



Nykaa - 'Synonymous to beauty', spreading wings wide

Let the hope and hype spring eternal for digital companies at least as long as interest rates remain low and capital is available in abundance or essentially free!!!

NYKAA

FSN E-Commerce Ventures

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SELL

The flywheel juggernaut

Leading Beauty and Fashion E-tailer in a large addressable market

Nykaa, India's leading super-vertical e-commerce participant, is one of the most dominant player in Beauty and Personal Care (BPC) segment. India BPC market is at an inflexion point with rising affordability, higher spending intensity and willingness of consumer to pay premium for quality and brand. There is a paradigm shift in consumer preference from 'looking good' to 'feeling good', and the industry is innovating to address the evolving consumer awareness and aspirations. Having built its core around BPC, Nykaa is expanding into fashion, men's grooming and B2B.

Over the trailing 5-7 years many structural positives aligned for a conducive runway of growth viz. smartphone penetration, affordable data, rapid digital adoption, evolution of logistics & payment eco-system. Leveraging these tailwinds, Nykaa created a formidable position in the online BPC space. BPC market of ~Rs 1,267bn/USD 17bn in CY19 (13% CAGR over CY16-19) offers a huge growth runway. Online BPC at Rs 91bn/ USD 1.2bn (71% CAGR) is a modest 8% (vs. 25-30% globally) of the BPC market. Online/Overall fashion at USD 8/78bn is even larger opportunity.

Strong business proposition similar to Dmart

We see Nykaa's business mindset similar to Dmart viz. both with inventory led model, in a large addressable market with high growth opportunity, strong recall and focus on profitability. Dmart attracts consumers through its EDLC-EDLP (Everyday low costs, Everyday low price) strategy whereas Nykaa achieves the same through its product curation, assortments and authenticity in an industry plagued with counterfeit and content driven engagement and conversions. Dmart has aced the brick-and-mortar format but is yet to see meaningful traction on digital. Nykaa is a leader in the futuristic digital space and supporting it with its omni-channel strategy.

Rich valuations leave limited room to err. Initiate with 'Sell'

The strengths of Nykaa highlight themselves in the unique combination of growth and profitability – a rarity in the internet space. Led by its strong business position, we expect it to trade at scarcity premium. But current valuations at 19.4/13.7x FY23/24E EV/Sales seem too rich for our comfort, howsoever long we may stretch the timeline. In the current valuations, implied expectations leave limited room to err on execution and growth trajectory of the space. The risks of increased competition from some of the large players remains key in our view. Stock supply is another risk. Initiate Sell with TP of Rs 1,600 @ 10x FY24 EV/Sales.

FINANCIALS (Rs Mn)

| Particulars | FY20A | FY21A | FY22E | FY23E | FY24E |
|-------------|----------|---------|--------|--------|--------|
| Revenue | 17,675 | 24,409 | 38,197 | 52,991 | 74,732 |
| Growth(%) | 59.0 | 38.1 | 56.5 | 38.7 | 41.0 |
| EBITDA | 811 | 1,614 | 1,993 | 4,543 | 8,333 |
| OPM(%) | 4.6 | 6.6 | 5.2 | 8.6 | 11.2 |
| PAT | (163) | 619 | 814 | 2,789 | 5,696 |
| Growth(%) | (33.4) | (479.1) | 31.4 | 242.6 | 104.3 |
| EPS(Rs.) | (0.3) | 1.3 | 1.7 | 5.9 | 12.1 |
| Growth(%) | (33.4) | (479.1) | 31.4 | 242.6 | 104.3 |
| PER(x) | (6500.9) | 1714.8 | 1304.8 | 380.9 | 186.5 |
| ROANW(%) | (5.9) | 15.3 | 8.4 | 17.6 | 28.4 |
| ROACE(%) | 4.4 | 9.9 | 7.4 | 15.9 | 25.6 |

| | |
|-------------------|----------------|
| CMP | Rs 2,248 |
| Target / Downside | Rs 1,600 / 29% |
| NIFTY | 17,415 |

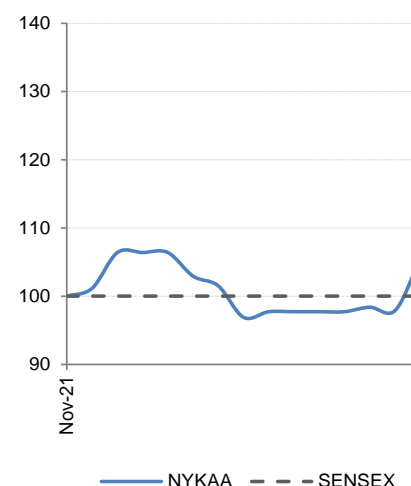
Scrip Details

| | |
|------------------|-----------------|
| Equity / FV | Rs 473mn / Rs 1 |
| Market Cap | Rs 1,062bn |
| | USD 14.3bn |
| 52-week High/Low | Rs 2,410/ 2,000 |
| Avg. Volume (no) | 6,799,500 |
| Bloom Code | NYKAA IN |

Shareholding Pattern

| | Nov'21 |
|--------------|--------|
| Promoters | 52.6 |
| MF/Banks/FIs | 3.3 |
| FII's | 14.8 |
| Public / | 29.3 |

Nykaa Relative to SENSEX



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Masterstroke of addressing the consumer and profitability issue

Nykaa identified the market gap in reference to consumer problems of counterfeit products, lack of education on BPC products, dearth of foreign brands. Nykaa addressed these problems taking ownership of the inventory (contrary to marketplace models for most internet companies) and generating rich online content to educate the customer base – a key customer acquisition, retention and conversion factor. These offered consumers a lot of confidence in the product authenticity and quality. Most online consumer businesses have profitability plans post certain scale. Nykaa always believed in the troika of assortments, convenience followed by pricing. This led to creation of favorable and scalable unit economics.

Virtuous cycle – deep relationship with consumers and brands

Nykaa's BPC offering comprises of an extensive portfolio of ~2lac units across categories. The breadth of portfolio coupled with understanding the needs and preferences of the consumers enables Nykaa to personalize selection across a diverse customer base. Nykaa has not only redefined the art of e-retailing BPC in India, but also have been instrumental in fostering the growth of a previously relatively nascent ecosystem. Many BPC brands look at Nykaa as a trusted partner for brand curation, category creation and consumer base expansion. This moat also leads Nykaa to drive a healthy and meaningful advertisement revenue from brands on its platform/stores. Leveraging the brand strength, consumer loyalty and backend prowess, Nykaa is seeding a lot of optionality in its business like Nykaa Fashion, Nykaa Men's grooming, 'SuperStore' an eB2B platform.

Operating and financial overview

Nykaa's strong assortment, relationship with brands and consequent consumer pull enabled it to register a healthy GMV growth of 57% over FY19-21 and revenue/GP/EBITDA growth of 48/45/181%. These is despite Covid led disruptions in FY21. As the situation normalizes and led by new verticals, store expansions and aggressive A&P for new customers acquisition, we expect Nykaa to deliver a healthy GMV growth of ~53% CAGR over FY21-24. Within categories, we estimate BPC to grow at ~42% CAGR and Fashion at 92% CAGR. Revenue/GP/EBITDA/APAT to grow at 47/52/77/115% CAGR led by economies of scale.

Key risks

Intense competition and discounting

Large opportunity size, lower barriers to entry, easy availability of capital have been the talk all over the street. Recent fund-raise by competitors like Purplle, Myglam have attracted players across categories in the online space and growth in most cases is at the cost of profitability. With valuation parameters linked to number of MAUs, transacting customers, most companies have been resorting to aggressive marketing and discounting. In India, majority of households tend to be value-conscious buyers. A few prioritize shopping experience and prefer purchasing from a wider product assortment in one place and lower delivery time.

Retaining Customers and Maintaining Average Order Values

Nykaa must generate a certain average order value and retain existing customers to maintain its margins and overcome its basic costs. The company has designed its platform in a manner in which customers can discover new trends and products. It has also on-boarded influencers and mainstream celebrities to grow its reach. In order to maintain high-order values, it must also target the right audience. Any shift in its customer demographic can impact it negatively.

Initiate Sell

We like Nykaa for its.....

- Large addressable opportunity size in the BPC and Fashion space
- Nykaa's strong business acumen viz. relationship with consumers and brands and profitability focus
- Leadership and brand recall
- Strong management and superior execution

.....but, dislike the implied expectations and valuations

- Nykaa's rich valuations on high expectations leaves limited room to err. Even our expectations of 10-year revenue/EBITDA/APAT CAGR of 31/45/55% barely justifies the current valuations. Investors' euphoria to lap-up the new-age economies in backdrop of large addressable market opportunities (buzzword) ignoring the risks of competition, change in consumer behaviours, execution slip, regulatory doesn't suit us. Initiate Sell with TP of Rs 1,650 @ 10x EV/Sales.
- Peer internet cos (Nazara, Affle etc) trades at ~8-9x. Dmart trades at 5.4x FY24E. Zomato trades at a rich 14x FY24E EV/Sales. Global established BPC player like L'Oreal, LVMH, Estee Lauder or even Chinese BPC like Proya and Marubi trades at 6-7x.

Exhibit 1: Abridged P&L summary FY21-31E

| Particulars (Rs Mn) | Rs Mn | | | | Chg YoY % | | 10 YR CAGR % | Common Size (%) | | | |
|---------------------|--------------|--------------|--------------|-----------------|---------------|----------------|--------------|-----------------|-------------|-------------|-------------|
| | FY19 | FY20 | FY21 | FY31E | FY20 | FY21 | FY21-31E | FY19 | FY20 | FY21 | FY31E |
| Revenue | 11,114 | 17,675 | 24,409 | 3,43,229 | 59.0 | 38.1 | 30.3 | 100.0 | 100.0 | 100.0 | 100.0 |
| COGS | 6,603 | 10,142 | 14,878 | 1,93,172 | 53.6 | 46.7 | 29.2 | 59.4 | 57.4 | 61.0 | 56.3 |
| GP | 4,511 | 7,533 | 9,531 | 1,50,058 | 67.0 | 26.5 | 31.7 | 40.6 | 42.6 | 39.0 | 43.7 |
| Semi-variable costs | 4,306 | 6,723 | 7,916 | 89,786 | 56.1 | 17.8 | 27.5 | 38.7 | 38.0 | 32.4 | 26.2 |
| EBITDA | 205 | 811 | 1,614 | 60,272 | 295.2 | 99.2 | 43.6 | 1.8 | 4.6 | 6.6 | 17.6 |
| PAT | -245 | -163 | 619 | 44,498 | (33.4) | (479.1) | 53.3 | -2.2 | -0.9 | 2.5 | 13.0 |

Source: Company, DART

Exhibit 2: Reverse valuation snapshot

| Description | |
|-----------------------------------|------------------|
| FY31E PAT (Rs Mn) | 44,498 |
| Target exit multiple (x) | 50 |
| Equity Value FY31E (Rs Mn) | 22,24,902 |
| WACC (%) | 12% |
| Discounted to FY24E | 2.21 |
| Equity Value FY24E (Rs Mn) | 10,06,433 |
| O/s sh (Mn) | 473 |
| TP (Rs/Sh) | 2,129 |

Source: Company, DART

Exhibit 3: Sensitivity to WACC and Terminal growth

| WACC | Terminal Growth % | | |
|------|-------------------|-------|-------|
| | 4% | 5% | 6% |
| 8% | 4,726 | 5,753 | 7,807 |
| 9% | 3,453 | 3,956 | 4,794 |
| 10% | 2,638 | 2,912 | 3,324 |
| 11% | 2,081 | 2,242 | 2,466 |
| 12% | 1,682 | 1,781 | 1,913 |
| 13% | 1,386 | 1,449 | 1,531 |

Source: Company, DART

Historical precedence dull!

Similar to current forecasts for digital companies, sky-high expectations and consequent euphoric valuations in IT sector over 1998-2002 or Real Estate/Infrastructure in 2006-08 ended into ugly outcomes. Telecom as a sunrise sector delivered on growth but returns have been below costs of capital due to unabated competition (invited by initial high-returns) and regulatory night-mare.

Recent listings of new-age companies has been mixed-bag with Zomato, PolicyBazaar and Nykaa doing well whereas PayTM, CarTrade, Fino Payments disappointing. Historically, Nazara, Affle and IndiaMart InterMesh have delivered healthy returns in the internet space.

Exhibit 4: Stock price performance of the Internet Companies

| Company | Mcap (Rs Bn)* | IPO Month | Issue Price (Rs) | CMP (Rs) | Chg (%) |
|--------------|---------------|-----------|------------------|----------|---------|
| Zomato | 1,216 | Jul-21 | 76 | 155 | 104 |
| PayTM | 1,136 | Nov-21 | 2,150 | 1,753 | (18) |
| Nykaa | 1,062 | Nov-21 | 1,125 | 2,246 | 100 |
| IRCTC | 690 | Oct-19 | 64 | 863 | 1,248 |
| PolicyBazaar | 585 | Nov-21 | 980 | 1,304 | 33 |
| IndiaMart | 223 | Jun-19 | 973 | 7,309 | 651 |
| Affle | 154 | Jul-19 | 149 | 1,153 | 674 |
| Nazara | 69 | Mar-21 | 1,101 | 2,262 | 105 |
| CarTrade | 45 | Aug-21 | 1,618 | 991 | (39) |
| Fino Bank | 37 | Nov-21 | 577 | 473 | (18) |

Source: DART, Company; Sorted on Mcap

Investment Thesis

- Nykaa is India's leading super-vertical e-commerce player in Beauty and Personal Care (BPC) space with large addressable market opportunities
- Nykaa is expanding further into Fashion a significantly large market, Men's grooming and B2B segments
- It offers a unique combination of growth and profitability – a rarity in the internet space

Catalyst

- Increase in unique transacting consumers and/or higher AOV and/or lower returns/discounts

Company Background

Nykaa was incorporated in 2012 to engage in the trading of beauty and wellness products through its online portal 'nykaa.com'. Since inception, capital and resources have been invested in designing a differentiated journey of brand discovery and building a digitally native consumer technology platform, by delivering a content-led, lifestyle retail experience for the consumers.

Nykaa is promoted by Falguni Nayar (Founder, Executive Chairperson & MD and CEO), a post-graduate diploma in management from the Indian Institute of Management, Ahmedabad and has over 26 years of experience in e-commerce, investment banking and broking. Both her kids Adwaita, ED & CEO, Nykaa Fashion and Anchit, ED & CEO, Nykaa E-Retail are active in the business.

Risk

- E-commerce remains a highly competitive industry with high cash burn on account of discounting and marketing towards customer acquisition and retention. Increase in competition with easy availability of capital is key risks.
- Growth expectations remain high for Nykaa. A moderation in growth on account of economic slowdown, change in consumer behavior or competition is another risks.

Event

- Inorganic expansion in core BPC or adjacent categories

Key Assumptions

| Particulars | FY21 | FY22E | FY23E | FY24E |
|------------------------|--------------|--------------|--------------|--------------|
| Consumers (Mn) | 6.2 | 8.5 | 10.9 | 13.6 |
| BPC | 5.6 | 7.3 | 9.1 | 10.9 |
| Fashion | 0.6 | 1.2 | 1.8 | 2.7 |
| Orders (Mn) | 19.5 | 33.0 | 43.2 | 57.0 |
| BPC | 17.1 | 27.5 | 34.4 | 43.0 |
| Fashion | 2.4 | 5.5 | 8.8 | 14.1 |
| Orders/Cust. pa | 3.1 | 3.9 | 4.0 | 4.2 |
| BPC | 3.1 | 3.8 | 3.8 | 3.9 |
| Fashion | 4.0 | 4.6 | 4.9 | 5.2 |
| AOV (Rs) | 2,075 | 2,102 | 2,298 | 2,525 |
| BPC | 1,963 | 1,874 | 2,053 | 2,258 |
| Fashion | 2,739 | 3,244 | 3,256 | 3,338 |
| GMV (Rs Bn) | 40.5 | 69.4 | 99.2 | 144.0 |
| BPC | 33.8 | 51.5 | 70.6 | 97.0 |
| Fashion | 6.7 | 17.8 | 28.7 | 47.0 |
| Chg YoY (%) | | | | |
| Consumers (Mn) | 14.8 | 36.8 | 28.5 | 25.0 |
| BPC | 5.7 | 30.0 | 25.0 | 20.0 |
| Fashion | 500.0 | 100.0 | 50.0 | 50.0 |
| Orders (Mn) | 7.7 | 69.2 | 30.8 | 32.1 |
| BPC | 0.6 | 60.8 | 25.0 | 25.0 |
| Fashion | 118.2 | 129.2 | 60.0 | 60.0 |
| Orders/Cust. pa | -6.2 | 23.7 | 1.8 | 5.7 |
| BPC | -4.8 | 23.7 | -0.0 | 4.2 |
| Fashion | -63.6 | 14.6 | 6.7 | 6.7 |
| AOV (Rs) | 39.9 | 1.3 | 9.3 | 9.9 |
| BPC | 35.6 | -4.5 | 9.6 | 10.0 |
| Fashion | 70.8 | 18.4 | 0.4 | 2.5 |
| GMV (Rs Mn) | 50.7 | 71.4 | 43.1 | 45.2 |
| BPC | 35.3 | 52.4 | 37.0 | 37.5 |
| Fashion | 256.3 | 168.0 | 60.6 | 64.0 |

Company Overview

| Particulars | Details |
|---------------------------|---|
| Company Background | Nykaa was incorporated in 2012 to engage in the trading of beauty and wellness products through its online portal 'nykaa.com'. The brand name Nykaa is derived from the Sanskrit word nayaka, meaning ' one in the spotlight '. Since inception, capital and resources have been invested in designing a differentiated journey of brand discovery and building a digitally native consumer technology platform, by delivering a content-led, lifestyle retail experience for the consumers. |
| Product Portfolio | The company has a diverse portfolio of beauty, personal care and fashion products, including owned brand products manufactured. As of August 31, 2021, it offered ~2.6lac SKUs from 2,644 national and international brands in BPC and 2.8mn SKUs from 1,434 brands in fashion vertical. |
| In-house Brands | Nykaa owns a portfolio of ~15 brands Nykaa House of Brands in BPC – Nykaa Naturals, Nykaa Cosmetics, Kay Beauty Nykaa Fashion – Nykd by Nykaa, 20 Dresses, RSVP, Mondano, Likha, Pipa Bella, Dot & Key |
| Management | <p>Falguni Nayar (Founder, Executive Chairperson & MD and CEO) is a post-graduate diploma in management from the Indian Institute of Management, Ahmedabad and has over 26 years of experience in e-commerce, investment banking and broking.</p> <p>Nihir Parekh (CEO, NykaaMan business arm of Nykaa E-Retail) is a MBA from INSEAD and has over 11 years' experience in technology and E-commerce sector. Previously employed with Genentech Inc, USA, and GE Healthcare</p> <p>Reena Chabra (CEO - Private labels) holds a Bachelor degree in arts from Punjab University and has over 23 years' experience in cosmetic and e-commerce industry. Previous employment experiences includes Colorbar Cosmetics Private Limited, Hindustan Unilever Limited, Marico Industries Limited</p> <p>The lists above is only illustrative and not an exhaustive one</p> |

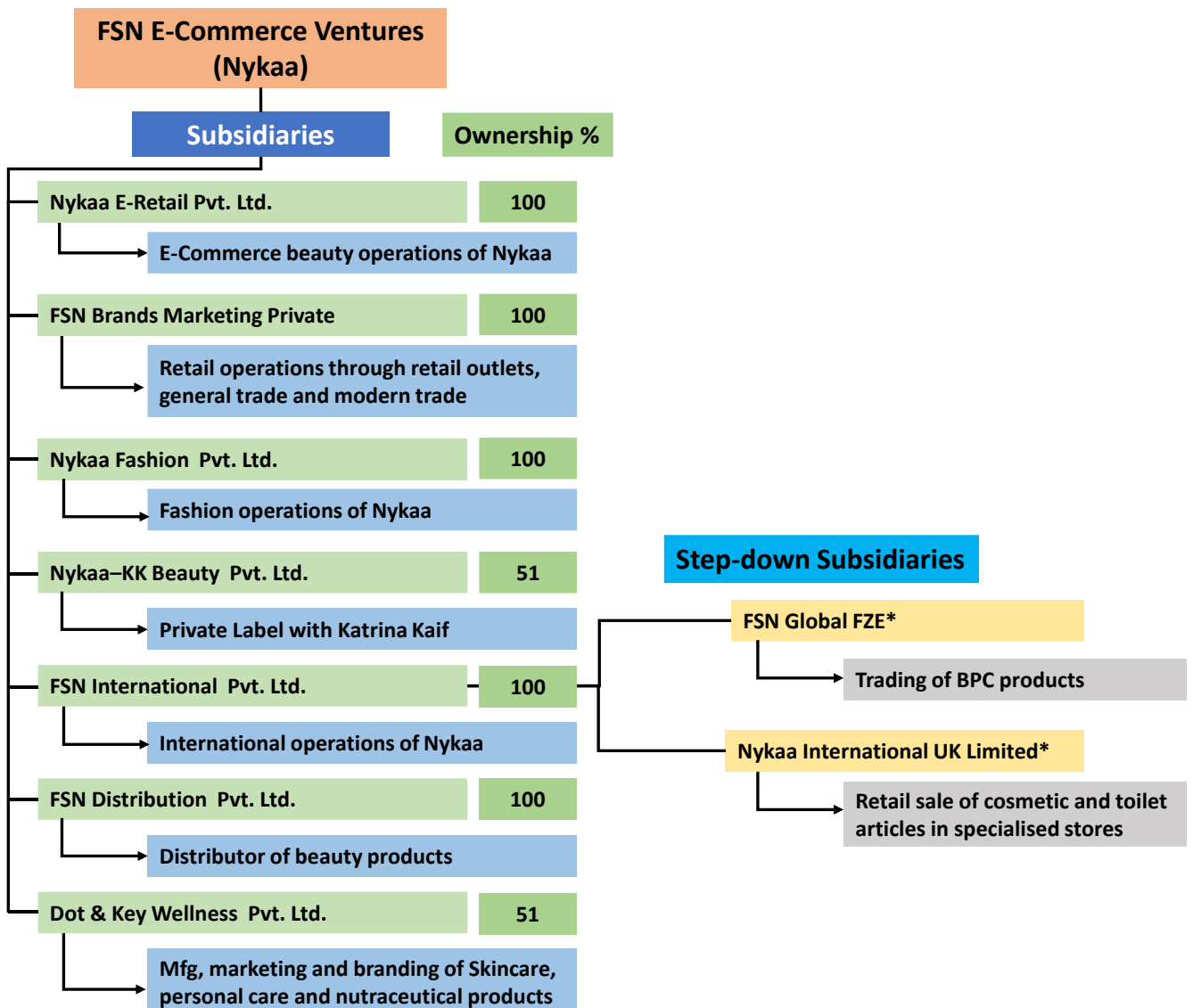
Source: Company, DART

Major Events and Milestones



Source: Company, DART

Corporate Structure



Source: Company, DART

Nykaa - ‘Synonymous to beauty’, spreading wings

FSN E-Commerce Ventures (Nykaa) was incorporated in 2012 and has, since, seen rapid growth over the years, to become the largest speciality BPC platform in India, as per RedSeer. Among the ecommerce players in India, Nykaa stands out for having achieved strong profitability earlier in its life cycle while continuing to grow exponentially. This is in sharp contrast to the other internet-based business models which have been burning cash to buy growth and thereby sacrificing profitability.

Nykaa is India’s leading super-vertical e-commerce player in Beauty and Personal Care (BPC) with expanding categories. Nykaa as a specialised beauty e-tailer is a perfect combination of growth (44% BPC GMV CAGR over FY19-21 despite Covid) and profitability (6.6% EBITDA margin in FY21) driven by its superior product assortment, content creation and discovery engine. It is now replicating the same model in large addressable market opportunity of Fashion, Men’s grooming as well as B2B segment.

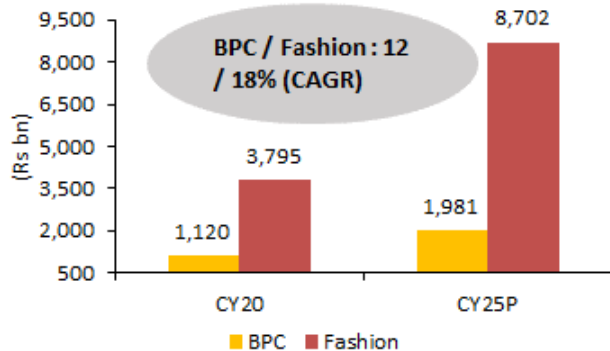
Currently, Nykaa has two major divisions – beauty & personal care (84% of GMV in FY21) and fashion (16% of GMV in FY21, ~27% in H1FY22).

Nykaa has a total addressable market across BPC and fashion of Rs 10,683bn (US \$152bn)

Nykaa’s Target Addressable Market and Competition

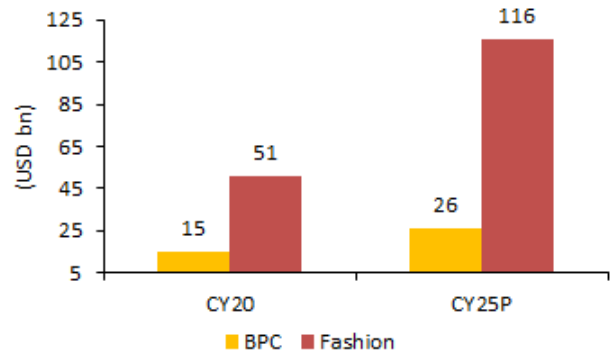
Nykaa has a large BPC market opportunity of Rs 1,120bn (US\$15 bn) growing at 12% p.a. to Rs 1,981bn (US\$28 billion) in 2025. Nykaa’s fashion opportunity of Rs 3,794bn (US\$54 bn) is expected to grow at 18% p.a. to Rs 8,702bn (US\$124 bn) in 2025. We discuss in detail in Industry Overview section on each of the business segments.

Exhibit 5: India BPC and Fashion Mkt Size



Source: Company, DART

Exhibit 6: India BPC and Fashion Mkt Size



Source: Company, DART

Size of the online BPC market

Online BPC penetration is a modest 8% of the overall BPC market

The online BPC market is currently at a modest 8% (or ~\$1.2bn) of the overall BPC market and growing impressively. Vertical e-commerce players like Nykaa and Purplle have been able to provide better assortment by offerings more international brands especially in the specialized category and are thus able to grow at a faster pace than the other players.

There is a paradigm shift in consumer preference from ‘looking good’ to ‘feeling good’, and the industry is innovating to address the evolving consumer awareness and aspirations.

Exhibit 7: Size of BPC and Online market in India and Nykaa's market share

| Particulars | FY21 | FY25E | CAGR (%) |
|--|-------|-------|----------|
| Internet users in India (mn) | 650 | 800 | 5 |
| Online Shoppers (mn) | 130 | 240 | 17 |
| Penetration of online BPC category (%) | 20 | 30 | 11 |
| BPC online shoppers | 26 | 72 | 29 |
| Avg spend per shoppers (Rs) | 3,200 | 4,000 | 6 |
| Online BPC Opportunity (Rs Bn) | 83 | 288 | 36 |
| Nykaa's GMV (Rs Bn) | 34 | 125 | 38 |
| Nykaa's Market Share (%) | 41.0 | 43.4 | |

Source: Media Articles, DART

HUL, in its annual investor presentation, highlighted the growing salience of digital with rise in penetration and time-spent. As per HUL, there are 25-30mn beauty shoppers online. HUL is aggressively adopting digital-first marketing approach.

HUL has set up the Premium Beauty Business Unit within Beauty & Personal Care organization to strengthen its play in beauty segment. The unit will work closely with their e-Commerce sales team and lead entry into niche premium formats like serums, sheet masks, hair masks etc. through existing and new brands. Technology-driven commerce will continue to grow disproportionately.

Estee Lauder Global recently in its Jun'21 earnings call highlighted

Online sales rose strong double-digits, reflecting the Company's increased focus on reaching consumers digitally, including the launches of new brand sites in India and several other countries as well as the launches on additional pure play retailers

HUL and Estee Lauder are amongst the top five suppliers to Nykaa

Women – Key target segment of Nykaa

The Indian market is unique in its own way – the breadth, the range of buying budget, headroom to increase penetration are all structural drivers that we believe will play out over this decade. From the perspective of size estimation, we reckon ~120mn Urban and ~200mn female customers in the age-group 15-44 years are the key target segment for Nykaa's BPC segment. This is against ~21mn unique visitors and ~7mn unique transacting consumers. We remain cognizant of Urban: Rural, family buying as well as income filters which may reduce the overall opportunity size but it would still remain significantly higher. Further, Nykaa's ~65% of the GMV's (gross merchandise value) is from tier II and III cities.

Further, as per recent Google-WPP-Kantar report on "Connected Beauty Consumer Report", gender divide in Beauty is a myth with broadly similar number of products purchased by Men and Women in Haircare, Skincare and Personal Care products. In that case, it significantly further increases the addressable market size for Nykaa.

To specifically address to the Men's categories, Nykaa has separately created a website and app Nykaaman.com. It offers products in categories like shaving, haircare, grooming kits and sports nutrition with exclusive brands. For example - The Shave Doctor, Clinique for Men and Beardo are only available in India with NykaaMan.

Women remains the key target segment for Nykaa.

That said, as per the recent Google-WPP-Kantar study gender divide in beauty is a myth which increases opportunity for Nykaa

Nykaa's robust business model in BPC

Nykaa's unique business model is driven by creating a moat in the BPC segment by focussing on

- Offering a wide product range to the consumers including some exclusive domestic and international brands and high margin retail categories,
- Inventory led sourcing which allows it to have an end-to-end control
- Content driven customer acquisition; original content creation with ~3,055+ influencers and a YouTube channel with 1.5m hours of content and 1.2m subscribers
- Detailed sort and search capabilities
- Higher AOVs given the primarily branded product offerings

Due to these benefits, Nykaa doesn't have to offer high discounts (a majority of it is borne by the brands) which provides healthy gross margins. A relatively high AOV translates to lower fulfilment costs as a % of sales, emphasis on differentiation (rather than discounting) has resulted in strong unit economics.

Nykaa's revenue composition – A healthy mix

- **Revenue from sales of products** – The BPC segment runs on the inventory model. It buys the goods from brands and sells these to consumers. It takes on the cost of working capital and the risk of obsolescence. In some cases, it also follows the SOR (sale or returns) or JIT (just in time inventory) model.
- **Revenue from marketplace** – The fashion division of Nykaa runs largely on the marketplace model. In this model, the company charges a commission from vendors who list and sell products on the Nykaa platform.
- The reason Nykaa has adopted marketplace model for Fashion business is due to the large number of SKUs involved in the fashion segment. Thus, inventory risk can be higher. Also, BPC is very brand centric and within brands it is very product centric. Fashion is very fragmented and products go in and out of style very frequently. Lastly, large premium and luxury brands are also not comfortable in handing over the inventory and prefer to make it available across aggregators.
- **Revenue from marketing support services** – This is the revenue that Nykaa gets for advertising by brands on its platform or for promoting brands in searches.
- **Revenue from delivery charges (trivial)** – This is a very small (negligible) component of Nykaa's revenue mix. However, in our view in the long-run company may look at recovering delivery charges from the customers especially for orders below a certain threshold as it goes more mass-market from upper-end funnel of the target consumers.

As per the management, the unit economics for BPC and Fashion are broadly similar except for difference in accounting

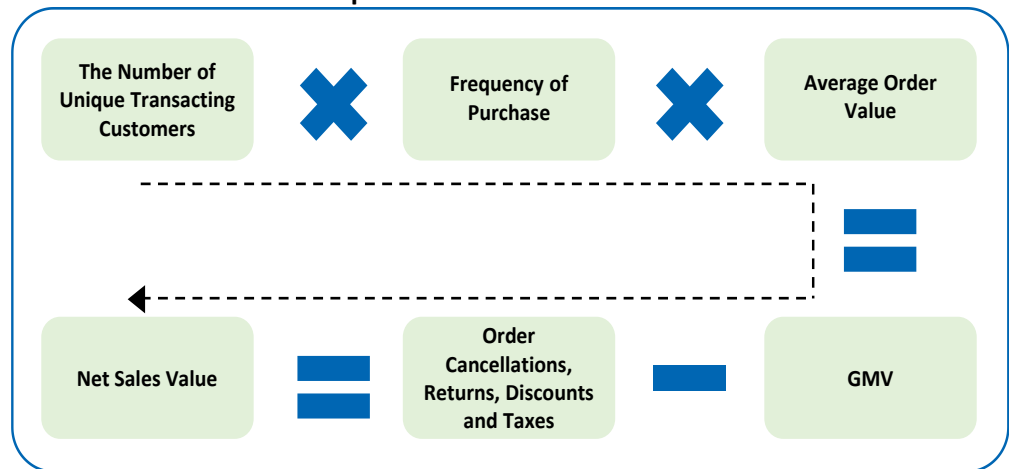
GMV to Revenue transition

The GMV or Gross Merchandise Value is inclusive of order cancellations, returns, discounts and taxes; excluding these items we arrive at the 'net sales value'.

'Net sales value' is not necessarily the same as 'net sales'. When Nykaa sells goods from its own inventory both NSV and Net sales are similar, but differ if it records only marketplace commission.

We believe value of sales less taxes, discounts, returns and cancellations at ~60-65% of GMV for BPC, and lower in Fashion segment on account of higher discounts.

Exhibit 8: The GMV is a composition of



Source: DART

Online vs. Off-line – key business dynamics and operational parameters

Before moving to the key drivers on e-commerce business, we compare below the key operational parameters and the business dynamics of off-line vs. online.

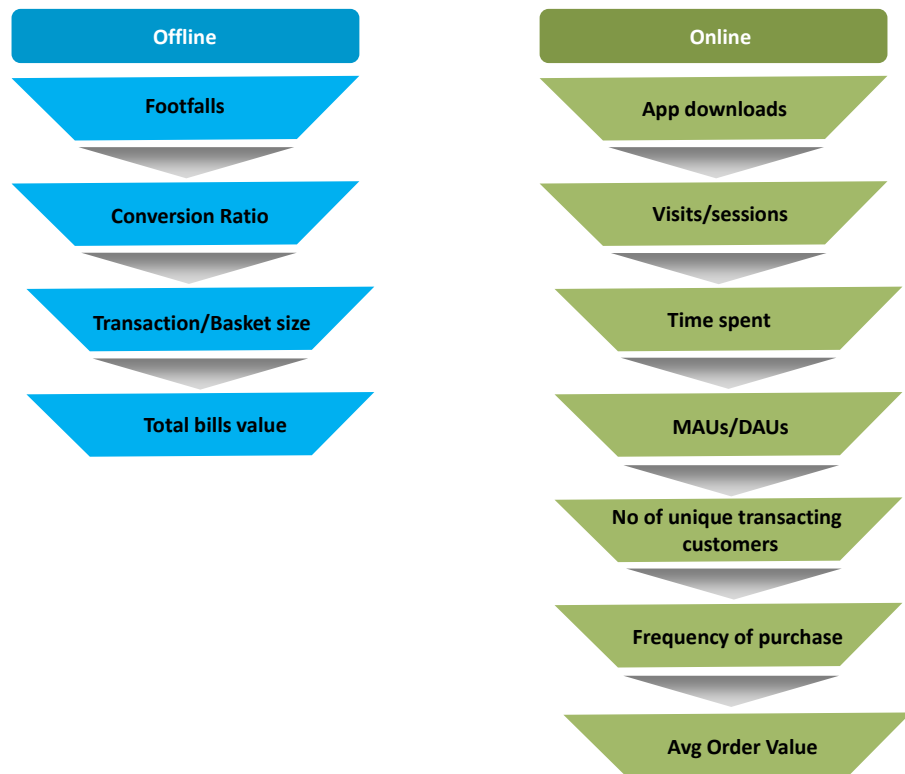
Exhibit 9: Offline vs. online – key business dynamics

| Offline | Online |
|---|--|
| Building a retail store requires huge investments in real estate (or rental costs) and furniture and fixtures, is capitalised as assets in the BS and expensed gradually over its useful life | While cost of developing an App is relatively less expensive, the cost to incentivise users to download the app (parallel to real estate cost in offline) is very high and it is expensed in the first year itself |
| Offline stores have high operating costs like rent, employee cost etc. which are fixed expenses, pushing up the break-even point compared to online | Once online reaches a sizeable scale, profitability of retailers can increase as benefits of operating leverage kicks in significantly. However to create the network effect, online companies need significantly higher marketing spend |

Source: Media articles, DART

Customer journey – Offline vs Online

Exhibit 10: Key milestones of customer journey - Offline vs. Online



Source: DART

The journey to unique transacting customers in digital economy involves

- (a) **App downloads:** Although purchases can be made on the website, ~85-90% of Nykaa’s GMV is derived on its app. Nykaa commonly known for BPC has a lot more to offer. Though the Nykaa app’s landing page is focused on beauty products, the company offers products in categories like laundry, breakfast options, dry fruits, consumer electronics, baby care, pet care, home decor etc.

To specifically address to the Men’s categories, Nykaa has separately created a website and app ‘Nykaaman.com.’ It offers products in categories like shaving, haircare, grooming kits and sports nutrition with exclusive brands. For eg. The Shave Doctor, Clinique for Men and Beardo are only available with NykaaMan.

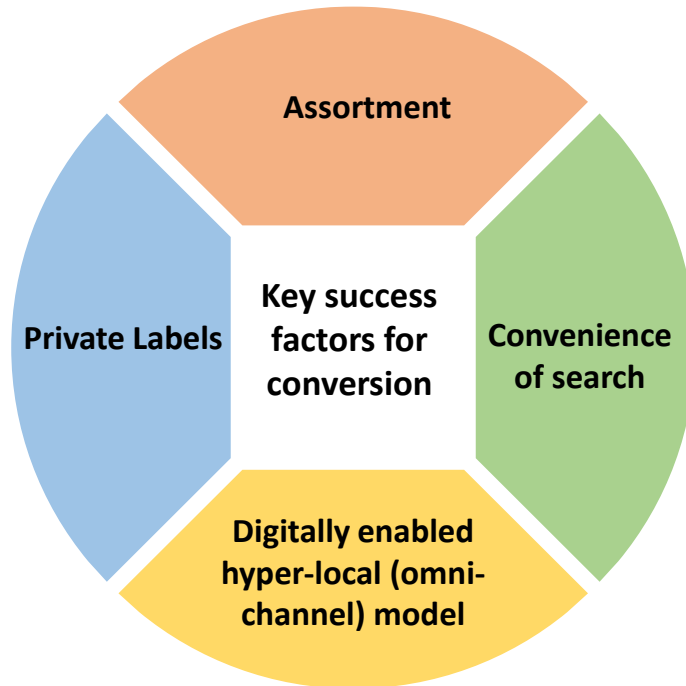
In Q2FY22, Nykaa launched “SuperStore by Nykaa” an eB2B platform bringing BPC access and expertise to underserved channels and markets using technology. Catering to retailers across India, the “SuperStore by Nykaa” aims to support and empower them to offer the best of the BPC products to their customers. The business will be an area of focus for quarters to come.

- (b) **Visit to the app:** Visit to the app is the next important step after the download. Beauty is a high involvement category, in which customers often research products before buying. Since Nykaa has launched the ‘Explore’ function in the app which allows users to view video content on styling, the number of visits increases, which is a positive sign.
- (c) **Unique visitors and unique transacting consumers:** While the total number of visits is one metric, it is also important that the number of unique visitors goes up and that the visits are not dominated by the same users just visiting more frequently. Conversion rate or conversion of visitors in customers is another most important metric.

Nykaa commonly known for BPC has a lot more to offer. The company has a total of ~20 listed categories on its app

While there is an opportunity to grow the number of customers by Nykaa, it needs to drive the journey from downloads to visits to transactions

Exhibit 11: Key success factors for conversion of customers



Source: Company, DART

Nykaa has ~0.25m SKUs and ~2,644 brands in the BPC segment as of Aug'21 which would be the widest choice available in this segment on any platform.

- A. **Assortment** of niche, premium and numerous brands. The most important driver for a user to come on board the Nykaa platform is the wide variety of brands offered and the ease of discovery.
- B. **Convenience of search:** Nykaa as a specialist in the BPC segment offer much better filters for a product and, therefore, a superior browsing experience. Potential users know this either via word of mouth or expect this given the specialised nature of the platform. This in our view is one of the reasons why a customer would buy on the Nykaa platform.

Nykaa management had categorically highlighted in its IPO meet that their experience has been consumer's preference for assortment, convenience followed by pricing.

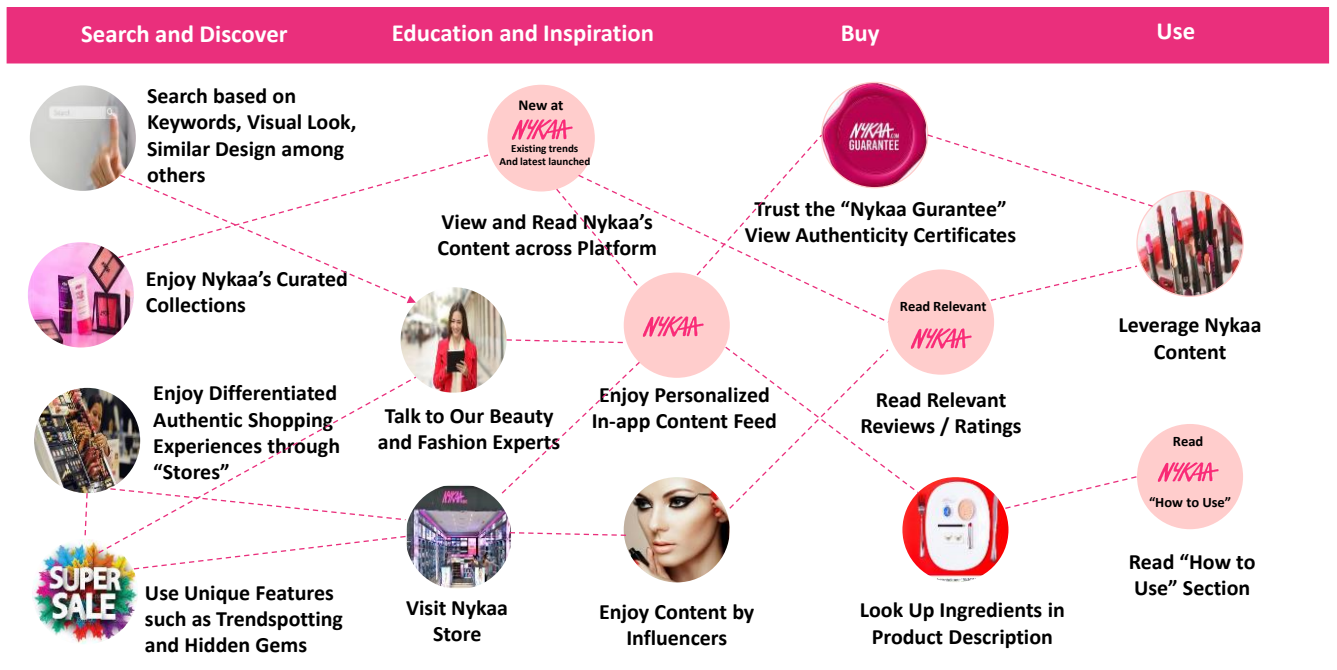
As per Redseer, Nykaa is one of the most influential lifestyle platforms in India with ~13.4 million followers across leading social media platforms as of Aug'21.

Virtuous cycle of content and traffic

- To build engagement on its platform, Nykaa works with over 3,055 (as of Aug'21) influencers including Generation Z trend setters, mommy bloggers, beauty, fashion and lifestyle bloggers, makeup artists and celebrities, to create content on its platform.
- *Nykaa TV* (a Youtube channel with 1.5m hours of content and 1.2m subscribers as of Aug'21) and *Explore* (a feature in the Nykaa app which allows users to watch content and at the same time buy the products featured in that video) prompt viewers to transact, thereby converting users of the app into customers.
- *Nykaa Network* is a peer-to-peer social community with 3.6m members, who can chat with other beauty enthusiasts, ask and answer beauty-related questions, give and seek advice, discover trends and join beauty-centric conversations on topics of their interest. It is one of the first interactive beauty forum.

Exhibit 12: Consumer Journey

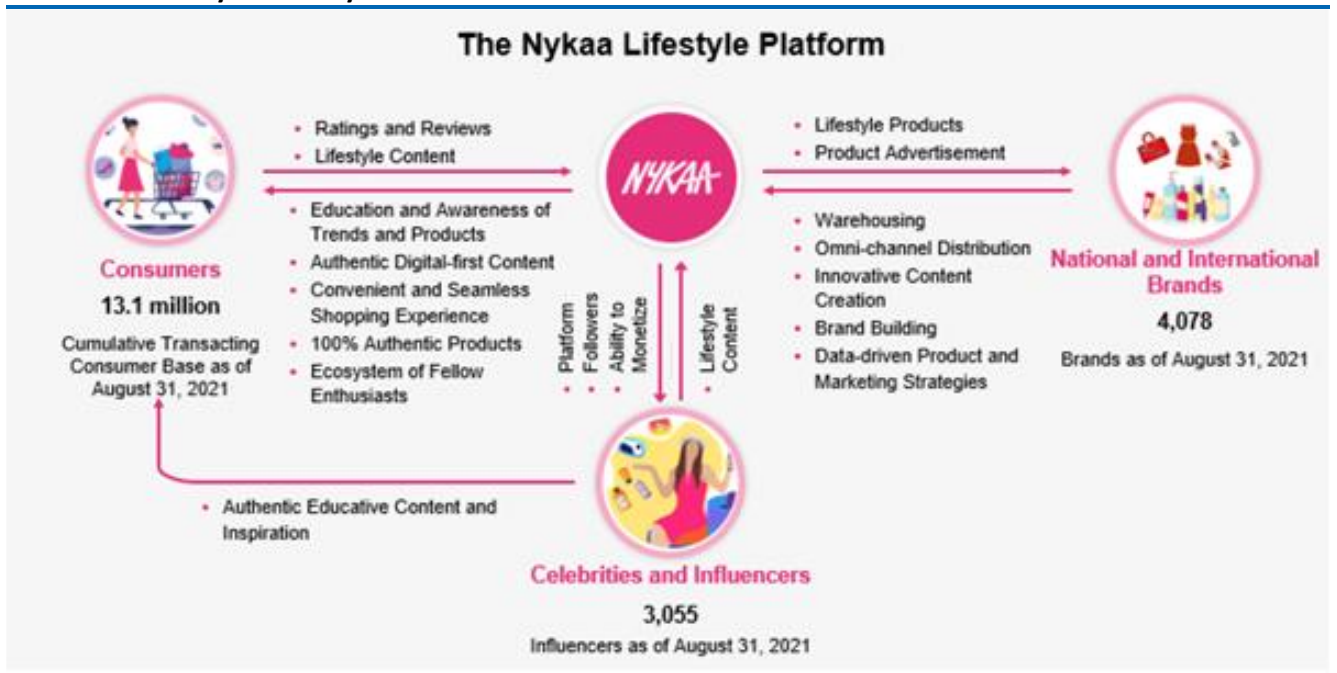
Illustrative Nykaa Consumer Journey



Source: Company, DART

In addition to leveraging its strengths in comprehensive merchandising, brand relationships and delivery experience, it focuses on educating consumers via digital content, digital communities and tech-product innovations, which is an integral component of Nykaa's business model.

Exhibit 13: The Nykaa Lifestyle Platform



Source: Company, DART

C. Digitally enabled hyper-local (omni-channel) model - The Next Wave

High customer acquisition and logistics cost of online are key barriers in our view pushing online players for convergence with offline. Online multi-brand platforms are constantly reinventing their existing business models and strategies to ensure that they are on the path to profitability. Many retailers and e-commerce firms are coming together to build a blended distribution network. Retailers (both e-tailers and B&M) appear to have ascertained that e-commerce is more of a friend than a foe. They are following the precedent set by the off-line retailers who have improved profitability and market share by leveraging private labels.

Exhibit 14: Hybrid model evolving

| Pros and Cons of Online Retail | | Pros and Cons of Off-line Retail | |
|--|-------------------------------------|--|--------------------------------------|
| Weakness | Strength | Strength | Weakness |
| No touch and feel of Product | Easy access to market for suppliers | Touch and feel of Product | Limitation in expansion |
| High Logistic cost | Convenience Door-step delivery | High customer satisfaction with wider product experience | Require customer's physical presence |
| Recommended only for standardized products | Low capex/inventory | Low logistic cost | High capex/inventory |

Source: DART

Retailers need to be present everywhere – whether B&M, on app, website, ecommerce platforms, social media, WhatsApp. The customer experience on all platforms has to be smooth with quick execution and delivery. The e-commerce stack includes web portals and mobile-sites and the capability to integrate seamlessly with over different marketplace partners. This are developed on a common technology platform that is robust, flexible and integrated with offline enterprise technology implemented in warehouses and stores, enabling seamless omni-channel capabilities. While the e-commerce functionality is standard in the apps, companies are also introducing ‘digital store’ capabilities, enabling customers to virtually shop in nearby stores and directly interact with store associates for planning visits, scheduling pickups or alterations. **Companies that have strong physical store networks, coupled with own e-commerce sites, would be able to make incremental margins over the long term.**

Omni channel – strategic focus area for Nykaa

Nykaa’s distribution capabilities enable it to reach customers residing in over 26,727 pin codes (89.2% coverage of all the serviceable India pin codes). An algorithm driven fulfilment model uses a pan India network of 20 warehouses (combined storage of 6,65,371 sqft) to ensure optimized delivery time, inventory management and shipping costs. The fulfilment is enacted through renowned 3rd party couriers that execute delivery from warehouse to the consumer pin. Leveraging its distribution capabilities, Nykaa has put in place its offline retail strategy, thereby establishing a footprint of a future omni-channel player.

Nykaa has 80 stores as of Aug’21 (84 as of Sep’21) across 40+ cities making it one of the largest offline multi-brand BPC platform.

Exhibit 15: Three store formats that decorate Nykaa’s retail strategy

| Store Brand | No of stores | Typical size (sqft) | Offerings | States |
|----------------|--------------|---------------------|---|---|
| Nykaa Luxe | 38 | 1100-1150 | Premium international brands | Grade A malls and High Streets in Mumbai, Delhi and Kolkata |
| Nykaa On Trend | 32 | 700-750 | Differentiated consumer experience for the premium to up-market segments offering best-selling products across categories | Coimbatore, Chennai and Jaipur |
| Nykaa Kiosks | 10 | | Free-standing units in the atriums of shopping malls | Bengaluru, Indore and Mohali |

Source: Company, DART

In addition to providing a plethora of benefits, physical stores are a customer recruitment tool. Store fronts are a free advertising space, footfalls drive brand visibility for consumers

The below excerpt from the DRHP aptly explains the role of the omni channel:

“Omnichannel model will be beneficial for online BPC platforms. Supplementing their online platforms with a physical retail store presence helps complete consumer experience. The touch and feel, test and try elements become crucial in certain specialized BPC categories. Offline stores play an important role in providing desired experience and help establish a stronger trust among the consumers. Consumers are likely to be engaged better if attended in-person, which is feasible in offline stores. Presence across online and offline channels expands the modes of acquiring consumers and increases the likelihood of receiving organic traffic. Retail stores provide added flexibility with respect to logistics while increasing delivery options for consumers including hyperlocal delivery, store pick-up.”

Nykaa thus plans to invest ~Rs 540mn to expand its physical presence and additional ~ Rs 924mn for warehouse capacity. These should significantly enhance the omni-channel capabilities of Nykaa and act as an enabler for growth acceleration.

Exhibit 16: Capex on expansion of stores / warehouses from the IPO proceeds

| Particulars | Estimated amount (Rs Mn) | Amount from IPO proceeds (Rs Mn) | Expansion plans (in Sqft) | No of stores/warehouse use | Capex/Sqft (Rs) | Capex/Store or warehouse (Rs Mn) |
|---|--------------------------|----------------------------------|--------------------------------|----------------------------|-----------------|----------------------------------|
| Funding the set-up of new retail stores | 539 | 420 | 75,000 @ (Avg 650sqft/store_ | ~115 | 7,187 | 4.7 |
| Capex for set-up of new warehouses | 924 | 420 | 350,000 @ (50k sqft/warehouse_ | ~7 | 2,640 | 132.0 |

Source: Company, DART

D. Private Labels

In recent years’ private labels have emerged as the rising star of retail and e-commerce. Private labels or in-house brands, typically offer shoppers value for money, while earning higher margins - around twice as much as external brands. Private labels have the potential to develop into self-sustaining brands with a loyal consumer base and grow beyond the captive platform.

Private label offers great supply chain efficiencies through absence of intermediaries, higher control across the value chain that reduces leakages and greater product customization abilities that translates into higher margins.

Our channel checks with the industry suggest that tier-2/3 customers regard ‘quality’ and ‘value for money’ much more than ‘brand’. We believe that by controlling the entire value chain – from contract manufacturing to logistics – companies can offer 20-30% lower prices.

Exhibit 17: Private Label - The approach aims at below

| Particulars | Outsourced | Private label |
|---|---|--|
| Margin | 30% | 60% |
| Idea generation to execution time frame | 6-12 months | 15-90 days |
| Adaption of trends | Slower, as order has to be placed months in advance | Faster- as order need not be placed in advanced internally |
| Risk | Lesser | Higher |
| Customer centric | Products are less customer centric | Products can be made more customer centric |

Source: DART, EY

Exhibit 18: Margin comparison of branded sales vs. private label

| Categories | Margin % | |
|------------|---------------|---------------|
| | Branded Sales | Private Label |
| Apparel | 35-40 | 60-65 |
| Grocery | 7-10 | 10-14 |
| Furniture | 18-20 | 45-50 |
| Cosmetics | 35-40 | 70-75 |
| Wellness | 15-18 | 22-25 |
| CDIT | 18-20 | 50-55 |

Source: DART, EY

Nykaa has the below private labels in fashion as well as the BPC space. Nykaa's private labels account for ~6-8% of revenue. It would be important to see how Nykaa manages the balance of growing its own private label portfolio vs. maintaining relationship with brands.

Exhibit 19: Nykaa's key owned brands in the BPC space

| Brands | Description |
|-----------------|---|
| Nykaa Cosmetics | A comprehensive makeup and beauty accessories brand present across lips, face, nails, eyes and beauty tools. |
| Nykaa Naturals | Naturally derived ingredients focused brand for skincare products such as bath and body offerings, masks and haircare |
| Kay Beauty | Kay Beauty offers premium range beauty products across lips, eyes, face and nails categories |
| Dot & Key | It offers premium skincare products across serums, toners, cleansers and face masks and has recently expanded into nutraceuticals |

Source: DART

Exhibit 20: Nykaa's key owned brands in the Fashion space

| Brands | Description |
|----------------|---|
| Twenty Dresses | The apparel product line includes western wear across dresses, jumpsuits, tops, pants skirts as well as footwear, bags, and accessories |
| Nykd by Nykaa | Nykd by Nykaa offers lingerie and includes bras, panties, sleepwear, shapewear and athleisure |
| Pipa Bella | Pipa Bella offers on-trend aesthetic jewelry such as earrings, necklaces, bracelets, rings and hair accessories. |
| RSVP | It offers a wide and premium collection of dresses, jumpsuits, tops and skirts as well as footwear and bags |
| Gajra Gang | It offers a wide and premium range of kurta sets, ethnic dresses, saree, tops and accessories. Recently it has expanded into Innerwear space. |

Source: DART

Nykaa Fashion has offerings from 1,434 brands and 2.8mn SKUs that cater to men, women, kids & home. The brands housed are established national, international, luxury brands and designer labels.

As per the management, the unit economics for BPC and Fashion are broadly similar except for difference in accounting

Nykaa Fashion – a high growth engine

The addressable market opportunity in Fashion segment is significantly larger for Nykaa viz. ~3.5x of the BPC segment. We discuss in detail on the industry size of overall Retail, BPC and Fashion in the Industry section of the report.

To deepen the focus on the fashion vertical, a separate online presence via website and mobile app for Nykaa Fashion has been set up, rather than embedding it within the existing app. This is one of the key differentiator that goes against the common strategy of other (online businesses) that enter adjacent verticals via the existing apps. We believe that this differentiated strategy is a key winning enabler for verticals that have several product sub-categories with large SKUs.

Reason for marketplace vs. inventory led model for Fashion business

Nykaa Fashion is predominantly a curated and managed market place unlike Nykaa BPC which is largely an inventory led model. The Fashion business model has been tweaked as fashion segment needs a far wider assortment of SKUs compared to the BPC segment. Thus, inventory risks is also higher in Fashion segment. Also, BPC is very brand centric and within brands it is very product centric. Further, Fashion is very fragmented and products go in and out of style very frequently.

Product curation is a key differentiator for Nykaa Fashion which helps build uniqueness around its offerings in the online platform space. This enables the company in selling full priced products (as against the common strategy of discounting pursued by its peers), which in turn leads to higher AOVs. This has resulted in 17.4/16.1% of the fashion vertical GMV in FY21/5m Aug-21 at full-price collections (at 10% or less discounts).

Nykaa does some level of pre-selection for customers based on quality of product, whether the product is in trend etc. Nykaa does not list brand partners' entire catalogue on their platform. Barring the above tweaks Nykaa Fashion has replicated the success of the BPC playbook strategy of customer acquisition, content creation and mining consumer data.

It can also leveraged the customer base of its BPC vertical and launched its own private labels to plug product gaps. The setting up of its first offline store in NCR is a precursor to mirror the omni-channel approach of the BPC vertical.

Number of customers

Having only recently entered the 'fashion' segment, the number of unique, annual transacting customers for Nykaa in the segment is low at ~1.3mn in Q2FY22. Growth though, on a low base, has been high.

Target audience

Unlike the BPC segment, where Nykaa has defined the target audience (female in age-group 14-44 years) in our view, the target audience for the fashion category would be similar to that of others such as Amazon, Myntra, Meesho, Flipkart etc.

However, at least in initial years, users are more likely to be female. If brand Nykaa can hold mainstream appeal in the fashion segment, we shall soon see a fair share of the male population as its customers as well. There are ~140mn ecommerce shoppers in India. While the number of fashion shoppers is not available, a significantly large part of this 140mm should also be fashion shoppers. Theoretically, each such online shopper could be the target audience for Nykaa in the long run.

Key drivers of the Nykaa's business

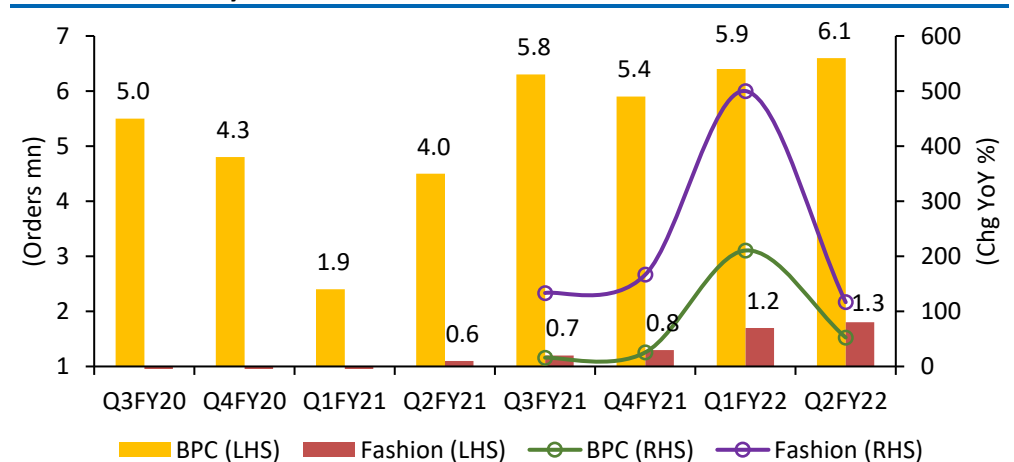
From a sector perspective, increase in the online BPC user base has been a key ingredient of the sector's growth. The rise in AOV (Average Order Value) despite the rising penetration in non-metros can be attributed to the wider acceptance of BPC as a key ecommerce category by Indian consumers in the last 3-4 years, due to the higher trust commanded by online BPC platforms with the help of engaging content and popular influencers. Trust is an important factor in this category, due to which vertical e-tailing platforms specializing in the BPC space, have enjoyed high growth in the online market. This has enabled consumers to shop for prestige BPC products and newer product categories, thus driving higher AOVs.

Number of orders

We believe that the number of orders placed on Nykaa platform is largely driven by base of consumers, mix of products and brands that are sold. An increase in Orders and GMV generally results in an increase in revenues from operations.

Contrary to expectations despite second wave of Covid in Q1FY22, Nykaa witnessed highest quarterly Orders and GMV for the business. Even in Q2FY22, it witnessed a moderate growth on QoQ basis.

Exhibit 21: Healthy trend of Orders



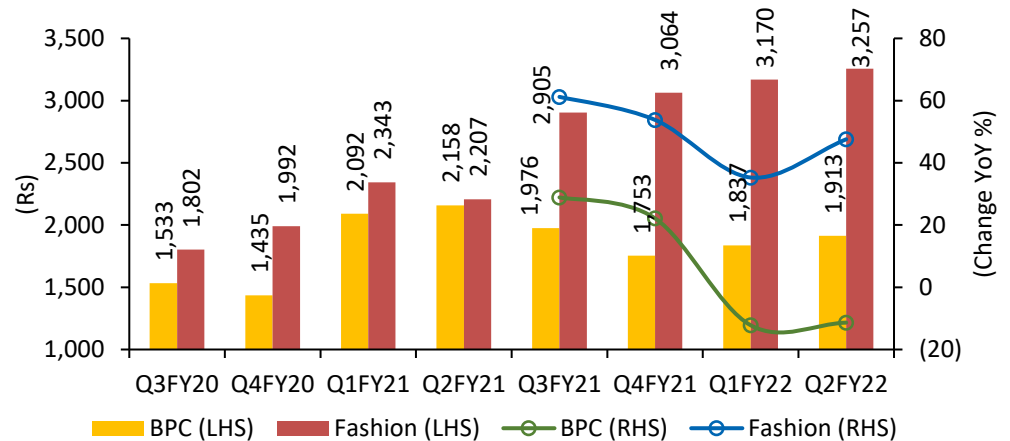
Source: Company, DART

Average Order Value and GMV

The lockdowns imposed due to the first wave of COVID-19 outbreak led to supply chain disruptions. Due to this, Nykaa decided to fulfil Orders only above a minimum AOV threshold and also increased the threshold for free shipping in BPC vertical, which led to an increase in AOV. Subsequently as lockdown restrictions were gradually relaxed, company reduced the minimum AOV threshold for Order placement and free shipping, which led to a normalisation of AOVs. Yet, the AOV continued to trend higher than pre-COVID-19, due to an increase in assortment leading to higher basket sizes and change in consumer behaviour in favor of purchasing more luxury and prestige brands resulting in an increase in average selling price per unit in BPC segment.

In fashion business, the increase in AOVs has been a result of an increase in assortment including the launch of new consumer divisions like Men and Kids and on boarding of premium brands. Nykaa does some level of pre-selection for customers based on quality of product, whether the product is in trend etc. Nykaa does not list brand partners' entire catalogue on their platform.

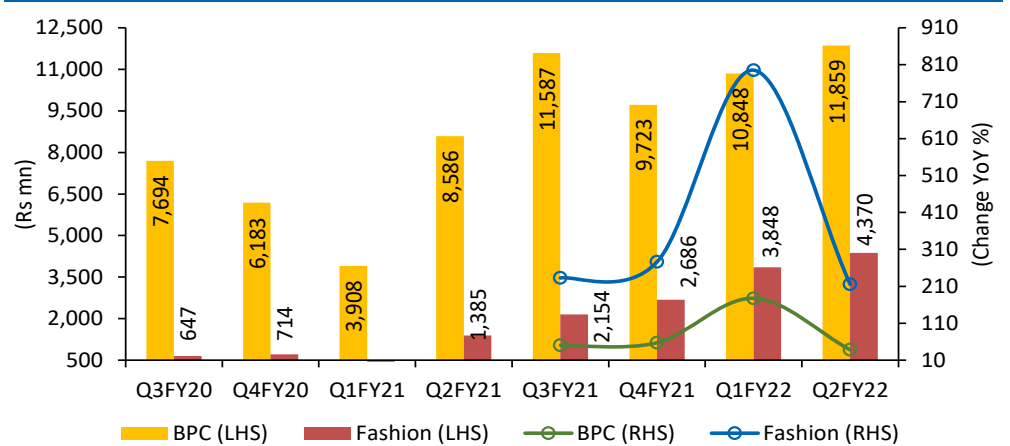
Exhibit 22: Nykaa enjoys a superior AOV



Source: Company, DART

We find the Nykaa's AOV on higher side. We believe it could potentially be on account of category-mix in the BPC segment, family rather than individual buying and the affluent class of customers that would have a higher per-capita spend

Exhibit 23: Quarterly trend of GMV



Source: Company, DART

Growth in GMV

We forecast GMV CAGR of 52% during FY21-24E, 33% over FY24-27E and 21% over FY27-31E viz. 33% CAGR over FY21-31E. Led by new customer additions, increase in categories purchased, premiumization, price increases and loyalty programs.

Nykaa - preferred partner for customers & brands – key strength

The brand affinity that Nykaa has built with consumers through authenticity, product curation, content, attracts them to engage on platform, rather than driving sales through aggressive marketing and discounting. This in our view is the key differentiator that brings brands to the platform. With more consumers and more transactions, it becomes imperative for more brands and more sellers to be associated with Nykaa which further increases the choice for consumers. Leveraging their brand strength, Nykaa continues to add more lifestyle verticals and adjacencies on its platform which is expected to further increase consumer base.

Nykaa's has tailored specific capabilities across marketing, technology, supply chain, fulfilment, and consumer service to create a differentiated ecosystem for brands and consumers. As a result, many global luxury brands such as Charlotte Tilbury, Huda Beauty, Mario Badescu, Pixi and Tangle Teezer have chosen Nykaa to import, launch and sell their products to consumers in India.

Nykaa's leading position drives self-reinforcing flywheels, which further drive strong network effects

Case study – Huda Beauty

Huda Beauty launched in India with Nykaa in Jan'18. With ~6,000 Liquid Matte Lipsticks sold in 24 hours, Huda Beauty clocked the highest revenue for a brand on its launch day on its platform. Huda Beauty continues to be a leading luxury brand and over 300,000 unique customers have purchased its product since launch. Given the success of this launch, Nykaa and Huda Beauty have expanded their relationship with the launch of Wishful and Kayali, new skincare and fragrance brands from Huda.

These above has made Nykaa, a preferred destination especially for the luxury and prestige BPC products for both consumers and brands. It is also reflected in the share of Nykaa's GMV from existing customers as well as top vendors.

Exhibit 24: Self-reinforcing flywheels drive strong network effects



Source: Company, DART

Exhibit 25: Top five vendors of Nykaa and their key brands

| Company | Brands |
|-------------------------------|---|
| Elca Cosmetics (Estee Lauder) | Clinique, Estée Lauder, Bobbi Brown, MAC |
| Hindustan Unilever | Lakme, Fair & Lovely |
| Honasa Consumers | Mamaearth |
| Huda Beauty | House of Huda, WildWish, GloWish, Kayali |
| L'Oreal India | Mass market (L'Oréal Paris, Garnier, Maybelline New-York and NYX Professional Make up); Hair and beauty salons (L'Oréal Professionnel, Matrix, Kérastase); |

Source: Company, DART

Top five vendors account for ~33% of Nykaa's BPC GMV view

Exhibit 26: Top Vendors Revenue from BPC segment

| Rs Mn | FY19 | FY20 | FY21 |
|--------------|-----------------|-----------------|-----------------|
| HUL | 1,76,550 | 1,73,450 | 1,79,640 |
| Loreal India | 32,744 | 34,614 | 28,584 |
| Honsaa | 53 | 168 | 1,098 |
| Elca | 2,687 | 3,230 | 3,831 |
| Total | 2,12,034 | 2,11,463 | 2,13,152 |

Source: Company, DART

Exhibit 27: Share of top five vendors in Nykaa's GMV

| Particulars | FY19 | FY20 | FY21 | 5m Aug'21 |
|--|---------------|---------------|---------------|---------------|
| GMV (Rs Mn) | 16,501 | 26,849 | 40,460 | 26,214 |
| - BPC | 16,219 | 24,981 | 33,804 | 19,316 |
| - Fashion | 282 | 1,868 | 6,656 | 6,897 |
| GMV from top five vendors (%) | 38.1 | 30.8 | 27.9 | 21.5 |
| Implied GMV from top five vendors (Rs Mn) | 6,287 | 8,270 | 11,288 | 5,636 |
| GMV from top five vendors as % of BPC GMV (computed) | 38.8 | 33.1 | 33.4 | 29.2 |

Source: Company, DART

While the revenue of top suppliers to Nykaa has been constant (largely on account of HUL), Nykaa's share of GMV from this vendors has been on rise which is positive.

Also, Nykaa's share of GMV as a % of their revenue is only a modest 5% which has significant headroom for growth.

Nykaa's top five suppliers accounts for ~22% (33% excluding Fashion) of Nykaa's GMV. BPC has been the key category for Nykaa. Fashion is a recent addition and fast-growing category. The top five vendors of Nykaa primarily seems to be BPC suppliers. The decline in share of top five vendors as % of GMV we believe is on account of Fashion business which forms part of denominator. Thus if we exclude fashion, the share of top five vendors have declined from 39% in FY19 to 33% in FY20 & FY21. We would ignore the share of top five vendors in 5m Aug'21 at 29% as this could be on account of seasonality factor.

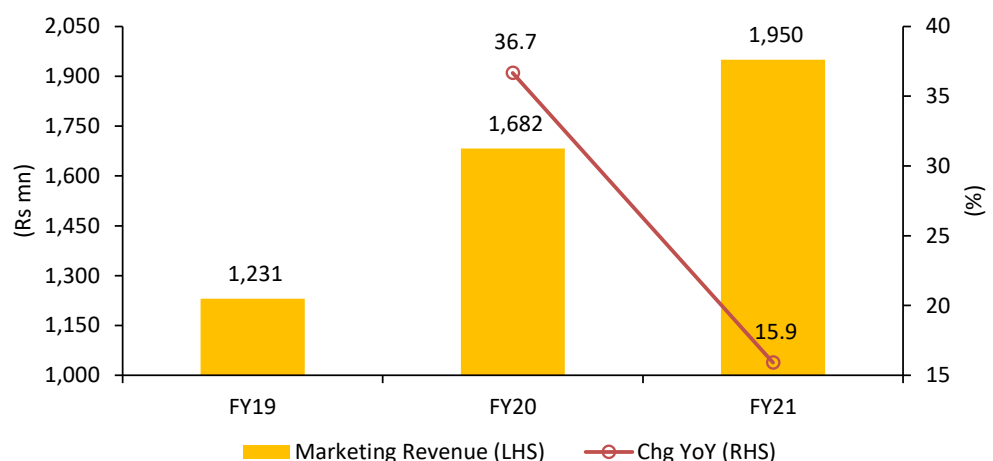
That said, we believe that as Nykaa keeps expanding its bouquet of offering across categories and vendors the share of top five vendors in GMV is likely to decline though the absolute size and scale of business keeps increasing.

Marketing support revenue

In addition to revenue from sale of products (either via marketplace or inventory model), Nykaa also gets revenues from marketing support. These includes (a) marketing income from visibility services provided by it to various brands at retail outlets and (b) revenue from advertising services which allow brands and sellers to place advertisements or show their products in particular areas of Nykaa's websites and mobile applications at fixed or variable fees". This is a very important driver of profit margins because there is little-to-nil associated cost in our view.

Increased customer visits and transactions and thus higher ad rates, roll out of physical stores shall result in greater avenues of display/merchandising-led fees and / or listing fees for brands which should further drive the marketing support revenues. Currently, contribution from the fashion vertical shall be negligible, but as it ramps up, there could be some contribution from fashion brands as well.

Exhibit 28: Marketing support revenue trend and growth (%)

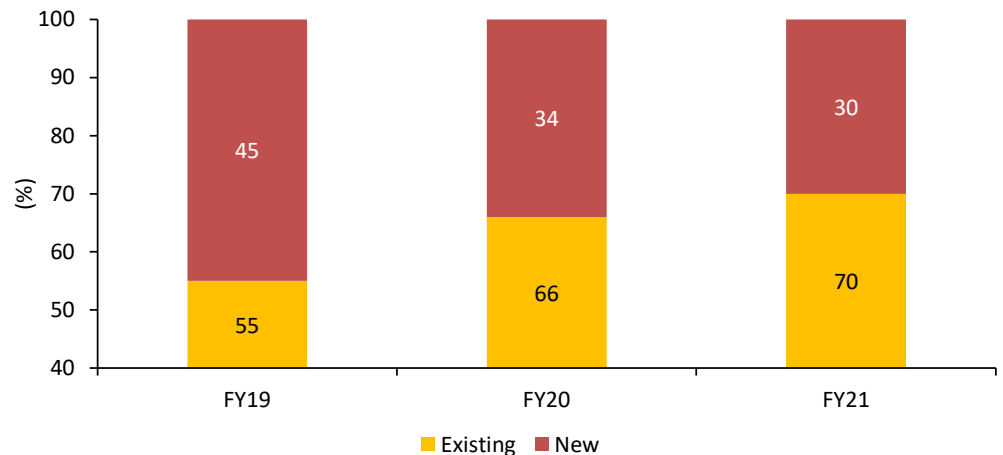


Source: Company, DART

Strong consumer pull – a positive

Nykaa’s success is significantly dependent on its ability to continually attract New Consumers, retain Existing Consumers and cultivate loyalty, including through increasing repeat purchases. We observe a high level of loyalty for Nykaa platform among consumers, with majority of its GMV stemming from Existing Consumers. The high consumer centricity is reflected in strong consumer retention and GMV contribution behaviour.

Exhibit 29: Contribution to GMV by existing and new customers (%)



Source: Company, DART

Nykaa has a loyalty programme for its consumers – ‘Nykaa Prive’, which had 2.1m members in FY21. Benefits for members include exclusive offers, discounts, complimentary gifts, free shipping, access to exclusive members’ only content and priority access to the consumer service team. In addition to the loyalty programme, normal consumers can also earn reward points by signing up (100 reward point = Re 1 with 2,000 points on signing up), writing reviews and answers, new customer referrals, etc. These rewards can be redeemed to make purchases on the Nykaa platform. Nykaa is currently redefining ‘Nykaa Prive’ to make it more comprehensive and rewarding for our consumers.

Costs structure

Nykaa’s costs structure primarily comprises of below-mentioned three variable / semi-variable items. We discuss on each of them below with our estimates in key assumption table. Employee costs is another major line-item.

Cost of goods sold (COGS)

COGS pertains to only those products that are sold based on the inventory model; it does not apply to marketplace sales. Therefore, calculating COGS as a percentage of revenue is not meaningful; one needs to look at it as a percentage of net sales (after discount) which in our view is difficult to ascertain in absence of disclosure. Thus, we are compelled to forecast COGS as a % of revenue.

As Nykaa’s scale of operations increases, it may be able to negotiate better margins. Alternatively, as some of the niche brands that sell via Nykaa are able to scale up and go mainstream their dependence on Nykaa may reduce. Further, as Nykaa expands into more mass-market brands and categories from luxury and prestige BPC products, margins from such avenues are likely to be lower, because trade margins for such brands are generally lower.

That said, broadly we believe COGS as a % of revenue to decline (and thus gross margin increases) as the share of Fashion business in overall GMV keeps increasing. These is on account of only commission revenue accounting in Fashion business owing to market place model. Increase in share of private label can also drive the GM higher.

Marketing and Advertising expenses

Nykaa invests in marketing and advertisement initiatives to drive new consumer's acquisitions on its platform and to encourage Existing Consumers to increase the frequency of purchase. While it has gained prominence as a lifestyle retail platform by leveraging core capabilities in content, social media and influencer marketing, its cost effectiveness depends on its ability to attract and retain consumers at reasonable marketing expenses.

As a % of revenue, marketing expenses decreased from 12.9% in FY19, 11.4% in FY20 and 6.9% in FY21. The drop in FY21 was due to an increase in AOV, an increase in GMV contribution from Existing Consumers and partially due to muted spend during H1FY21 on account of Covid. However in Q1/Q2FY22 the spend again inched up to 11.1/13.3% of revenue due to higher spend in marketing for new consumer acquisition across verticals and for building awareness for new initiatives of online platforms such as "Nykaafashion.com" and "Nykaaman.com".

For the next few years, as Nykaa would want to maintain high growth in customer additions, it will have to increase the pace of advertising partly off-set by higher scale of operations and repeat purchases. However, when customer addition growth slows down, marketing costs can come off and significant operating leverage would be available on this cost item. We estimate the marketing costs to gradually decline from 11-13% and to settle around 7-8% by FY31.

Fulfilment costs

AOV impacts fulfilment costs

Nykaa incurs freight, packaging costs and payment gateway charges for the products that it ships from warehouses as a part of other expenses. It works with delivery companies to ensure smooth and efficient delivery of products to consumers. It pays service fees to delivery companies that carry out deliveries and pick-up services. Nykaa's cost effectiveness depends on its ability to continue optimising fulfilment costs on a per order / shipment basis through operational efficiencies like improved terms on service fee with delivery partners with increasing orders.

As a % of revenue from operations, fulfilment costs decreased from 9.7% in the FY19 to 8.9% in the FY21 due to an improvement in AOV over this period. However, as a % of revenue from operations, fulfilment costs increased to 11.4% for Q1FY22 due to higher split shipment on account of capacity constraints and partial dilution in AOV. Surprisingly the costs declined significantly in Q2FY22 to 10.3% of revenues.

AOV also has an implication on the fulfilment costs. A higher AOV would imply lower fulfilment costs and vice-versa. With new warehouse addition coupled with increase in scale of operations we expect some efficiencies in the fulfilment costs.

That said we believe company would be fine growing the overall revenues through a combination of higher unique transacting consumers * higher orders/customers and/or * higher AOV.

Key Operating Assumptions

| Particulars | FY19 | FY20 | FY21 | FY22E | FY23E | FY24E | FY25E | FY26E | FY27E | FY28E | FY29E | FY30E | FY31E |
|------------------------------|---------------|---------------|---------------|---------------|---------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Consumers (Mn) | 3.5 | 5.4 | 6.2 | 8.5 | 10.9 | 13.6 | 16.3 | 19.7 | 23.1 | 27.2 | 30.8 | 35.0 | 39.8 |
| BPC | 3.5 | 5.3 | 5.6 | 7.3 | 9.1 | 10.9 | 12.6 | 14.4 | 16.2 | 18.3 | 20.1 | 22.1 | 24.3 |
| Fashion | - | 0.1 | 0.6 | 1.2 | 1.8 | 2.7 | 3.8 | 5.3 | 6.9 | 8.9 | 10.7 | 12.9 | 15.5 |
| Orders (Mn) | 11.4 | 18.1 | 19.5 | 33.0 | 43.2 | 57.0 | 72.0 | 91.5 | 109.6 | 131.8 | 150.0 | 171.0 | 195.3 |
| BPC | 11.0 | 17.0 | 17.1 | 27.5 | 34.4 | 43.0 | 51.5 | 61.9 | 71.1 | 81.8 | 90.0 | 99.0 | 108.9 |
| Fashion | 0.4 | 1.1 | 2.4 | 5.5 | 8.8 | 14.1 | 20.4 | 29.6 | 38.5 | 50.0 | 60.0 | 72.0 | 86.5 |
| Orders/Cust. pa (Nos) | 3.3 | 3.4 | 3.1 | 3.9 | 4.0 | 4.2 | 4.4 | 4.6 | 4.7 | 4.8 | 4.9 | 4.9 | 4.9 |
| BPC | 3.1 | 3.2 | 3.1 | 3.8 | 3.8 | 3.9 | 4.1 | 4.3 | 4.4 | 4.5 | 4.5 | 4.5 | 4.5 |
| Fashion | - | 11.0 | 4.0 | 4.6 | 4.9 | 5.2 | 5.4 | 5.6 | 5.6 | 5.6 | 5.6 | 5.6 | 5.6 |
| AOV (Rs) | 1,447 | 1,483 | 2,075 | 2,102 | 2,298 | 2,525 | 2,710 | 2,900 | 3,083 | 3,270 | 3,411 | 3,555 | 3,702 |
| BPC | 1,433 | 1,448 | 1,963 | 1,874 | 2,053 | 2,258 | 2,428 | 2,610 | 2,806 | 3,016 | 3,167 | 3,325 | 3,491 |
| Fashion | 655 | 1,604 | 2,739 | 3,244 | 3,256 | 3,338 | 3,421 | 3,507 | 3,595 | 3,684 | 3,777 | 3,871 | 3,968 |
| GMV (Rs Mn) | 16,501 | 26,849 | 40,460 | 69,351 | 99,211 | 1,44,009 | 1,94,995 | 2,65,251 | 3,37,909 | 4,31,055 | 5,11,693 | 6,08,010 | 7,23,166 |
| BPC | 16,219 | 24,981 | 33,804 | 51,511 | 70,554 | 97,012 | 1,25,145 | 1,61,437 | 1,99,577 | 2,46,726 | 2,84,969 | 3,29,139 | 3,80,156 |
| Fashion | 282 | 1,868 | 6,656 | 17,840 | 28,657 | 46,997 | 69,850 | 1,03,814 | 1,38,333 | 1,84,328 | 2,26,724 | 2,78,870 | 3,43,011 |
| Change YoY (%) | | | | | | | | | | | | | |
| Consumers (Mn) | | 54.3 | 14.8 | 36.8 | 28.5 | 25.0 | 20.0 | 20.8 | 17.2 | 17.7 | 13.3 | 13.5 | 13.7 |
| BPC | | 51.4 | 5.7 | 30.0 | 25.0 | 20.0 | 15.0 | 15.0 | 12.5 | 12.5 | 10.0 | 10.0 | 10.0 |
| Fashion | | - | 500.0 | 100.0 | 50.0 | 50.0 | 40.0 | 40.0 | 30.0 | 30.0 | 20.0 | 20.0 | 20.0 |
| Orders (Mn) | | 58.8 | 7.7 | 69.2 | 30.8 | 32.1 | 26.2 | 27.1 | 19.9 | 20.3 | 13.8 | 14.0 | 14.2 |
| BPC | | 54.5 | 0.6 | 60.8 | 25.0 | 25.0 | 20.0 | 20.0 | 15.0 | 15.0 | 10.0 | 10.0 | 10.0 |
| Fashion | | 175.0 | 118.2 | 129.2 | 60.0 | 60.0 | 45.0 | 45.0 | 30.0 | 30.0 | 20.0 | 20.0 | 20.0 |
| AOV (Rs) | | 2.5 | 39.9 | 1.3 | 9.3 | 9.9 | 7.3 | 7.0 | 6.3 | 6.1 | 4.3 | 4.2 | 4.1 |
| BPC | | 1.0 | 35.6 | -4.5 | 9.6 | 10.0 | 7.5 | 7.5 | 7.5 | 7.5 | 5.0 | 5.0 | 5.0 |
| Fashion | | 144.9 | 70.8 | 18.4 | 0.4 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 |
| GMV (Rs Mn) | | 54.0 | 35.3 | 71.4 | 43.1 | 45.2 | 35.4 | 36.0 | 27.4 | 27.6 | 18.7 | 18.8 | 18.9 |
| BPC | | 563.3 | 256.3 | 52.4 | 37.0 | 37.5 | 29.0 | 29.0 | 23.6 | 23.6 | 15.5 | 15.5 | 15.5 |
| Fashion | | 62.7 | 50.7 | 168.0 | 60.6 | 64.0 | 48.6 | 48.6 | 33.3 | 33.3 | 23.0 | 23.0 | 23.0 |

Source: Company, DART

Revenue composition

| Particulars | FY19 | FY20 | FY21 | FY22E | FY23E | FY24E | FY25E | FY26E | FY27E | FY28E | FY29E | FY30E | FY31E |
|----------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Revenue break-up | | | | | | | | | | | | | |
| Sale of products | 9,739 | 15,838 | 21,809 | 32,778 | 45,808 | 64,831 | 85,316 | 1,13,406 | 1,43,829 | 1,80,856 | 2,12,920 | 2,50,765 | 2,95,086 |
| Sale of services | 1,361 | 1,815 | 2,503 | 5,225 | 6,932 | 9,595 | 12,724 | 17,190 | 21,739 | 27,510 | 32,831 | 39,242 | 46,946 |
| - Mktg support | 1,231 | 1,682 | 1,950 | 3,656 | 4,400 | 5,337 | 6,244 | 7,321 | 8,307 | 9,433 | 10,347 | 11,356 | 12,468 |
| - Marketplace | 130 | 133 | 553 | 1,569 | 2,532 | 4,258 | 6,481 | 9,869 | 13,432 | 18,077 | 22,484 | 27,886 | 34,478 |
| Other Op Income | 14 | 22 | 97 | 207 | 251 | 306 | 371 | 451 | 549 | 667 | 811 | 985 | 1,198 |
| Total | 11,114 | 17,675 | 24,409 | 38,210 | 52,991 | 74,732 | 98,412 | 1,31,047 | 1,66,117 | 2,09,032 | 2,46,562 | 2,90,992 | 3,43,229 |
| Revenue Mix (%) | | | | | | | | | | | | | |
| Sale of products | 87.6 | 89.6 | 89.3 | 85.8 | 86.4 | 86.8 | 86.7 | 86.5 | 86.6 | 86.5 | 86.4 | 86.2 | 86.0 |
| Sale of services | 12.2 | 10.3 | 10.3 | 13.7 | 13.1 | 12.8 | 12.9 | 13.1 | 13.1 | 13.2 | 13.3 | 13.5 | 13.7 |
| - Mktg support | 11.1 | 9.5 | 8.0 | 9.6 | 8.3 | 7.1 | 6.3 | 5.6 | 5.0 | 4.5 | 4.2 | 3.9 | 3.6 |
| - Marketplace | 1.2 | 0.8 | 2.3 | 4.1 | 4.8 | 5.7 | 6.6 | 7.5 | 8.1 | 8.6 | 9.1 | 9.6 | 10.0 |
| Other Op Income | 0.1 | 0.1 | 0.4 | 0.5 | 0.5 | 0.4 | 0.4 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 |
| Total | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |
| Revenue chg YoY (%) | | | | | | | | | | | | | |
| Sale of products | | 62.6 | 37.7 | 50.3 | 39.8 | 41.5 | 31.6 | 32.9 | 26.8 | 25.7 | 17.7 | 17.8 | 17.7 |
| Sale of services | | 33.4 | 37.9 | 108.7 | 32.7 | 38.4 | 32.6 | 35.1 | 26.5 | 26.5 | 19.3 | 19.5 | 19.6 |
| - Mktg support | | 36.7 | 15.9 | 87.5 | 20.4 | 21.3 | 17.0 | 17.2 | 13.5 | 13.5 | 9.7 | 9.7 | 9.8 |
| - Marketplace | | 2.4 | 316.5 | 183.8 | 61.4 | 68.2 | 52.2 | 52.3 | 36.1 | 34.6 | 24.4 | 24.0 | 23.6 |
| Other Op Income | | 54.0 | 340.7 | 113.4 | 21.6 | 21.6 | 21.6 | 21.6 | 21.6 | 21.6 | 21.6 | 21.6 | 21.6 |
| Total | | 59.0 | 38.1 | 56.5 | 38.7 | 41.0 | 31.7 | 33.2 | 26.8 | 25.8 | 18.0 | 18.0 | 18.0 |

Consolidated P&L

| (Rs Mn) | FY19 | FY20 | FY21 | FY22E | FY23E | FY24E | FY25E | FY26E | FY27E | FY28E | FY29E | FY30E | FY31E |
|------------------------|--------|--------|--------|--------|--------|--------|--------|----------|----------|----------|----------|----------|----------|
| Revenue | 11,114 | 17,675 | 24,409 | 38,197 | 52,991 | 74,732 | 98,412 | 1,31,047 | 1,66,117 | 2,09,032 | 2,46,562 | 2,90,992 | 3,43,229 |
| COGS | 6,603 | 10,142 | 14,878 | 21,997 | 30,248 | 42,583 | 55,977 | 74,409 | 94,155 | 1,18,271 | 1,39,261 | 1,64,063 | 1,93,172 |
| Gross Profit | 4,511 | 7,533 | 9,531 | 16,200 | 22,744 | 32,149 | 42,435 | 56,638 | 71,962 | 90,761 | 1,07,301 | 1,26,929 | 1,50,058 |
| Employee costs | 1,173 | 1,956 | 2,836 | 4,072 | 5,582 | 7,719 | 9,967 | 13,013 | 16,175 | 19,957 | 23,082 | 26,711 | 30,893 |
| Marketing | 1,428 | 2,022 | 1,695 | 4,399 | 5,299 | 6,726 | 8,611 | 11,139 | 13,705 | 16,723 | 19,109 | 21,824 | 24,884 |
| Fulfilment | 1,074 | 1,730 | 2,177 | 3,597 | 4,574 | 6,205 | 8,030 | 10,712 | 13,177 | 16,631 | 19,405 | 23,207 | 27,167 |
| Other exps | 631 | 1,015 | 1,208 | 2,139 | 2,746 | 3,166 | 3,595 | 4,046 | 4,554 | 5,078 | 5,615 | 6,198 | 6,841 |
| Total Op. Exps | 4,306 | 6,723 | 7,916 | 14,207 | 18,201 | 23,816 | 30,202 | 38,910 | 47,611 | 58,389 | 67,211 | 77,941 | 89,786 |
| EBITDA | 205 | 811 | 1,614 | 1,993 | 4,543 | 8,333 | 12,233 | 17,728 | 24,351 | 32,372 | 40,090 | 48,988 | 60,272 |
| D&A | 309 | 595 | 671 | 857 | 996 | 1,143 | 1,295 | 1,440 | 1,570 | 1,699 | 1,839 | 1,991 | 2,155 |
| EBIT | (104) | 215 | 943 | 1,136 | 3,547 | 7,191 | 10,938 | 16,288 | 22,781 | 30,673 | 38,251 | 46,997 | 58,117 |
| Finance Costs | 263 | 443 | 307 | 443 | 530 | 609 | 617 | 581 | 546 | 514 | 484 | 456 | 429 |
| Other Income | 50 | 103 | 117 | 311 | 469 | 539 | 618 | 709 | 814 | 934 | 1,112 | 1,351 | 1,643 |
| PBT | (317) | (124) | 753 | 1,004 | 3,486 | 7,121 | 10,939 | 16,417 | 23,049 | 31,092 | 38,878 | 47,893 | 59,331 |
| Tax | (72) | 39 | 134 | 190 | 697 | 1,424 | 2,735 | 4,104 | 5,762 | 7,773 | 9,720 | 11,973 | 14,833 |
| PAT | (245) | (163) | 619 | 814 | 2,789 | 5,696 | 8,204 | 12,313 | 17,287 | 23,319 | 29,159 | 35,919 | 44,498 |
| AEPS (Rs) | (0.6) | (0.4) | 1.4 | 1.7 | 5.9 | 12.1 | 17.4 | 26.1 | 36.6 | 49.4 | 61.7 | 76.0 | 94.2 |
| Common Size (%) | | | | | | | | | | | | | |
| Revenue | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |
| COGS | 59.4 | 57.4 | 61.0 | 57.6 | 57.1 | 57.0 | 56.9 | 56.8 | 56.7 | 56.6 | 56.5 | 56.4 | 56.3 |
| Gross Profit | 40.6 | 42.6 | 39.0 | 42.4 | 42.9 | 43.0 | 43.1 | 43.2 | 43.3 | 43.4 | 43.5 | 43.6 | 43.7 |
| Employee costs | 10.6 | 11.1 | 11.6 | 10.7 | 10.5 | 10.3 | 10.1 | 9.9 | 9.7 | 9.5 | 9.4 | 9.2 | 9.0 |
| Marketing | 12.9 | 11.4 | 6.9 | 11.5 | 10.0 | 9.0 | 8.8 | 8.5 | 8.3 | 8.0 | 7.8 | 7.5 | 7.3 |
| Fulfilment | 9.7 | 9.8 | 8.9 | 9.4 | 8.6 | 8.3 | 8.2 | 8.2 | 7.9 | 8.0 | 7.9 | 8.0 | 7.9 |
| Other exps | 5.7 | 5.7 | 5.0 | 5.6 | 5.2 | 4.2 | 3.7 | 3.1 | 2.7 | 2.4 | 2.3 | 2.1 | 2.0 |
| Total Op. Exps | 38.7 | 38.0 | 32.4 | 37.2 | 34.3 | 31.9 | 30.7 | 29.7 | 28.7 | 27.9 | 27.3 | 26.8 | 26.2 |
| EBITDA | 1.8 | 4.6 | 6.6 | 5.2 | 8.6 | 11.2 | 12.4 | 13.5 | 14.7 | 15.5 | 16.3 | 16.8 | 17.6 |
| D&A | 2.8 | 3.4 | 2.8 | 2.2 | 1.9 | 1.5 | 1.3 | 1.1 | 0.9 | 0.8 | 0.7 | 0.7 | 0.6 |
| EBIT | (0.9) | 1.2 | 3.9 | 3.0 | 6.7 | 9.6 | 11.1 | 12.4 | 13.7 | 14.7 | 15.5 | 16.2 | 16.9 |
| Finance Costs | 2.4 | 2.5 | 1.3 | 1.2 | 1.0 | 0.8 | 0.6 | 0.4 | 0.3 | 0.2 | 0.2 | 0.2 | 0.1 |
| Other Income | 0.4 | 0.6 | 0.5 | 0.8 | 0.9 | 0.7 | 0.6 | 0.5 | 0.5 | 0.4 | 0.5 | 0.5 | 0.5 |
| PBT | (2.9) | (0.7) | 3.1 | 2.6 | 6.6 | 9.5 | 11.1 | 12.5 | 13.9 | 14.9 | 15.8 | 16.5 | 17.3 |
| Tax | (0.6) | 0.2 | 0.5 | 0.5 | 1.3 | 1.9 | 2.8 | 3.1 | 3.5 | 3.7 | 3.9 | 4.1 | 4.3 |
| PAT | (2.2) | (0.9) | 2.5 | 2.1 | 5.3 | 7.6 | 8.3 | 9.4 | 10.4 | 11.2 | 11.8 | 12.3 | 13.0 |

Source: Company, DART

Consolidated P&L.....Cont.....

| (Rs Mn) | FY19 | FY20 | FY21 | FY22E | FY23E | FY24E | FY25E | FY26E | FY27E | FY28E | FY29E | FY30E | FY31E |
|--------------------|------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Chg YoY (%) | | | | | | | | | | | | | |
| Revenue | - | 59 | 38 | 56 | 39 | 41 | 32 | 33 | 27 | 26 | 18 | 18 | 18 |
| COGS | - | 54 | 47 | 48 | 38 | 41 | 31 | 33 | 27 | 26 | 18 | 18 | 18 |
| Gross Profit | - | 67 | 27 | 70 | 40 | 41 | 32 | 33 | 27 | 26 | 18 | 18 | 18 |
| Employee costs | - | 67 | 45 | 44 | 37 | 38 | 29 | 31 | 24 | 23 | 16 | 16 | 16 |
| Marketing | - | 42 | (16) | 160 | 20 | 27 | 28 | 29 | 23 | 22 | 14 | 14 | 14 |
| Fulfilment | - | 61 | 26 | 65 | 27 | 36 | 29 | 33 | 23 | 26 | 17 | 20 | 17 |
| Other exps | - | 61 | 19 | 77 | 28 | 15 | 14 | 13 | 13 | 12 | 11 | 10 | 10 |
| Total Op. Exps | - | 56 | 18 | 79 | 28 | 31 | 27 | 29 | 22 | 23 | 15 | 16 | 15 |
| EBITDA | - | 295 | 99 | 23 | 128 | 83 | 47 | 45 | 37 | 33 | 24 | 22 | 23 |
| D&A | - | 93 | 13 | 28 | 16 | 15 | 13 | 11 | 9 | 8 | 8 | 8 | 8 |
| EBIT | - | (308) | 338 | 20 | 212 | 103 | 52 | 49 | 40 | 35 | 25 | 23 | 24 |
| Finance Costs | - | 68 | (31) | 44 | 20 | 15 | 1 | -6 | -6 | -6 | -6 | -6 | -6 |
| Other Income | - | 107 | 14 | 165 | 51 | 15 | 15 | 15 | 15 | 15 | 19 | 22 | 22 |
| PBT | - | (61) | (706) | 33 | 247 | 104 | 54 | 50 | 40 | 35 | 25 | 23 | 24 |
| Tax | - | (154) | 243 | 42 | 267 | 104 | 92 | 50 | 40 | 35 | 25 | 23 | 24 |
| PAT | - | (33) | (479) | 31 | 243 | 104 | 44 | 50 | 40 | 35 | 25 | 23 | 24 |

Source: Company, DART

Costs break-up

| Rs Mn | FY19 | FY20 | FY21 | FY22E | FY23E | FY24E | FY25E | FY26E | FY27E | FY28E | FY29E | FY30E | FY31E |
|-----------------------------|--------------|--------------|--------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Employee Costs | | | | | | | | | | | | | |
| Employee Costs (Rs Mn) | 1,173 | 1,956 | 2,836 | 4,042 | 5,582 | 7,719 | 9,967 | 13,013 | 16,175 | 19,957 | 23,082 | 26,711 | 30,893 |
| Emp. Count (Nos) | - | 1,772 | 2,045 | 2,909 | 3,669 | 4,704 | 5,631 | 6,817 | 7,856 | 8,987 | 9,637 | 10,339 | 11,087 |
| Revenue/Emp (Rs Mn) | - | 10.0 | 11.9 | 13.1 | 14.4 | 15.9 | 17.5 | 19.2 | 21.1 | 23.3 | 25.6 | 28.1 | 31.0 |
| Salary/Emp (Rs Mn) | - | 1.1 | 1.4 | 1.4 | 1.5 | 1.6 | 1.7 | 1.9 | 2.0 | 2.1 | 2.3 | 2.5 | 2.7 |
| Chg YoY % | | | | | | | | | | | | | |
| Employee Costs (Rs Mn) | | 66.8 | 45.0 | 42.5 | 38.1 | 38.3 | 29.1 | 30.6 | 24.3 | 23.4 | 15.7 | 15.7 | 15.7 |
| Emp. Count (Nos) | | - | 15.4 | 42.3 | 26.1 | 28.2 | 19.7 | 21.1 | 15.2 | 14.4 | 7.2 | 7.3 | 7.2 |
| Revenue/Emp (Rs Mn) | | - | 19.7 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 |
| Salary/Emp (Rs Mn) | | - | 25.6 | - | 7.5 | 7.5 | 7.5 | 7.5 | 7.5 | 7.5 | 7.5 | 7.5 | 7.5 |
| Emp. Costs as % of Rev | 10.6 | 11.1 | 11.6 | 10.6 | 10.5 | 10.3 | 10.1 | 9.9 | 9.7 | 9.5 | 9.4 | 9.2 | 9.0 |
| Other Expenses | | | | | | | | | | | | | |
| Marketing (Rs Mn) | 1,428 | 2,022 | 1,695 | 4,399 | 5,299 | 6,726 | 8,611 | 11,139 | 13,705 | 16,723 | 19,109 | 21,824 | 24,884 |
| Fulfilment (Rs Mn) | 1,074 | 1,730 | 2,177 | 3,597 | 4,574 | 6,205 | 8,030 | 10,712 | 13,177 | 16,631 | 19,405 | 23,207 | 27,167 |
| Other opex (Rs Mn) | 631 | 1,015 | 1,208 | 2,139 | 2,746 | 3,166 | 3,595 | 4,046 | 4,554 | 5,078 | 5,615 | 6,198 | 6,841 |
| Total (Rs Mn) | 3,133 | 4,767 | 5,080 | 10,135 | 12,619 | 16,097 | 20,235 | 25,897 | 31,436 | 38,431 | 44,128 | 51,230 | 58,893 |
| Cost as % of Revenue | | | | | | | | | | | | | |
| Marketing | 12.9 | 11.4 | 6.9 | 11.5 | 10.0 | 9.0 | 8.8 | 8.5 | 8.3 | 8.0 | 7.8 | 7.5 | 7.3 |
| Fulfilment | 9.7 | 9.8 | 8.9 | 9.4 | 8.6 | 8.3 | 8.2 | 8.2 | 7.9 | 8.0 | 7.9 | 8.0 | 7.9 |
| Other opex | 5.7 | 5.7 | 5.0 | 5.6 | 5.2 | 4.2 | 3.7 | 3.1 | 2.7 | 2.4 | 2.3 | 2.1 | 2.0 |
| Total | 28.2 | 27.0 | 20.8 | 26.5 | 23.8 | 21.5 | 20.6 | 19.8 | 18.9 | 18.4 | 17.9 | 17.6 | 17.2 |
| Chg YoY % | | | | | | | | | | | | | |
| Marketing | | 41.6 | -16.2 | 159.6 | 20.5 | 26.9 | 28.0 | 29.4 | 23.0 | 22.0 | 14.3 | 14.2 | 14.0 |
| Fulfilment | | 61.0 | 25.8 | 65.2 | 27.2 | 35.7 | 29.4 | 33.4 | 23.0 | 26.2 | 16.7 | 19.6 | 17.1 |
| Other opex | | 60.9 | 19.1 | 77.0 | 28.4 | 15.3 | 13.5 | 12.6 | 12.6 | 11.5 | 10.6 | 10.4 | 10.4 |
| Total | | 52.1 | 6.6 | 99.5 | 24.5 | 27.6 | 25.7 | 28.0 | 21.4 | 22.3 | 14.8 | 16.1 | 15.0 |
| Mktg costs/Cust (Rs). | 408 | 374 | 273 | 519 | 486 | 494 | 527 | 564 | 593 | 614 | 620 | 624 | 626 |
| Fulfil. costs/order (Rs) | 94 | 96 | 112 | 109 | 106 | 109 | 112 | 117 | 120 | 126 | 129 | 136 | 139 |
| Fulfil. costs/BPC order | 98 | 102 | 127 | 131 | 133 | 144 | 156 | 173 | 185 | 203 | 216 | 234 | 250 |

Source: Company, DART

Valuation and Outlook

There's a lot to like about Nykaa as a business. Given the increasing opportunity size in a burgeoning industry and with new segments additions, the company is likely to register a healthy growth in the foreseeable future. Indian e-Commerce, while having a large market opportunity, has seen high cash burn & lack of profitability. The exception to this is Nykaa. We thus value Nykaa at 10x FY24 EV/Sales based on comparison with domestic and global internet & BPC companies. Initiate with Sell and TP of Rs 1,600.

The problem is current valuations build in no room for error. Neither in the future potential of the space itself nor for any execution hiccups that can impact growth even in the short-term. Long-term investors in our view can wait for the company to execute for couple of quarters before deciding to jump the bandwagon from hereon. Post the listing gain, we expect Nykaa to go through a price and time correction.

Exhibit 30: Valuation Snapshot

| Description | Rs Mn |
|----------------------------------|-----------------|
| FY24E Revenue | 74,732 |
| EV/Sales (x) | 10.0 |
| EV (Rs Mn) | 7,49,561 |
| Net debt/(cash) | (6,885) |
| Equity Value (Rs Mn) | 7,56,446 |
| No of O/s shares (Mn) | 473 |
| Target Price (Rs) (A+B+C) | 1,600 |
| CMP (Rs) | 2,246 |
| Upside/(Downside) % | (28.7) |

Source: Company, DART

Exhibit 31: Sensitivity of Nykaa's EV/Sales multiple

| Revenue (Rs Bn) | 38.2 | 53.0 | 74.7 |
|-----------------|-------|-------|-------|
| EV/Sales (x) | FY22 | FY23 | FY24 |
| 5 | 416 | 571 | 805 |
| 8 | 658 | 908 | 1,280 |
| 10 | 820 | 1,132 | 1,600 |
| 12 | 982 | 1,356 | 1,912 |
| 15 | 1,224 | 1,692 | 2,386 |
| 20 | 1,628 | 2,253 | 3,177 |

Source: Company, DART

What in our view is market implying for Nykaa's Valuations?

A Decade of hyper growth, No bumps from competition and to the Dot execution!

Exhibit 32: Abridged P&L summary FY21-31E

| Particulars (Rs Mn) | Rs Mn | | | | Chg YoY % | | 10 YR CAGR % | Common Size (%) | | | |
|---------------------|--------|--------|--------|----------|-----------|--------|--------------|-----------------|-------|-------|-------|
| | FY19 | FY20 | FY21 | FY31E | FY20 | FY21 | FY21-31E | FY19 | FY20 | FY21 | FY31E |
| Revenue | 11,114 | 17,675 | 24,409 | 3,43,229 | 59.0 | 38.1 | 30.3 | 100.0 | 100.0 | 100.0 | 100.0 |
| COGS | 6,603 | 10,142 | 14,878 | 1,93,172 | 53.6 | 46.7 | 29.2 | 59.4 | 57.4 | 61.0 | 56.3 |
| GP | 4,511 | 7,533 | 9,531 | 1,50,058 | 67.0 | 26.5 | 31.7 | 40.6 | 42.6 | 39.0 | 43.7 |
| Semi-variable costs | 4,306 | 6,723 | 7,916 | 89,786 | 56.1 | 17.8 | 27.5 | 38.7 | 38.0 | 32.4 | 26.2 |
| EBITDA | 205 | 811 | 1,614 | 60,272 | 295.2 | 99.2 | 43.6 | 1.8 | 4.6 | 6.6 | 17.6 |
| PAT | -245 | -163 | 619 | 44,498 | -33.4 | -479.1 | 53.3 | -2.2 | -0.9 | 2.5 | 13.0 |

Source: Company, DART

Exhibit 33: Implied Valuation snapshot

| Description | |
|----------------------------|-----------|
| FY31E PAT (Rs Mn) | 44,498 |
| Tgt exit multiple (x) | 50 |
| Equity Value FY31E (Rs Mn) | 22,24,902 |
| WACC (%) | 12% |
| Discounted factor to FY24E | 2.21 |
| Equity Value FY24E (Rs Mn) | 10,06,433 |
| O/s sh (Mn) | 473 |
| TP (Rs/Sh) | 2,129 |
| Rs/\$ | 75.0 |
| Equity Value FY24E (\$ Mn) | 13,419 |

Source: Company, DART

Exhibit 34: Sensitivity analysis to WACC and target PE to FY31E PAT (Rs 44.5bn)

| WACC | Target PE multiple in FY31 | | |
|------|----------------------------|-------|-------|
| | 30 | 40 | 50 |
| 8% | 1,648 | 2,197 | 2,747 |
| 10% | 1,449 | 1,933 | 2,416 |
| 12% | 1,278 | 1,704 | 2,129 |
| 14% | 1,129 | 1,505 | 1,881 |

Source: Company, DART

Reverse DCF Valuation Summary

| (Rs mn) | FY24 | FY25 | FY26 | FY27 | FY28 | FY29 | FY30 | FY31 |
|---------------|--------------|--------------|--------------|---------------|---------------|---------------|---------------|---------------|
| EBIT | 7,766 | 11,810 | 17,604 | 4,562 | 33,124 | 41,348 | 50,916 | 63,087 |
| Tax | (1,941) | (2,953) | (4,401) | (6,141) | (8,281) | (10,337) | (12,729) | (15,772) |
| Depreciation | 1,143 | 1,295 | 1,440 | 1,570 | 1,699 | 1,839 | 1,991 | 2,155 |
| W Cap changes | (2,920) | (3,743) | (4,650) | (4,790) | (6,053) | (4,886) | (5,713) | (6,654) |
| Capex | (1,485) | (1,193) | (1,018) | (805) | (1,054) | (755) | (646) | (213) |
| FCFF | 2,562 | 5,217 | 8,975 | 14,396 | 19,435 | 27,209 | 33,819 | 42,603 |

Source: Company, DART

Valuation snapshot

| Valuation date | 01-Apr-24 |
|------------------------|-----------------|
| PV of CF | 4,61,043 |
| TV | 3,73,753 |
| Enterprise value | 8,34,795 |
| Net debt/(Cash) | (6,885) |
| Equity value | 8,41,681 |
| O/s shares | 473 |
| Value per share | 1,781 |

Note: Key assumptions for (1) FCFF growth beyond FY31 is @ 20% CAGR over FY31-26, FY37-41 @ 15%, and FY42-46 @ 10%, and (2) FY46 onwards terminal growth of 5% (3) WACC @ 12%

Sensitivity analysis to WACC and Terminal growth

| WACC | Terminal Growth % | | |
|------|-------------------|-------|-------|
| | 4% | 5% | 6% |
| 8% | 4,726 | 5,753 | 7,807 |
| 9% | 3,453 | 3,956 | 4,794 |
| 10% | 2,638 | 2,912 | 3,324 |
| 11% | 2,081 | 2,242 | 2,466 |
| 12% | 1,682 | 1,781 | 1,913 |
| 13% | 1,386 | 1,449 | 1,531 |

Source: Company, DART

Internet / Peer Valuations (Domestic Companies)

| Company | O/s sh (Mn) | Price (Rs) | Mcap (Rs bn) | Sales (Rs bn) | | | EBITDA (Rs bn) | | | Mcap/Sales (x) | | | Mcap/EBITDA (x) | | |
|-----------|-------------|------------|--------------|---------------|-------|-------|----------------|-------|-------|----------------|-------|-------|-----------------|-------|-------|
| | | | | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E |
| Dmart | 648 | 4,880 | 3,161 | 323 | 460 | 576 | 29 | 45 | 59 | 9.8 | 6.9 | 5.5 | 107.7 | 70.0 | 53.7 |
| Zomato | 7,845 | 156 | 1,224 | 40 | 58 | 84 | (10) | (7) | (1) | 30.5 | 21.0 | 14.6 | NA | NA | NA |
| Nykaa | 473 | 2,246 | 1,062 | 38 | 53 | 75 | 2 | 5 | 8 | 27.8 | 20.0 | 14.2 | 532.7 | 233.7 | 127.4 |
| InfoEdge | 129 | 5,965 | 768 | 14 | 18 | 21 | 5 | 6 | 8 | 53.3 | 43.8 | 37.1 | 168.2 | 127.7 | 101.8 |
| IndiaMart | 30 | 7,309 | 222 | 8 | 9 | 11 | 4 | 4 | 5 | 29.1 | 24.0 | 20.3 | 62.3 | 53.6 | 46.0 |
| Affle | 133 | 1,153 | 154 | 9 | 12 | 16 | 2 | 3 | 4 | 18.1 | 13.2 | 9.5 | 81.7 | 55.5 | 39.9 |
| Nazaara | 30 | 2,262 | 69 | 6 | 9 | 12 | 1 | 1 | 2 | 11.0 | 7.6 | 5.6 | 73.0 | 48.6 | 31.5 |
| Just Dial | 62 | 723 | 45 | 7 | 8 | 9 | 1 | 2 | 2 | 6.6 | 5.4 | 4.9 | 65.5 | 24.5 | 23.6 |

Source: Bloomberg, DART

Peer valuations (International Companies)

| | Mcap (USD bn) | Sales (USD Bn) | | | EBITDA (USD Bn) | | | Mcap/Sales (x) | | | Mcap/EBITDA (x) | | |
|--------------|---------------|----------------|-------|-------|-----------------|-------|-------|----------------|-------|-------|-----------------|-------|-------|
| | | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E |
| L'Oreal | 267 | 34.5 | 36.9 | 38.7 | 8.5 | 9.1 | 9.7 | 7.7 | 7.2 | 6.9 | 31.3 | 29.2 | 27.4 |
| LVMH | 405 | 68.9 | 74.6 | 78.8 | 22.3 | 24.7 | 24.9 | 5.9 | 5.4 | 5.1 | 18.2 | 16.4 | 16.2 |
| Estee Lauder | 124 | 18.8 | 20.5 | 22.1 | 4.4 | 5.0 | 5.5 | 6.6 | 6.1 | 5.6 | 28.0 | 25.0 | 22.7 |
| Shishiedo | 26 | 9.2 | 9.8 | 10.5 | 1.4 | 1.8 | 2.0 | 2.8 | 2.6 | 2.4 | 17.7 | 14.3 | 13.1 |
| Beiersdorf | 26 | 9.1 | 9.5 | 9.9 | 1.5 | 1.6 | 1.7 | 2.9 | 2.7 | 2.6 | 17.4 | 16.1 | 15.0 |
| AmorePacific | 9 | 4.5 | 5.1 | 5.8 | 0.8 | 0.8 | 0.9 | 1.9 | 1.7 | 1.5 | 11.4 | 10.4 | 9.3 |
| Amazon | 1,812 | 555 | 649 | 738 | 85 | 108 | 131 | 3.3 | 2.8 | 2.5 | 21.3 | 16.8 | 13.8 |
| Alphabet | 1,948 | 245 | 284 | 322 | 119 | 136 | 158 | 8.0 | 6.9 | 6.1 | 16.3 | 14.4 | 12.4 |
| Netflix | 292 | 34 | 39 | 44 | 8 | 11 | 13 | 8.6 | 7.5 | 6.6 | 34.8 | 27.6 | 22.5 |
| Facebook | 949 | 140 | 166 | 189 | 66 | 80 | 95 | 6.8 | 5.7 | 5.0 | 14.3 | 11.9 | 9.9 |

Source: Bloomberg, DART

Key Risks

Retaining Customers and Maintaining Average Order Values

Nykaa must generate a certain average order value and retain existing customers to maintain its margins and overcome its basic costs. The company has designed its platform in a manner in which customers can discover new trends and products. It has also on-boarded influencers and mainstream celebrities to grow its reach. In order to maintain high-order values, it must also target the right audience. **Any shift in its customer demographic can impact it negatively.**

Discounting and Competition

Large opportunity size, lower barriers to entry, availability of capital have attracted players across categories in the online space and growth in most cases is at the cost of profitability. Lastly with valuation parameters linked to number of MAUs/DAUs, transacting customers etc most companies have been resorting to aggressive marketing and discounting.

Discount continues to remain the main mantra when it comes to online shopping. This is because the market potential is huge and multiple players are ramping up their businesses. And also, because in India, a large quantum of households is value-conscious. They are price sensitive and prioritize discounts over other factors. A few prioritize shopping experience and prefer purchasing from a wider product assortment in one place and lower delivery time.

Intense Competition

The sector faces intense competition with competitors in general e-commerce and other niche companies focusing on the same market as Nykaa. The competitors include a number of online marketplaces, retailers with physical stores, and brands that take a direct-to-consumer approach, effectively removing third-party platforms like Nykaa from the distribution and sales process. The Internet and mobile networks provide new, rapidly evolving and competitive channels for the sale of all types of goods and services. Consumers who purchase goods and services through Nykaa also have other alternatives, and sellers have other channels to reach consumers.

A list of beauty and wellness brands that have recently raised capital from investors. The list includes Purplle, MyGlamm, Sugar Cosmetics, Mamaearth, Juicy Chemistry, Plum, Bombay Shaving Company, The Man Company and new-age Ayurveda based beauty companies like Forest Essentials and Kama Ayurveda among others. That said, while many of this direct-to-consumer companies with digital first as their strategy use aggregators like Nykaa, Amazon, Myntra etc for grabbing customers, in the near-term they are likely to complement Nykaa's growth strategy. But as they achieve scale, they may compel Nykaa to either reduce its commission or prefer going D2C which may be a risk.

We highlight below the key metrics of the key competitors of Nykaa

Purplle - Nykaa's competitor raised \$135mn @ \$630mn valuation

- Online beauty products platform Purplle has raised \$135mn at valuation of \$630mn. Funding is led by Kedaara and Premji invests along with existing investors Sequoia and Blume Ventures. Valuations have inched up 4x from last round six months ago when it raised \$45mn from Sequoia and others.

Competition and discounting in our view is the biggest challenge for Nykaa. While it has been able to grow healthily and profitably, sustenance of the profitable growth trajectory in light of impending competition could be an acid test.

Nykaa vs. Purplle

- As per media reports, Purplle is growing at ~80% YoY. We believe this is due to lower base. Recently Purplle does monthly GMV of ~Rs 1bn. Nykaa did a GMV of Rs 16.2bn in Q1FY22. In Q3FY21 Nykaa did a GMV of Rs 13.7bn and assuming 40-50% growth YoY, recent run-rate should be ~Rs 19-21bn for Q3FY22E or Rs 6.5-7bn per month i.e. 6.5-7x of Purplle.
- Purplle (standalone) in FY19/20 did revenues of Rs 100/87cr and EBITDA loss of Rs -4.5/-29.4cr respectively. These is against Nykaa's (consolidated) FY19/20 revenues of Rs 1,111/1,765cr and EBITDA of Rs 21/81cr. **A remarkable difference between Purplle and Nykaa.**

About Purplle

- Similar to Nykaa, Purplle too started its operations in 2012 and opened first physical store in Phoenix City, Kurla in 2017. Like Nykaa, Purplle too is co-founded by an ex-investment banker, Manish Taneja who earlier was with Fidelity, Avendus, Lehman Bros etc
- Purplle's mission is of democratising beauty across the heartlands of India, with affordable and accessible products.

Good Glamm recently raised \$140mn at a valuation of \$1bn

- The Good Glamm Group is a culmination of three brands MyGlamm, digital media/e-commerce platform, POPxo and online parenting startup BabyChakra. The three companies and their founders — Darpan Sanghvi (MyGlamm), Priyanka Gill (POPxo) and Naiyya Saggi (BabyChakra) — have created this entity to set up a house of brands and further enhance each other's presence in the beauty and personal care space.
- In Sep'21, Good Glamm had raised ~\$100mn as part of Series C funding at valuation of ~\$300mn before the current Series D funding of \$140mn at ~\$1.2bn.
- With a strong portfolio of D2C brands and proprietary content assets, the group is well positioned to scale rapidly and create a large digital-first business in the BPC space as per their investors.

Mamaearth raised \$50 million led by Sofina in July, valuing it at \$730mn

Tata Digital is looking to launch an online store in competition to Nykaa as per media. Tata Digital's online store for cosmetics and personal care products will be separate from Tata Cliq and existing ecommerce verticals such as Westside.

Exhibit 35: Key Players – Traditions vs. New Age Companies



Source: DART, Inc42

Social Media Flaks

Aggregators and D2C companies’ overdependence on social media for brand building and marketing means any negative feedback on those platforms can affect their sales and impact their credibility. For eg: adverse claims were made against us relating to our workplace culture through an anonymous Instagram account. Such claims, even when untrue, could damage reputation, business, and results of operations.

Data protection

Nykaa’s online platform manages and stores personal information of its customers, such as phone number, e-mail ID, address, etc which it uses for marketing and promotion of products and for customer retention. Such platforms are susceptible to security breaches and cyber-attacks which pose a risks.

Industry Overview

India Retail – A large addressable opportunity

India will be a huge Rs 91 trillion retail opportunity by CY25

As per RedSeer, India retail market size was estimated at ~Rs 63 trillion in CY19 growing at 11% CAGR over the trailing three years. India's retail sector was impacted by the first wave of COVID-19 thus declining 13% to ~Rs 55 trillion in CY20. Both the supply and demand of most consumer goods were adversely affected. As the pandemic eases out, the retail market is expected to bounce back in the coming years to reach ~Rs 91 trillion at 11% CAGR over CY20-25 (6.3% over CY19-25).

The COVID-19 waves have turned out as a boon for the internet economy in India

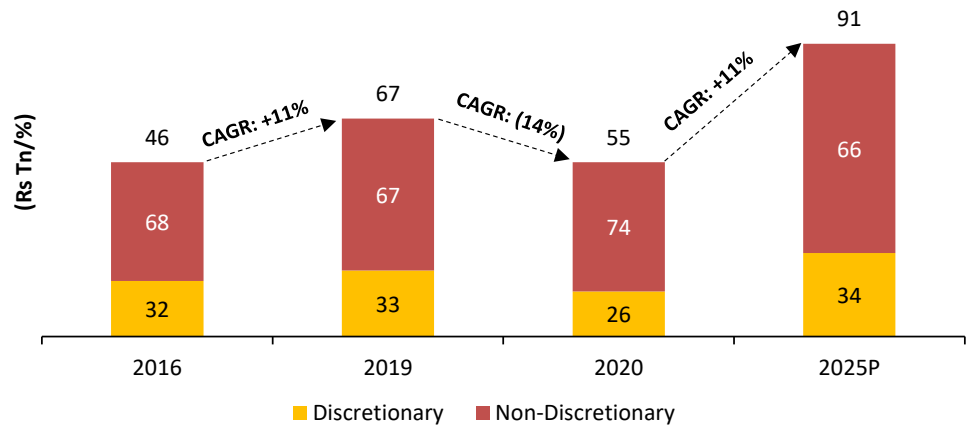
The discretionary (excluding the essential categories like food and grocery and pharma) portion of the retail market was sized at ~Rs 21 trillion in CY19. The discretionary portion saw a sharper decline of 32% in CY20, led by reduction in the spending on non-essential products. Discretionary is set to make a strong recovery and register healthy growth to reach ~Rs 31 trillion at 17% CAGR over CY20-25 (6.9% over CY19-25).

Fashion and BPC combined at ~Rs 4.9tn accounted for ~35% of the discretionary retail in India in 2020; a key target segment of Nykaa

The growth in retail industry is enabled by the rising middle class, soaring income levels, increasing demand from Tier 3-4 cities and rural markets, rise in youth spending, improvement in infrastructure, shift from unorganized to organized and the entry of new Indian and global brands across the product categories.

E-commerce penetration in India grew 1.6x from 3% in CY19 to ~5% in CY20, with a large headroom ahead as indicated by the higher penetration in the developed markets (e-commerce penetration in the United States and China in 2020 was 12-17% and 25-30%, respectively).

Exhibit 36: Overall Retail Industry in India

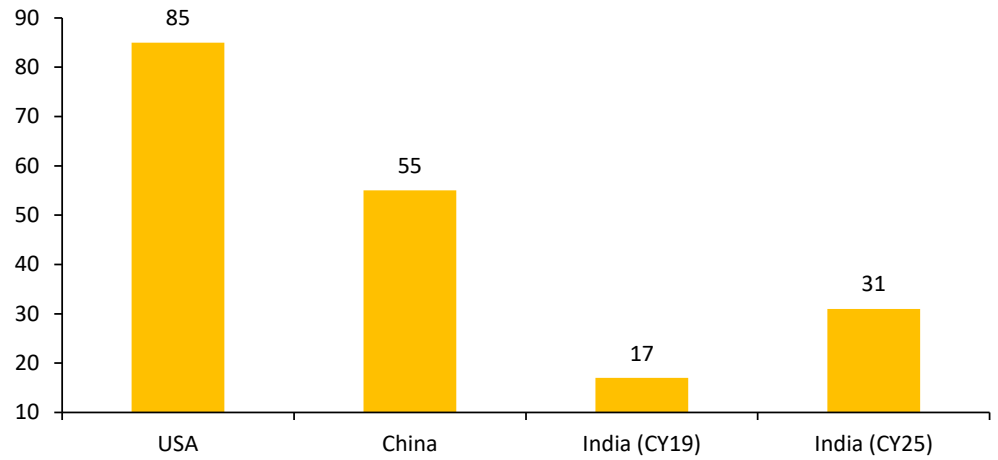


Source: Company, RedSeer Research, DART

Robust growth in organized retail led by increasing online retail penetration presents a massive opportunity for brands in India

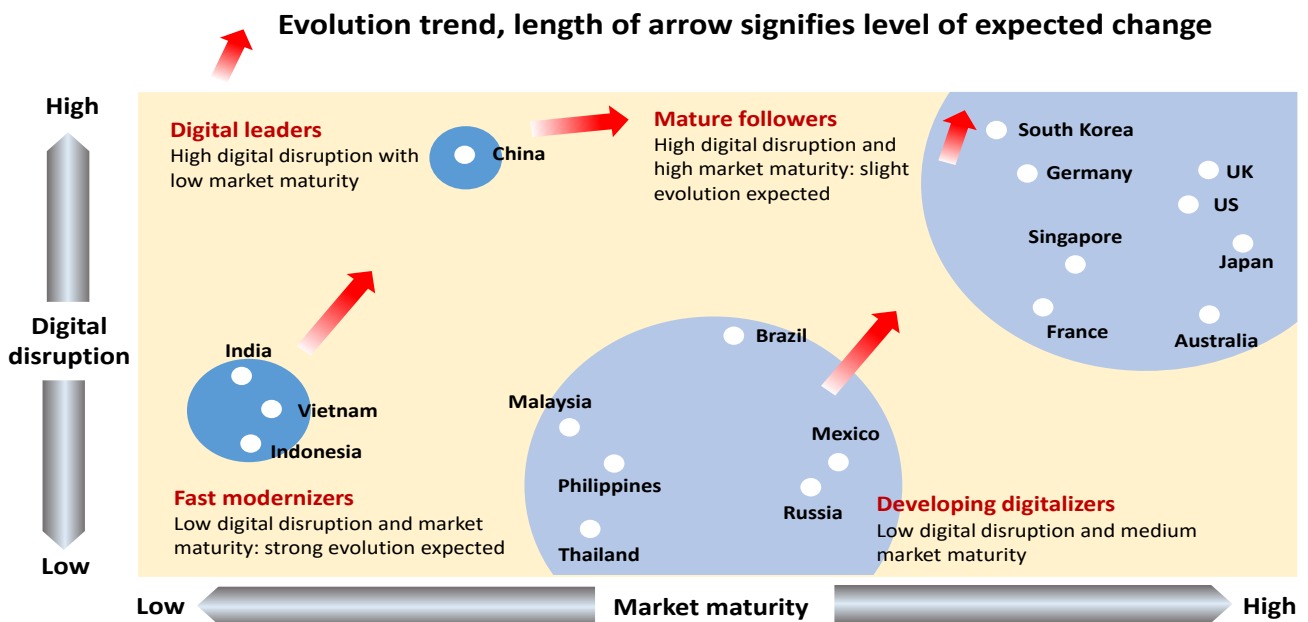
High rentals and low number of malls and shopping complex are constraints to organized retail penetration. Thus, India e-commerce is likely to mimic China trend of high e-tail penetration due to sluggish growth in retail mall space (0.8 malls per million people in India vs 36 in USA) and high rental costs (20-25% of sales in India and China vs. 10-15% in USA). Indian Retail market is large and unorganized; e-commerce is driving the penetration of organized retail.

Exhibit 37: Organized retail penetration (% of overall retail)



Source: Deloitte and the Retailers Association of India report "Unravelling the Indian Consumer February 2019", Avendus estimates, DART

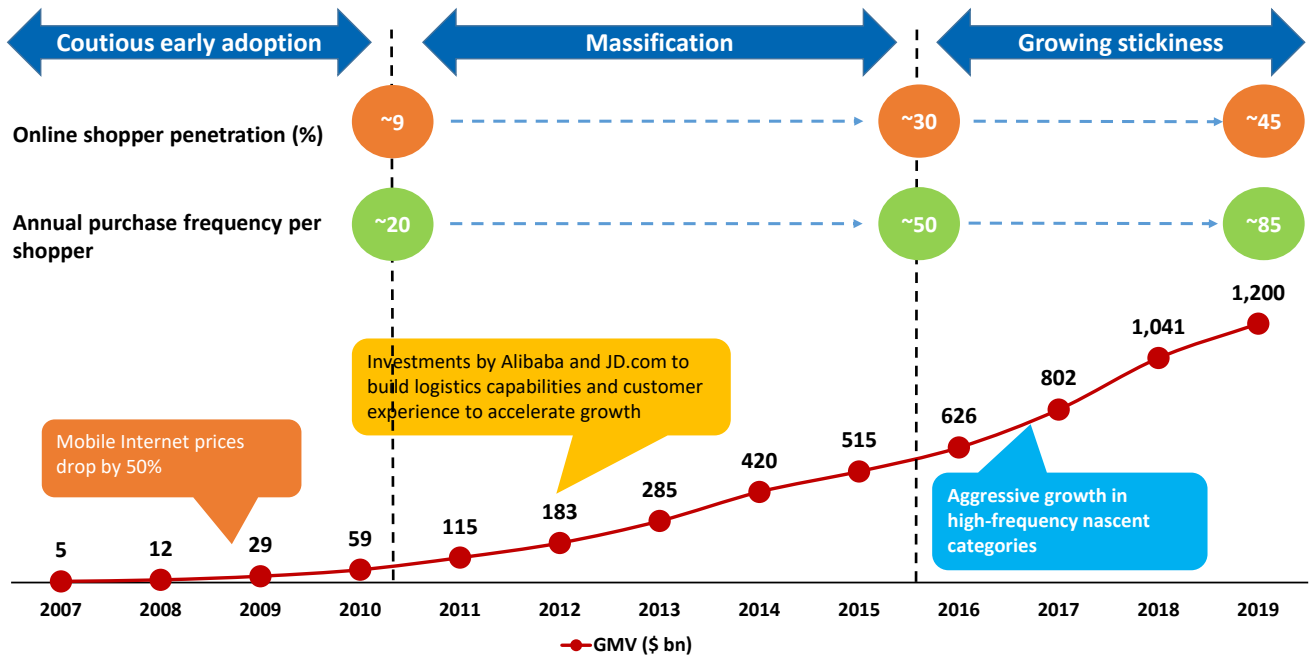
Exhibit 38: Asia-pacific countries can be divided into four retail categories, each with its own trajectory



Source: Euromonitor, Forester, Planet Retail, Global Data, EIU, Demogrpahia, OMDIA (Ovum), DART

Exhibit 39: China has been an example of swift transition to online

Increase mobile and internet penetration coupled with improved logistics and payment infrastructure drove Chinese e-retail growth



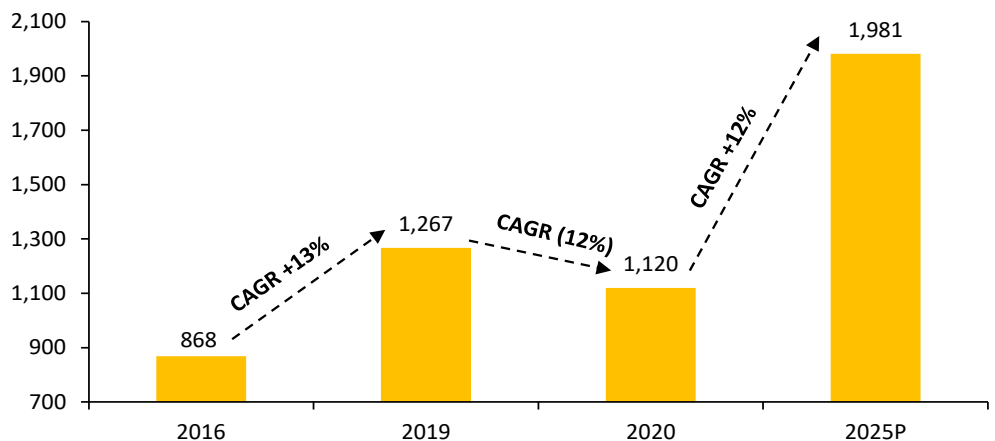
Source: Euromonitor, Forester, Planet Retail, Global Data, EIU, Demograpia, OMDIA (Ovum), DART

India BPC – on strong foundation for makeover

The Beauty and Personal Care (BPC) market in India was sized at Rs 1,267bn (\$17 bn) in CY19, growing at a CAGR of 13% in the last 3 years. Though the market declined by 12% to Rs 1,120bn (\$15bn) in CY20 as a result of reduced spending during the first COVID-19 wave, it is projected to grow to Rs 1,981bn (\$ 26bn) by CY25 at 12% CAGR (7.7% CAGR from pre-COVID).

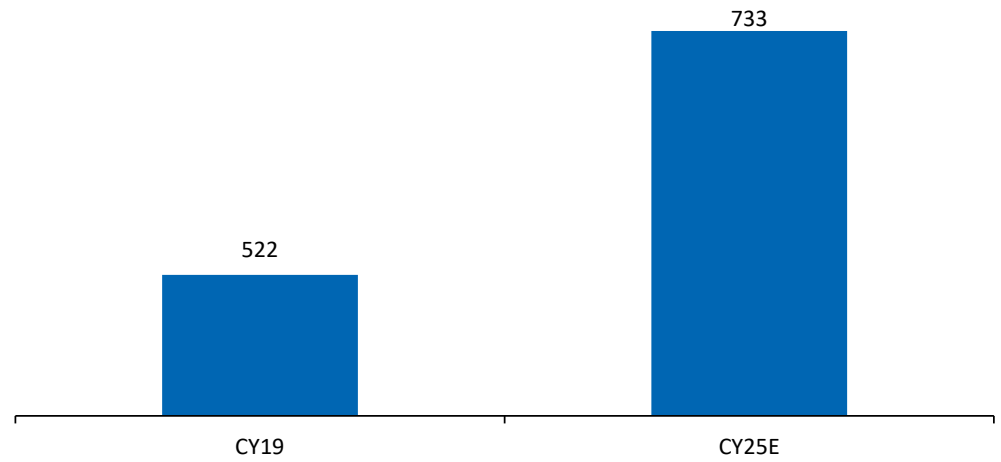
Similar to the overall retail space, India BPC is heavily dominated by the unorganized channel, which primarily includes local grocery shops and departmental stores. With Indian consumers becoming more evolved in their BPC shopping habits, share of unorganized BPC market had reduced to 72% in CY20 from 77% in CY16.

Exhibit 40: India Beauty and Personal Care Market Size and Growth (Rs bn)



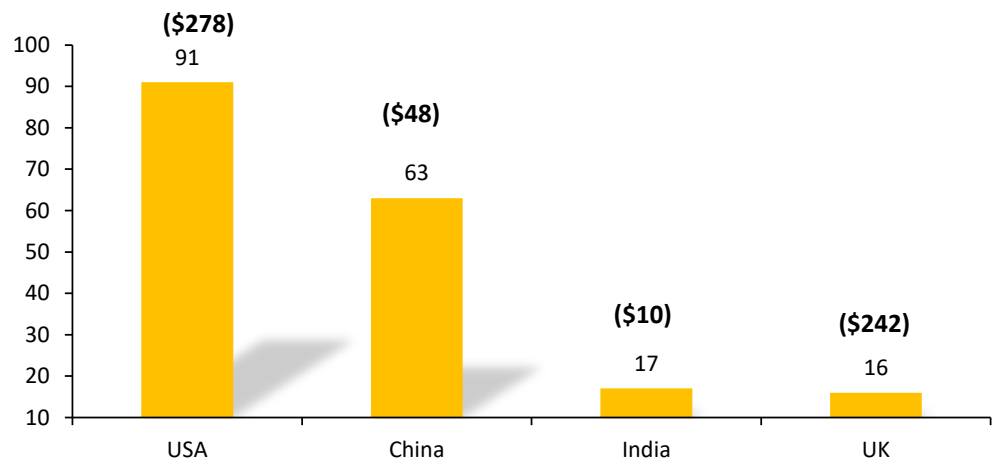
Source: Company, DART

Exhibit 41: BPC is a \$500bn+ market globally, USA and China being the largest



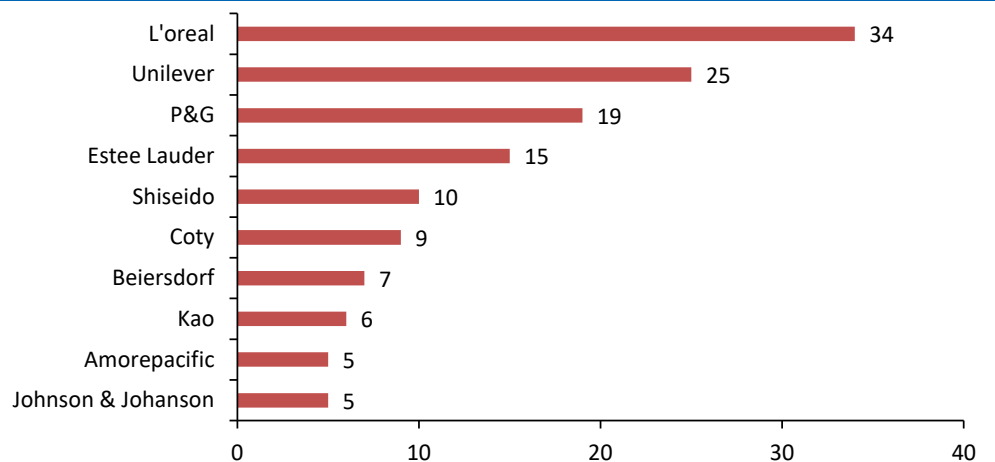
Source: Company, DART

Exhibit 42: BPC market size (USD bn) and per capita spend



Source: Company, DART

Exhibit 43: Global revenue (USD bn) from beauty segments of leading cos



Source: Avendus Estimates, DART

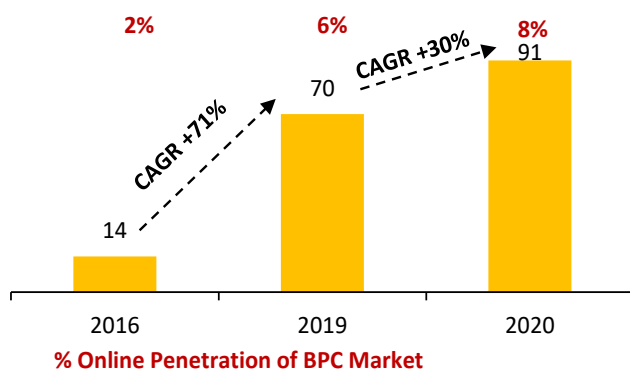
Online BPC Market in India has grown at promising 60% CAGR in the last 4 years, penetrating 8% of the India BPC Market in 2020.

India Online BPC market – tip of the iceberg

Online channel accounted for a modest 2% of the India BPC market in 2016. Following this, the sector grew at a strong 71% CAGR over CY16-19 to penetrate 6% of the BPC market at ~Rs 70bn. **While the overall BPC market declined 12%, Online grew at 30% to reach Rs 91bn between CY19 and CY20.**

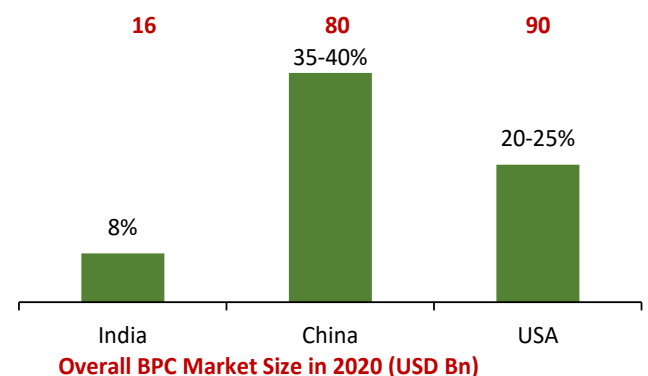
Online BPC retail platforms are effectively resolving challenges faced by both consumers and brands with the help of superior application of technology, efficient supply chain and quality control, access to a wider selection of products and brands including niche luxury brands, original content and advice from experts, door-step deliveries and wider geographic reach.

Exhibit 44: Online BPC Size (Rs bn) and Growth (%)



Source: Company, DART

Exhibit 45: Online BPC Penetration vs. Global



Source: Company, DART

Growing online shopping penetration in Tier 2+ cities, consistent investment for growth of the sector, rising affinity for branded products that are available online with a wide assortment, increasing need for convenient shopping experience, rising adoption of e-commerce by Generation Zs and Millennials who are the key growth enablers in the BPC category and higher consumer trust on products bought online, are the key drivers of growth in the market. There is a large headroom ahead for penetration led growth in India.

Segments in the BPC market

BPC market in India can be categorized in two broader categories as under:

Generic categories

- Generics category of BPC includes products across oral care, hair care and bath and shower, addressing basic consumer needs.
- Generic category will grow slowly & steadily. Brands with functional benefits & value-for-money products will dominate the category

Specialized categories

- Specialized category includes products addressing latent consumer needs comprising of discretionary and evolved sub-categories like make-up, skin care, fragrances, men’s grooming, sexual wellness and women hygiene.
- Specialized category of the BPC market has been growing significantly faster than the generic category.

Share of specialized category of the BPC market has been on a rise

- Entry of international brands with aspirational values that demonstrate high price propensity is also expected to drive growth
- It is expected to outpace the market growth in coming years, owing to higher disposable income, social media influence, increased adoption of products, latent demand fulfilment and high acceptance of beauty & cosmetic variants being offered.

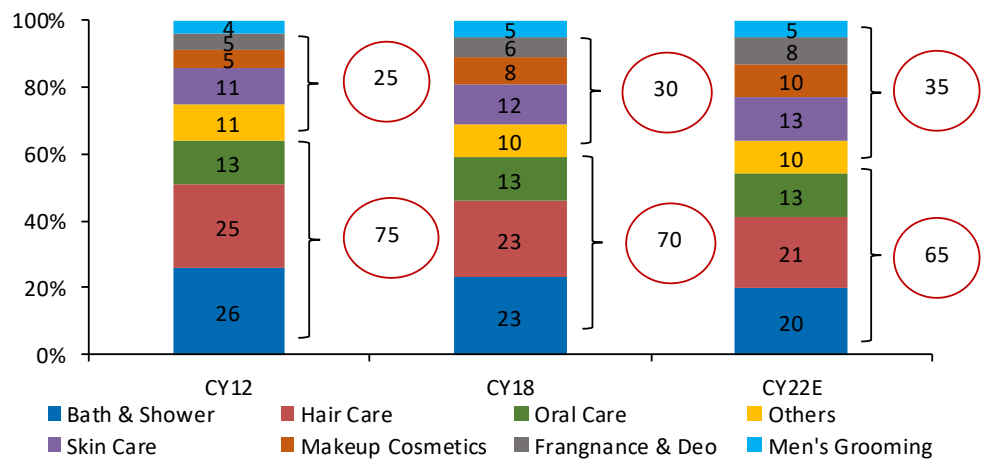
Emergence of a sizable Prestige BPC Segment

- Prestige BPC segment refers to the BPC products sold by brands positioning themselves in the non-mass category.

Exhibit 46: Category-wise split of BPC market

High indulgence categories like Cosmetics & Fragrance are driving the growth of the BPC market

Make-up, Skin care and Hair care constitute ~70% of Nykaa's BPC revenue

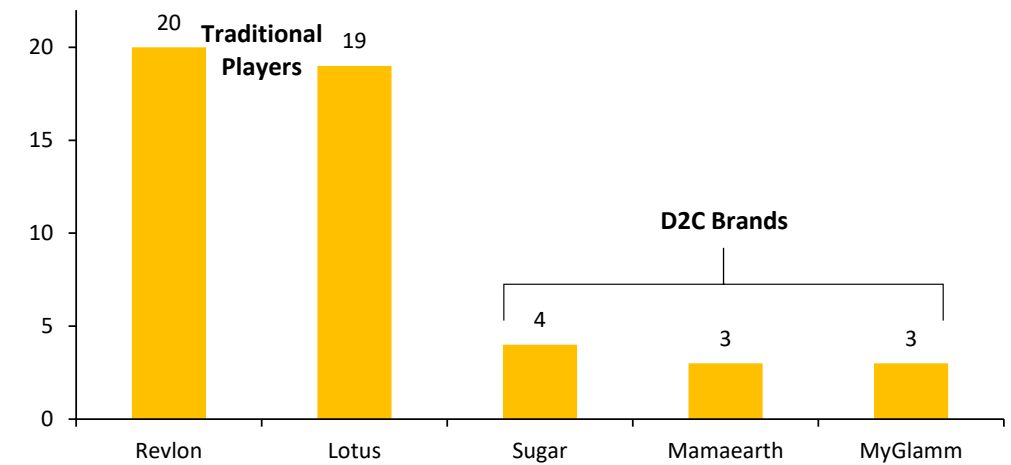


Source: Redseer, DART

Nykaa – a key enabler to increasing phenomenon of D2C players

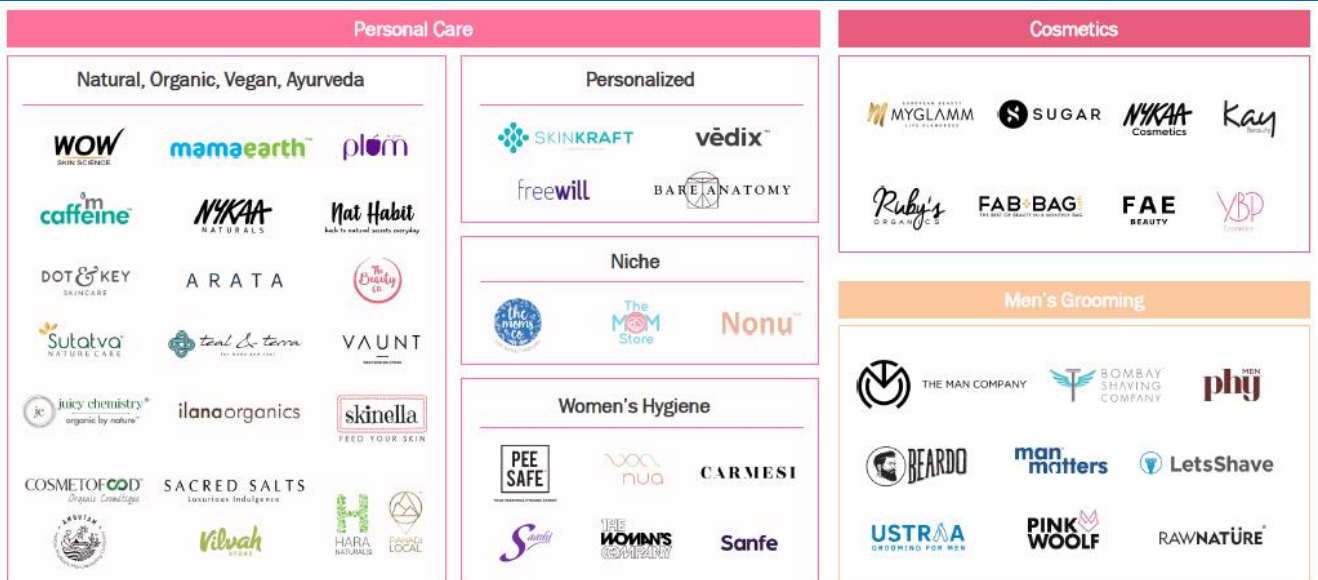
- There are visible green shoots of increasing brand adoption. Untapped white space offers significant head room for brand creations. Direct-to-consumer (D2C) brands have been quick to capitalize on the product and price white space, witnessing rapid acceleration of scale.
- **D2C brands refer to businesses that have** (i) majority of their revenue or customer acquisition from direct to consumer online channels; OR (ii) started with an online first distribution before going omni-channel.
- Vertical e-commerce players like Nykaa acts as an enabler to reach-out the consumers for the leading international and domestic D2C brands. While own platform can give access to customer data and insights, distribution through Nykaa gives sales velocity, reduces time to market and customer acquisition costs.

Exhibit 47: No of years to achieve Rs 100cr revenues for the brands



Source: Avendus Estimates, DART

Exhibit 48: Indian D2C landscape has more than 80 brands



Source: Avendus Estimates, DART; The list is illustrative and not exhaustive

Content – a key pull factor especially for GenZ and Millennials

Rise in Popularity of Online Content-led Discovery

- Online content has become the primary lever of BPC purchase decisions, by effectively facilitating discovery and understanding of BPC products and brands. This is providing a significant push to the market as the **Generation Z (in the 10-24 years age group) and Millennial (in the 25-39 years age group) consumers**, the most active BPC buyers, are also the active consumers of online content on social media platforms.
- The live e-commerce market, **comprising of influencers**, merchants and key opinion leaders selling directly to consumers on the platform via video live streaming, is likely to become an important enabler of discovery in the BPC category.

Influencers and Live Commerce play a significant role in China

The best lipstick salesman in China is a man. Austin Li or Li Jiaqi, also known as 'Lipstick Brother' or 'King of Lipsticks', is perhaps the biggest male beauty influencer in China. In the recently-held Annual Shopping Festival (Oct'21) conducted by Alibaba group, 'Lipstick Brother' sold \$1.9 billion worth of goods in one day.

Live commerce influencers hold so much sway in China that Viya, a leading influencer there, sold \$6 Bn worth of goods through her account in 2020. However, it is yet to be implemented worldwide.

Online learning is only one part of the 'live' experience in the beauty space. The bigger slice of the pie is live commerce, and Chinese platforms like Alibaba's Taobao, Douyin (TikTok) and WeChat have already used this format successfully to sell global beauty brands like L'oreal, Clinique and Estée Lauder. In fact, it has become an integral part of their brand marketing strategies at home.

Although the Chinese ecosystem allows users to buy goods from their favourite celebs' live shows seamlessly (with minimum clicks and through a single app), the rest of the world (including the USA, where digital commerce formats have matured most) has not managed this feat yet.

A similar format is used in India for social commerce transactions, and resellers often go live via their business accounts (similar to social media accounts) to drive sales. But this usually involves multiple touchpoints where users view, book and pay for products on different platforms. This model may change soon, though, as Indian startups such as Woovly, Trell, 335bazaar and Hypd are exploring their way around live commerce offerings. Of course, the endgame is all about sales conversion; at least, that is what the brands focus upon. So, most of these platforms are looking at cross-selling and covering specific segments, including beauty, personal care and fashion, as Indian consumers are more comfortable e-shopping in these segments.

While Live Commerce is in infancy in India, role of influencers is significant. Nykaa effectively utilizes the influencers for customer acquisition and retention. To build engagement on its platform, Nykaa works with over 3,055 (as of Aug'21) influencers including Generation Z trend setters, mommy bloggers, beauty, fashion and lifestyle bloggers, makeup artists and celebrities, to create content on its platform.

KTAs from Google-WPP-Kantar 'Connected Beauty Report'

We summarize the role of Digital / Online BPC from some of the important key takeaways from the Google-WPP-Kantar connected beauty reports which we believe are vital and positive from the perspective of Nykaa are:

- Beauty consumers are highly engaged with content online with 93% engaging more than once a month, 50% weekly and 33% Daily
- 9 out of 10 consumer journeys have a digital touchpoint
- 2/3rd of the consumers are not loyal to one brand
- Online has moved beyond its traditional role as a research medium to being an important purchase platform.

To summarize, a large population of connected consumers and a dynamic content & creator ecosystem has created an unprecedented opportunity for brands. Nykaa as an aggregator/distributor of brands on the burgeoning digital distribution channel stands to benefit.

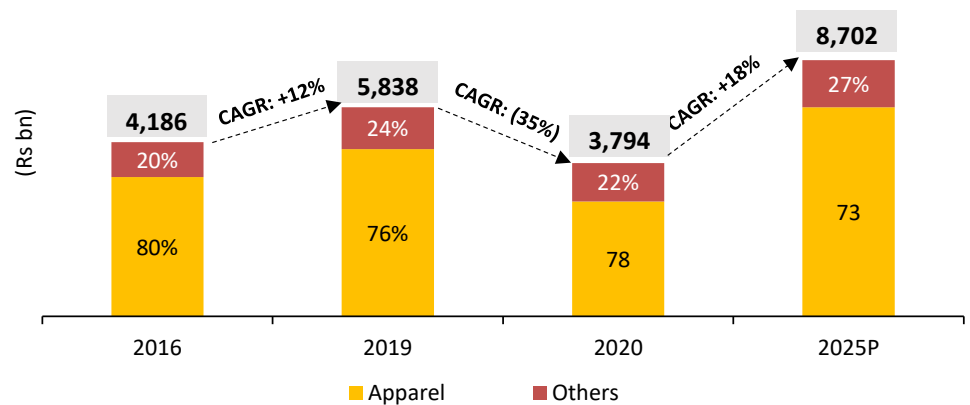
Fashion – ~3.5x the size of BPC

The size of Fashion Market in India was Rs 4,186 billion in CY16, constituting more than 9% of the retail market. Apparel accounted for ~80% of this market and footwear and accessories combined covered the remaining 20%. The Fashion Market grew at a 12% CAGR over CY16-19 to reach Rs 5,838 bn.

It declined by 35% in 2020 during the first COVID-19 wave, driven by the reduction in discretionary spending and disruption in supply chain due to the lockdown. The Fashion Market in India is projected to recover strongly and grow at 18% CAGR over the next five years to reach Rs 8,702bn by CY25. Apparel are projected to continue driving ~73% of the market in 2025.

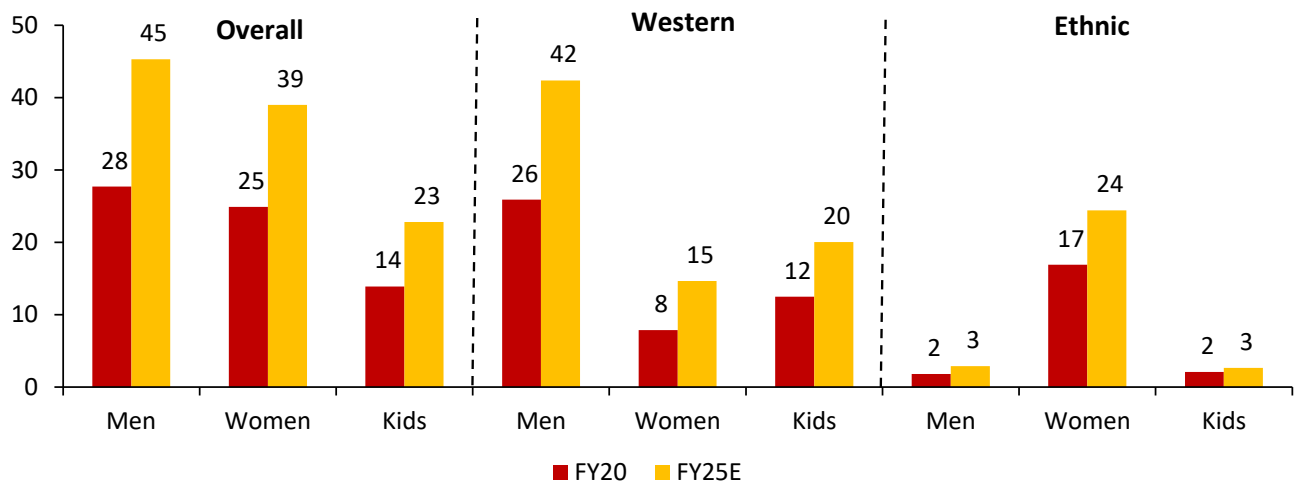
The Fashion Market in India is currently dominated by the unorganized channel, majorly comprising of local apparel, footwear and accessories stores. Hence, the current market is underserved as most traditional retailers try to serve broad demographic and are slow in reacting to changing trends. The organized segment has grown at a much faster pace as its share jumped from 29% to 37% over CY16-20.

Exhibit 49: India Fashion Market Size and Growth



Source: RHP, RedSeer, DART

Exhibit 50: Apparel market size (USD bn) broken into Men, Women and Kids



Source: DART, Wazir Analysis

India Vs. Global Apparel Market

Global apparel industry has grown to become an estimated market of over USD 1.9 trillion, which reflects 2% of the global GDP of USD 84.9 trillion. EU and USA dominate the global apparel market with a combined share of ~41%, while they account for only 11% of the world population. On the other hand, highly populated Asian countries, such as China, India and Japan, home to ~38% of the world population, collectively account for a market of 21%.

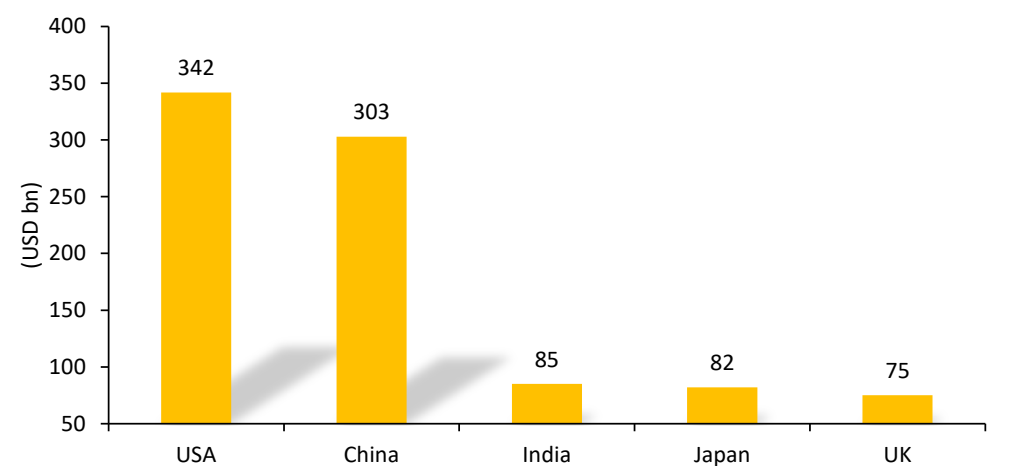
Exhibit 51: Global Apparel Market*

| Particulars | Size (USD Bn) | | Mix % | | CAGR (%) | Key Players |
|---------------|---------------|--------------|--------------|--------------|------------|--|
| | 2018 | 2025E | 2018 | 2025E | | |
| EU-28 | 427 | 458 | 22.5 | 17.4 | 1.0 | Zara, Gucci, Louis Vuitton, H&M |
| United States | 348 | 400 | 18.3 | 15.2 | 2.0 | Gap, Ralph Lauren, Calvin Klein Nike, Adidas, |
| China | 231 | 450 | 12.2 | 17.1 | 10.0 | Lane Crawford, Joyce, Attos, Sammy, Dong Liang |
| Japan | 100 | 107 | 5.3 | 4.1 | 1.0 | Fast Retailing, Uniqlo |
| India | 74 | 164 | 3.9 | 6.2 | 12.0 | |
| Brazil | 66 | 93 | 3.5 | 3.5 | 5.0 | |
| Russia | 39 | 54 | 2.1 | 2.1 | 4.8 | |
| Canada | 32 | 36 | 1.7 | 1.4 | 1.7 | |
| RoW | 580 | 872 | 30.6 | 33.1 | 6.0 | |
| | 1,897 | 2,634 | 100.0 | 100.0 | 4.8 | |

Source: DART, Wazir Analysis, FICCI * Includes Home and technical textiles

Among the top ten markets of apparel, Asian giants China and India are expected to deliver the most promising growth rates of 10% and 12%. In China and other parts of the region, retail is leapfrogging development stages that the US and Europe once toiled through.

Exhibit 52: India is 3rd largest fashion market in the world



Source: DART, MOSPI; Note: Fashion comprises of apparel, footwear, accessories, eyewear etc

Key factors driving the growth for Indian fashion spending

- Fashion is the highest discretionary spend category
- Higher disposable incomes and the need to look and feel good has helped fashion market grow at healthy rate
- COVID-19 has accelerated the shift to digital channels
- COVID-19 has accelerated consumers' journey to online shopping, made smoother by conveniences such as seamless online payments, expansive logistics and hassle-free return options
- Surge of fast fashion which is likely to be the mainstay
- Women and kids' brands are relatively underpenetrated, leading to higher growth rates than men's fashion. **Women is a key target segment of Nykaa.**

Exhibit 53: Men's fashion has more brand penetration than women's fashion wear

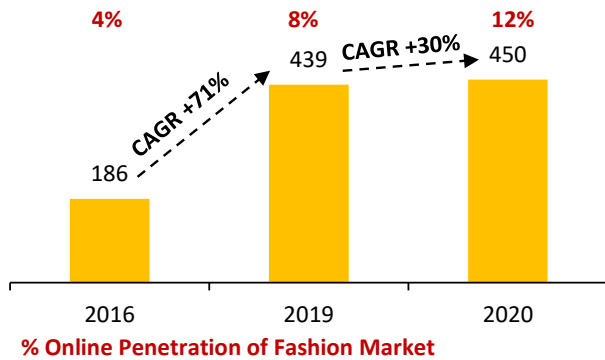


Source: Company, DART

India Online Fashion Market – ~6x of BPC

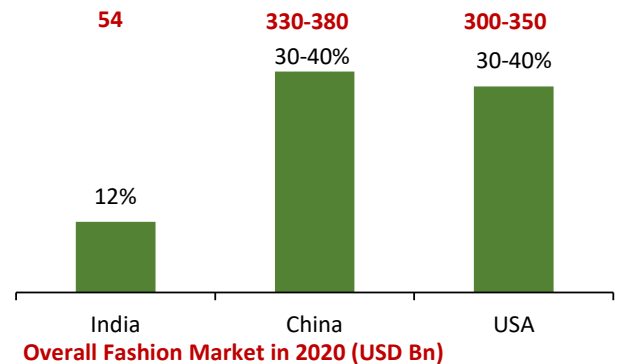
The online fashion retail sector size was Rs 440bn in CY20, growing at 25% CAGR over the past 4 years. This led to online penetration growing 3x in 4 years to 12% in CY20, with relatively higher penetration in the footwear and accessories categories compared to apparel.

Exhibit 54: India Online Fashion Market Size and Growth (Rs Bn)



Source: RHP, RedSeer Research, DART

Exhibit 55: India Online Fashion Penetration Global Benchmarks* (% Penetration)

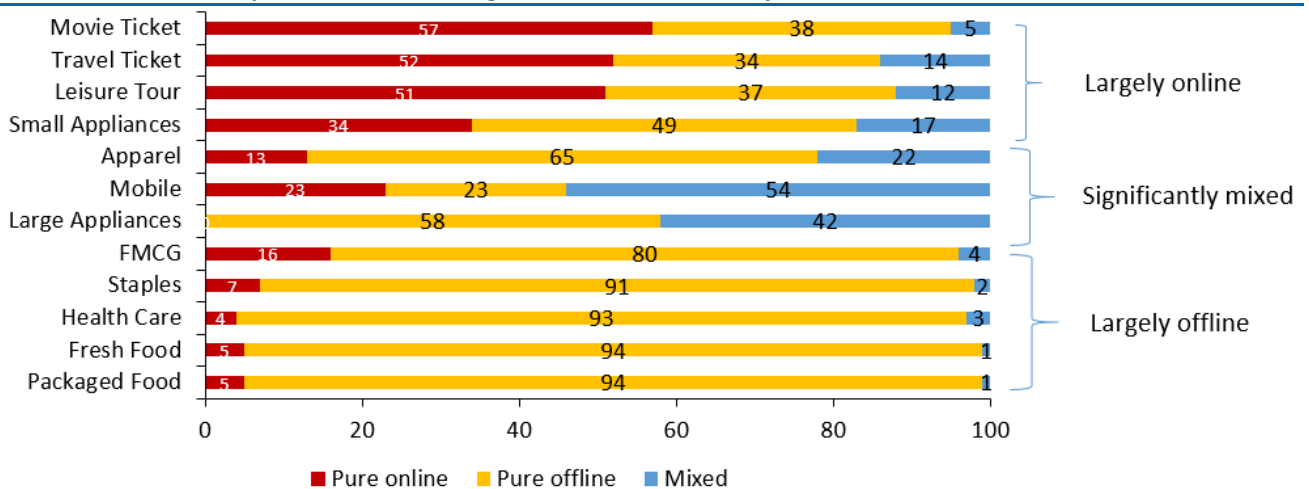


Source: RHP, RedSeer Research, DART

*Fashion market of USA and china includes only apparels and footwear, while in India, the market is inclusive of apparel, footwear and accessories

- **E-Commerce** was expected to disrupt a lot of traditional businesses. Ecommerce has grown significantly but is still a long way to go. Online-penetration varies across categories and is mixed bag for Apparel as a category. That said, Fashion is the 2nd largest category online after electronics. Increased smartphone penetration, convenience of online shopping along-with hassle free returns is driving the online penetration.
- Few categories lend themselves to create large outcomes only through online channels such as women’s innerwear where existing buying experience is sub-optimal

Exhibit 56: Online adoption % across categories – Mixed Pathways



Source: DART, BCG

Fashion – large opportunity but fragmented and competitive

In the fashion segment, Nykaa is a relatively late-comer, where vertical platforms such as Myntra (Flipkart affiliate), AJio, Tata CliQ, Meesho as well as horizontal platforms (Amazon) have significant presence. Meesho recently raised ~\$570mn at valuation of \$4.9bn. It earlier raised \$300mn in Apr'21 at valuation of \$2.1bn.

Myntra started in 2007 is now owned by Flipkart and is one of the leading fashion ecommerce platforms in India. Starting in metros, Myntra has significantly expanded its presence in tier-2 and tier-3 cities in the past few years. Despite a significantly higher GMV at ~\$2bn it is yet to turn profitable.

We like Nykaa's business proposition of focussing on curation through differentiated product offerings with focus on profitability. However, in view of presence of large competitive players with deep-pockets; achieving a meaningful size and scale alongwith profitability in Fashion business could be tough ask.

Exhibit 57: Abridged P&L of Myntra

| Rs Mn | FY19 | FY20 |
|----------------------|----------------|----------------|
| Revenue | 10,411 | 16,754 |
| COGS | 4,158 | 9,184 |
| Gross Profit | 6,253 | 7,570 |
| Emp Cost | 4,252 | 4,606 |
| Other Exps | 7,210 | 9,250 |
| EBITDA | (5,209) | (6,286) |
| D&A | 219 | 346 |
| EBIT | (5,428) | (6,632) |
| Finance Costs | 441 | 1,242 |
| Other Income | 477 | 431 |
| PBT/PAT | (5,392) | (7,443) |
| Common Size % | | |
| Revenue | 100.0 | 100.0 |
| COGS | 39.9 | 54.8 |
| Gross Profit | 60.1 | 45.2 |
| Emp Cost | 40.8 | 27.5 |
| Other Exps | 69.3 | 55.2 |
| EBITDA | (50.0) | (37.5) |
| D&A | 2.1 | 2.1 |
| EBIT | (52.1) | (39.6) |
| Finance Costs | 4.2 | 7.4 |
| Other Income | 4.6 | 2.6 |
| PBT/PAT | (51.8) | (44.4) |

Source: Company, DART

Profit and Loss Account

| (Rs Mn) | FY21A | FY22E | FY23E | FY24E |
|--|---------------|---------------|---------------|---------------|
| Revenue | 24,409 | 38,197 | 52,991 | 74,732 |
| Total Expense | 22,795 | 36,204 | 48,449 | 66,399 |
| COGS | 14,878 | 21,997 | 30,248 | 42,583 |
| Employees Cost | 2,836 | 4,072 | 5,582 | 7,719 |
| Other expenses | 5,080 | 10,135 | 12,619 | 16,097 |
| EBIDTA | 1,614 | 1,993 | 4,543 | 8,333 |
| Depreciation | 671 | 857 | 996 | 1,143 |
| EBIT | 943 | 1,136 | 3,547 | 7,191 |
| Interest | 307 | 443 | 530 | 609 |
| Other Income | 117 | 311 | 469 | 539 |
| Exc. / E.O. items | 0 | 0 | 0 | 0 |
| EBT | 753 | 1,004 | 3,486 | 7,121 |
| Tax | 134 | 190 | 697 | 1,424 |
| RPAT | 619 | 814 | 2,789 | 5,696 |
| Minority Interest | 0 | 0 | 0 | 0 |
| Profit/Loss share of associates | 0 | 0 | 0 | 0 |
| APAT | 619 | 814 | 2,789 | 5,696 |

Balance Sheet

| (Rs Mn) | FY21A | FY22E | FY23E | FY24E |
|-------------------------------|--------------|---------------|---------------|---------------|
| Sources of Funds | | | | |
| Equity Capital | 151 | 473 | 473 | 473 |
| Minority Interest | 8 | 13 | 19 | 28 |
| Reserves & Surplus | 4,749 | 13,942 | 16,731 | 22,427 |
| Net Worth | 4,899 | 14,415 | 17,203 | 22,900 |
| Total Debt | 3,327 | 1,939 | 1,845 | 2,518 |
| Net Deferred Tax Liability | 73 | 104 | 154 | 215 |
| Total Capital Employed | 8,308 | 16,470 | 19,222 | 25,661 |

Applications of Funds

| | | | | |
|---|--------------|------------------|---------------|---------------|
| Net Block | 2,306 | 2,857 | 4,082 | 5,166 |
| CWIP | 0 | 0 | 0 | 0 |
| Investments | 1,084 | 1,591 | 2,062 | 2,703 |
| Current Assets, Loans & Advances | 9,630 | 19,822 | 24,139 | 32,783 |
| Inventories | 4,981 | 8,178 | 11,837 | 15,981 |
| Receivables | 766 | 1,595 | 2,276 | 2,892 |
| Cash and Bank Balances | 2,477 | 7,585 | 6,909 | 9,403 |
| Loans and Advances | 0 | 0 | 0 | 0 |
| Other Current Assets | 1,406 | 2,464 | 3,117 | 4,508 |
| Less: Current Liabilities & Provisions | 4,712 | 7,800 | 11,062 | 14,992 |
| Payables | 3,162 | 5,689 | 8,050 | 10,721 |
| Other Current Liabilities | 1,550 | 2,111 | 3,012 | 4,270 |
| | | <i>sub total</i> | | |
| Net Current Assets | 4,918 | 12,023 | 13,078 | 17,792 |
| Total Assets | 8,308 | 16,470 | 19,222 | 25,661 |

E – Estimates

Important Ratios

| Particulars | FY21A | FY22E | FY23E | FY24E |
|---|--------------|--------------|--------------|--------------|
| (A) Margins (%) | | | | |
| Gross Profit Margin | 39.0 | 42.4 | 42.9 | 43.0 |
| EBIDTA Margin | 6.6 | 5.2 | 8.6 | 11.2 |
| EBIT Margin | 3.9 | 3.0 | 6.7 | 9.6 |
| Tax rate | 17.8 | 18.9 | 20.0 | 20.0 |
| Net Profit Margin | 2.5 | 2.1 | 5.3 | 7.6 |
| (B) As Percentage of Net Sales (%) | | | | |
| COGS | 61.0 | 57.6 | 57.1 | 57.0 |
| Employee | 11.6 | 10.7 | 10.5 | 10.3 |
| Other | 20.8 | 26.5 | 23.8 | 21.5 |
| (C) Measure of Financial Status | | | | |
| Gross Debt / Equity | 0.7 | 0.1 | 0.1 | 0.1 |
| Interest Coverage | 3.1 | 2.6 | 6.7 | 11.8 |
| Inventory days | 74 | 78 | 82 | 78 |
| Debtors days | 11 | 15 | 16 | 14 |
| Average Cost of Debt | 8.2 | 16.8 | 28.0 | 27.9 |
| Payable days | 47 | 54 | 55 | 52 |
| Working Capital days | 74 | 115 | 90 | 87 |
| FA T/O | 10.6 | 13.4 | 13.0 | 14.5 |
| (D) Measures of Investment | | | | |
| AEPS (Rs) | 1.3 | 1.7 | 5.9 | 12.1 |
| CEPS (Rs) | 2.7 | 3.5 | 8.0 | 14.5 |
| DPS (Rs) | 0.0 | 0.0 | 0.0 | 0.0 |
| Dividend Payout (%) | 0.0 | 0.0 | 0.0 | 0.0 |
| BVPS (Rs) | 10.4 | 30.5 | 36.4 | 48.5 |
| RoANW (%) | 15.3 | 8.4 | 17.6 | 28.4 |
| RoACE (%) | 9.9 | 7.4 | 15.9 | 25.6 |
| RoAIC (%) | 13.5 | 12.5 | 26.8 | 40.3 |
| (E) Valuation Ratios | | | | |
| CMP (Rs) | 2248 | 2248 | 2248 | 2248 |
| P/E | 1714.8 | 1304.8 | 380.9 | 186.5 |
| Mcap (Rs Mn) | 1,062,251 | 1,062,251 | 1,062,251 | 1,062,251 |
| MCap/ Sales | 43.5 | 27.8 | 20.0 | 14.2 |
| EV | 1,063,101 | 1,056,605 | 1,057,188 | 1,055,366 |
| EV/Sales | 43.6 | 27.7 | 20.0 | 14.1 |
| EV/EBITDA | 658.6 | 530.2 | 232.7 | 126.6 |
| P/BV | 216.8 | 73.7 | 61.7 | 46.4 |
| Dividend Yield (%) | 0.0 | 0.0 | 0.0 | 0.0 |
| (F) Growth Rate (%) | | | | |
| Revenue | 38.1 | 56.5 | 38.7 | 41.0 |
| EBITDA | 99.2 | 23.5 | 127.9 | 83.4 |
| EBIT | 337.7 | 20.5 | 212.2 | 102.7 |
| PBT | (706.1) | 33.3 | 247.2 | 104.3 |
| APAT | (479.1) | 31.4 | 242.6 | 104.3 |
| EPS | (479.1) | 31.4 | 242.6 | 104.3 |
| Cash Flow | | | | |
| (Rs Mn) | FY21A | FY22E | FY23E | FY24E |
| CFO | 1,498 | (355) | 2,169 | 4,657 |
| CFI | (400) | (893) | (1,603) | (1,485) |
| CFF | (377) | 6,356 | (1,242) | (678) |
| FCFF | 1,078 | (1,247) | 566 | 3,172 |
| Opening Cash | 1,756 | 2,477 | 7,585 | 6,909 |
| Closing Cash | 2,477 | 7,585 | 6,909 | 9,403 |

E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

| | |
|------------|-----------|
| Buy | > 20% |
| Accumulate | 10 to 20% |
| Reduce | 0 to 10% |
| Sell | < 0% |

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