Talwalkars Better Value Fitness Limited Revised

November 05, 2018

Summary of Rated Instrument:

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-convertible debenture Programme	80.0	80.0	[ICRA]AA-(S), outlook revised to Negative from Stable
Long-term loans	85.09	85.09	[ICRA]AA-(S), outlook revised to Negative from Stable
Proposed non-convertible debenture Programme	25.0	25.0	[ICRA]AA-(S), outlook revised to Negative from Stable
Total	**190.09**	**190.09**	

Material Event

Talwalkars Better Value Fitness Limited has announced its quarterly results on October 30, 2018. The company reported an operating income of Rs.30.2 crore (excluding other income of Rs 6.3 crore) and Profit after tax (PAT) of Rs. 7.0 crore during H1FY2019 against an operating income of Rs. 25.3 crore (excluding other income of Rs. 1.3 crore) and a PAT of Rs. 3.3 crore in H1FY2018. The company reported a total debt of Rs. 215.8 crore with cash and liquid investments of Rs. 68.3 crore as on September 30, 2018. ICRA has also taken updates from the management on progress of the company's deleveraging plan.

Impact of the Material Event

ICRA has revised the outlook on long-term rating of [ICRA]AA-(S) (pronounced ICRA double A minus S)[1] of the Rs. 80.0-crore[2] non-convertible debenture (NCD) programme, the Rs. 25.0-crore proposed NCD programme and the Rs. 85.09-crore bank term loans of Talwalkars Better Value Fitness Limited (TBVFL) from Stable to Negative. The letter "S" in parenthesis suffixed to the rating symbol denotes that the rating is based on a guarantee (or any other such form of support) without a well-defined payment mechanism. An (S) rating does not represent ICRA's opinion on the general credit quality of the entity concerned.

Rationale and outlook

ICRA's rating reflects corporate guarantee extended by TBVFL and Talwalkars Lifestyles Limited (TLL) to each other's credit facilities, as confirmed by the TBVFL management. The companies are together referred to as the Talwalkars Group or the Group. The company's gym business is under TLL and TBVFL has all other lifestyle businesses (smaller in size compared to the gym business).

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[1] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

[2] *100 lakh = 1 crore = 10 million*

The revision in outlook to Negative from Stable reflects slower-than-expected progress in the deleveraging/ asset monetisation plan of the company. The asset monetisation under its lifestyle business remains core to significantly deleverage the Group's overall debt levels and improve its debt coverage metrics. ICRA will continue to monitor the developments related to asset monetisation and any further delay will be a rating trigger.

Apart from asset monetisation, ICRA expects the Group to improve asset turnover from current levels by reducing capital intensity for new gyms and by scaling up the lifestyle business which will be crucial to improve the combined return ratios.

The rating remains constrained by the capital intensity of the business, with significant capital expenditure incurred towards the expansion of its gym, lifestyle and club businesses. Further, it requires recurring capital expenditure to maintain/upgrade its existing infrastructure. This is reflected in low operating income/gross block of ~44% and high estimated total debt/OPBDITA of 3.1x in FY2018 for the Group (consolidated financials of gym and lifestyle business).

Additionally, the Group has inorganic expansion plans; the funding mix and returns on the same will be a key rating sensitivity. ICRA notes that the company's first club project in Pune (Maharashtra) is expected to commence by the end of CY2018. The performance of the same in terms of member additions will be one of the key monitorables. The rating also factors in the highly fragmented nature of the gym and the fitness industry as well as the susceptibility of revenues and profits to the seasonality of the industry.

The rating favourably factors in the long operating track record of the Group in the Indian fitness industry, its strong pan-India presence with outlets across India as well as its market leadership position within the organised gym industry. The rating also favourably factors in the healthy operating margins of the Group supported by high retention rate due to the Talwalkars brand loyalty and competitive pricing.

Key rating drivers

Credit strengths

Financial support from stronger Group entity –ICRA's rating incorporates corporate guarantee extended by the two de-merged companies—TBVFL and TLL—to each other's credit facilities, as confirmed by the TBVFL management. On a standalone basis, TBVFL's credit profile is significantly weaker compared to TLL with high Total Debt/OPBDIT of 5.0x times as on March 31, 2018. Thus, ICRA expects timely financial support from the stronger entity, TLL, to aid the credit profile of TBVFL.

Long operating track record of the Group in the Indian fitness industry –Set up in 2003, the Group has an established operating track record in the fitness industry with an experienced promoter team.

Strong pan India presence of outlets– Post demerger, the group operates 251 fitness centres (as on March 31, 2018) across India and Sri Lanka under TLL, while it offers various lifestyle activities such as Nuform, aerobics, yoga, spa, massage, zumba programmes and diet and weight loss programmes like Reduce under TBVFL. In terms of region-wise coverage, the Group enjoys a major presence across northern, western and southern India, which together account for 95% of the total fitness centres in India.

Market leadership position within the organised segment–The company enjoys market leadership in the organised domestic fitness segment with a market share (in terms of number of centres) of ~48%, which, as per the company's estimates, represent ~10% of the total estimated centres.

Consistently high operating margins of the company- The operating margins of TLL (gym business) remained healthy at ~56%, while operating margins of TBVFL (lifestyle business) remained at ~67% in FY2018. The high operating margins in the gym business are supported by a high retention-rate due to the Talwalkars brand loyalty and competitive pricing as well as value-added services in the lifestyle business.

Credit challenges

High capital intensity in the business and ability to reduce its debt levels–The gym and lifestyle business are capital intensive in nature with significant investment required to scale up the revenues and there is a recurring capital expenditure to maintain and upgrade the existing facilities. This is reflected in low operating income/gross block of 44% in FY2018 for the Group (consolidated financials of gym and lifestyle business). ICRA expects the Group to significantly reduce overall debt levels and improve its debt coverage metrics by monetising properties (valued at ~Rs. 130 crore) under its lifestyle business; any further delay in asset monetisation will be a rating trigger. Further, the ability of the Group to improve its asset turnover by reducing capital intensity for new gyms and by scaling up its higher value-added lifestyle business will be crucial to improve overall credit profile.

Performance of the club business will be a key rating monitorable–TBVFL has made significant investments in setting up its first club at Pune (Maharashtra) in collaboration with David Lloyd Leisure Limited. The club is expected to become operational by the end of CY2018. Hence, performance of the same in terms of member additions will be one of the key rating monitorables.

Highly fragmented nature of the gym and fitness industry; susceptibility of revenues and profits to seasonality of the industry –The gym and fitness industry is highly fragmented with the unorganised market comprising a majority of the share, thus leading to intense competition. Further, the business remains seasonal with the second and fourth quarters typically being the peak revenue-generating quarters for the company.

The previous detailed rating rationale is available on the following link: Click here

Corrigendum

Previously published document dated November 5, 2018 has been corrected with revisions as detailed below:

- Revision on Page 1 – the first paragraph under the Rationale and outlook section has been rephrased
- Revision on Page 2 – the paragraph under Credit Strength- Financial support from stronger Group entity, has been rephrased

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