.75	-25.35	-27.49	-30.24	-33.27
Net long term assets (net of liabilities)	11.15	28.97	82.85	80.96	79.76
Total Assets	**389.06**	**568.25**	**748.20**	**827.16**	**906.08**

Key Financial Ratios

	FY14	FY15	FY16	FY17e	FY18e
Growth Ratios (%)					
Revenue	24.1	20.5	11.4	20.3	17.9
EBITDA	27.0	33.7	19.9	17.1	20.4
Net Profit	21.9	25.8	19.5	20.2	26.6
EPS	14.6	25.8	8.5	16.6	26.6
Margins (%)					
Operating Profit Margin	49.5	55.2	57.1	56.0	57.0
Gross profit Margin	43.7	49.9	52.7	51.4	53.5
Net Profit Margin	21.3	21.4	22.0	21.4	23.1
Return (%)					
ROCE	11.6	10.9	9.6	9.3	10.4
RONW	16.6	18.1	15.8	14.6	16.0
Valuations					
Market Cap/ Sales	2.3	4.3	2.2	2.6	2.2
EV/EBITDA	6.6	9.9	5.2	5.8	4.8
P/E	11.5	21.1	9.9	12.1	9.5
P/BV	1.8	3.6	1.3	1.6	1.4
Other Ratios					
Interest Coverage	5.8	6.7	5.8	5.8	7.0
Debt Equity	0.8	1.1	0.9	0.8	0.7
Net Debt-Equity Ratio	0.8	1.0	0.5	0.4	0.2
Current Ratio	0.4	1.5	2.1	2.5	3.2
Turnover Ratios					
Fixed Asset Turnover	0.5	0.5	0.5	0.6	0.6
Total Asset Turnover	0.5	0.5	0.4	0.4	0.4
Inventory Turnover	867.5	1935.4	2692.5	3428.0	3928.9
Debtors Turnover	7.5	6.8	7.6	8.9	9.4
Creditor Turnover	10.6	8.3	8.7	11.4	10.7
WC Ratios					
Inventory Days	0.4	0.2	0.1	0.1	0.1
Debtor Days	48.5	53.5	47.8	41.0	38.7
Creditor Days	34.5	44.1	41.7	32.0	34.1
Cash Conversion Cycle	14.5	9.6	6.2	9.1	4.7

Cumulative Financial Data

Figures in crores

	FY11-12	FY13-14	FY15-16	FY17-18
No. of gyms opened	52	34	27	35
Income from operations	212	338	477	659
Operating profit	95	165	268	372
EBIT	78	129	189	268
PBT	60	106	158	226
PAT after MI	38	67	101	150
Dividends	6	9	11	11
OPM (%)	44.6	48.9	56.2	56.5
NPM (%)	19.7	21.4	21.8	22.3
Interest coverage	4.3	5.7	6.2	6.4
ROE (%)	-	17.7	15.3	15.2
ROCE (%)	-	11.9	9.9	9.9
Debt Equity	1.0	0.8	0.9	0.7
Fixed asset turnover	-	0.5	0.5	0.6
Debtors turnover	-	6.5	7.5	9.3
Inventory turnover	-	2743.6	2056.7	3688.6
Creditors turnover	-	12.6	10.5	11.3
Debtor days	-	56.3	48.8	39.3
Inventory days	-	0.1	0.2	0.1
Creditor days	-	29.0	34.7	32.3
Cash conversion	-	27.4	14.2	7.0
Dividend payout ratio (%)	16.6	13.7	10.6	7.4

FY11-12 implies two years ending fiscal 12

Talwalkars is a perfect example of a company riding the growth trajectory. Cumulative profit is estimated to grow by almost 50% to Rs. 150 crs ($22.3 mn) in FY17-18 period from Rs. 101 crs ($15.1 mn) in the FY 15-16 period. The cash conversion cycle is expected to be the lowest in the analyzed period on account of fall in the debtor days (39.3 days in FY17-18 from 48.8 days in FY15-16). The gradual decrease in debt-equity ratio will help the company in achieving its target debt-equity ratio of 0.5 in the next couple of years.

Expanding presence through acquisitions, subsidiaries and franchisees will not only aid in the revenue growth- 3.1x increase in FY17-18 from FY11-12- but also boost the profitability. The huge capex undertaken by the company in FY15-16- Rs. 236 crs ($35.2 mn) helped in expansion of its network. Cost efficiencies and benefits of operating leverage would boost the operating margins in the ensuing years.

Financial Summary – US dollar denominated

million $	FY14	FY15	FY16	FY17e	FY18e
Share capital	4.4	4.2	4.5	4.4	4.4
Shareholders' funds	39.4	43.7	63.9	72.2	83.9
Total debt	33.3	49.4	54.6	57.0	57.4
Net fixed assets (incl. CWIP)	74.3	82.7	84.6	88.2	88.3
Investments	1.5	0.8	1.5	1.8	2.1
Net Current assets	-9.6	6.1	17.9	25.2	37.2
Total Assets	64.7	90.8	112.8	123.2	135.0
Revenues	31.0	36.9	38.4	45.0	53.1
EBITDA	15.5	20.5	23.0	26.2	31.6
EBDT	13.5	18.4	20.2	23.2	28.4
PBT	9.5	11.9	13.1	14.8	18.8
PAT	6.1	7.5	8.4	9.9	12.5
EPS($)	0.23	0.29	0.29	0.33	0.42
Book value ($)	1.50	1.67	2.15	2.43	2.82

income statement figures translated at average rates; balance sheet and cash flow at year end rates; projections at current rates
*All $ values adjusted for extraordinary items.

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