

## FUTURE RETAIL

RETAIL

25 OCT 2017

Company Update

**BUY**

Target Price: Rs 650

### Cementing its leadership position; BUY

After a series of acquisitions in the small stores format, recent HyperCity acquisition will help Future Retail (FRL) to further strengthen its leadership position in modern retail. HyperCity fits perfectly into FRL's premium Big Bazaar GenNxt format and grants it access to key store locations in metros and a loyal customer base. We expect FRL to improve HyperCity's performance given its scale, sourcing capability, back-end expertise and strong private labels (including fbb format).

We now estimate 20% revenue CAGR over FY17-20 (double-digit SSSg at Big Bazaar, addition of HyperCity, fbb gaining share in high-growth value fashion category and rapid expansion of EasyDay convenience store format) and 140 bps EBITDA margin expansion to 4.8% in FY20 (rising share of private label and positive operating leverage). Maintain **BUY** with TP of Rs 650 (Rs 560 earlier) based on 28x target P/E.

CMP : Rs 539  
Potential Upside : 21%

#### MARKET DATA

No. of Shares : 490 mn  
Free Float : 50%  
Market Cap : Rs 264 bn  
52-week High / Low : Rs 593 / Rs 116  
Avg. Daily vol. (6mth) : 933,489 shares  
Bloomberg Code : FRETAIL IB Equity  
Promoters Holding : 50%  
FII / DII : 17% / 5%

### HyperCity in strong hands; premium positioning in sync with Big Bazaar GenNxt format

- ♦ **HyperCity sales throughput to improve with introduction of FRL private labels:** FRL's management plans to convert some of the HyperCity stores into its premium Big Bazaar GenNxt format given their similarity in customer profile. This will help FRL comfortably achieve its target of opening 25-35 hypermarket stores annually. FRL also intends to introduce its private labels in food and fbb stores within all the HyperCity stores, which will be a key driver to increase sales throughput at HyperCity stores (we estimate 11% sales throughput growth over FY17-20E). We estimate HyperCity to contribute 6% to company sales in FY19
- ♦ **Margin improvement to be driven by rising share of apparel:** We estimate the gross margin of HyperCity to improve from 22.7% in FY17 to 24% by FY19, as FRL introduces fbb at all HyperCity stores, thereby increasing the share of higher-margin private label apparel from 16% currently at HyperCity to ~33% share at Big Bazaar. FRL's FY19 net profit will also improve due to tax benefits from Rs 7 bn in accrued losses at HyperCity

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#### Financial summary (Standalone)

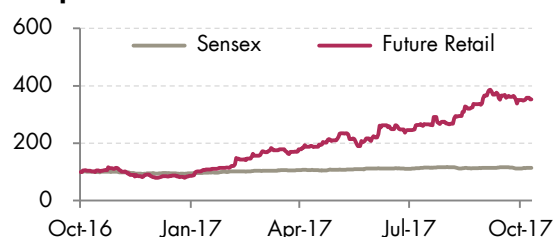
| Y/E March       | FY17    | FY18E   | FY19E   | FY20E   |
|-----------------|---------|---------|---------|---------|
| Sales (Rs mn)   | 170,751 | 206,517 | 250,701 | 292,787 |
| Adj PAT (Rs mn) | 3,683   | 6,501   | 10,243  | 12,439  |
| Con. EPS* (Rs)  | -       | 18.1    | 20.7    | -       |
| EPS (Rs)        | 7.8     | 13.0    | 20.6    | 25.0    |
| Change YOY (%)  | -       | 67.2    | 57.5    | 21.4    |
| P/E (x)         | 69.1    | 41.3    | 26.2    | 21.6    |
| RoE (%)         | 16.6    | 22.0    | 26.5    | 23.5    |
| RoCE (%)        | 16.8    | 20.2    | 25.2    | 27.9    |
| EV/E (x)        | 47.3    | 33.0    | 24.1    | 17.3    |
| DPS (Rs)        | -       | -       | -       | 5.0     |

Source: \*Consensus broker estimates, Company, Axis Capital

#### Key drivers

| (%)                      | FY18E | FY19E | FY20E |
|--------------------------|-------|-------|-------|
| Total store count (Nos.) | 1,186 | 1,440 | 1,760 |
| Sales growth             | 20.9  | 21.4  | 16.8  |
| EBITDA margin            | 3.9   | 4.3   | 4.8   |
| Net profit margin        | 3.1   | 4.1   | 4.2   |

#### Price performance



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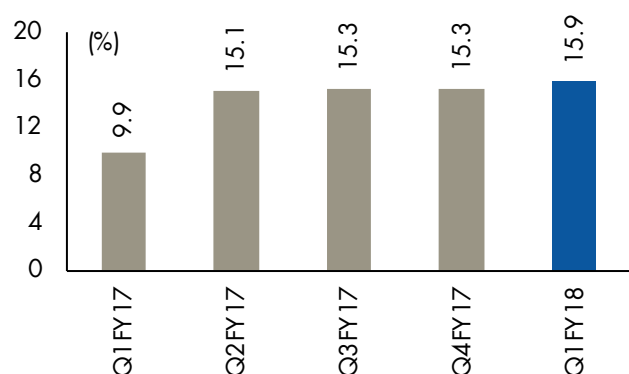
**Q2FY18 preview:** We estimate growth momentum to continue (mid-teen SSSg) as FRL benefits from implementation of GST and shift from unorganized to organized. EBITDA margin is to improve by 120 bps at 4.2% in Q2 driven by positive operating leverage and operational efficiencies.

### Exhibit 1: Store network

| Number of stores | Jun-15     | Sep-15     | Dec-15     | Mar-16     | Jun-16     | Sep-16     | Dec-16     | Mar-17     | Jun-17     |
|------------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|
| Big Bazaar       | 207        | 211        | 211        | 228        | 231        | 230        | 231        | 235        | 253        |
| FoodHall         | 6          | 6          | 6          | 4          | 5          | 6          | 6          | 7          | 7          |
| fbf              | 51         | 50         | 51         | 51         | 50         | 50         | 54         | 54         | 54         |
| e-Zone           | 96         | 93         | 91         | 92         | 88         | 90         | 87         | 30         | 19         |
| Home Town        | 38         | 42         | 42         | 43         | 38         | 37         | 37         | 37         | 37         |
| EasyDay          | 0          | 0          | 0          | 320        | 331        | 338        | 379        | 538        | 523        |
| <b>Total</b>     | <b>398</b> | <b>402</b> | <b>401</b> | <b>738</b> | <b>743</b> | <b>751</b> | <b>794</b> | <b>901</b> | <b>893</b> |

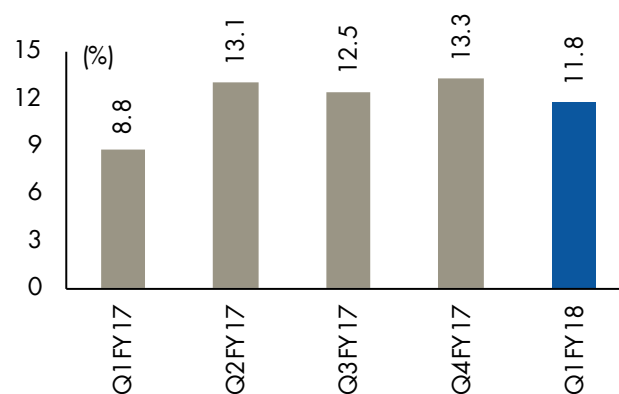
Source: Company

### Exhibit 2: Big Bazaar – SSSg



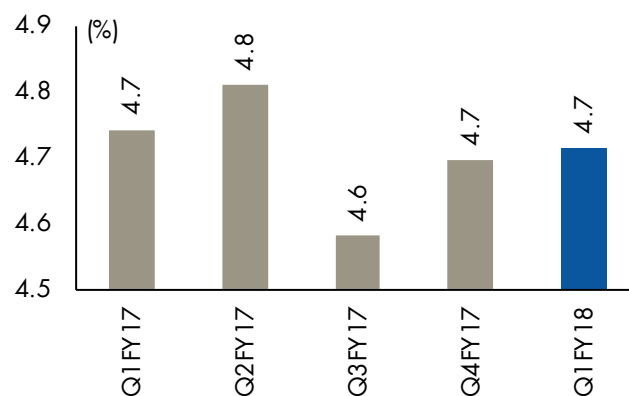
Source: Company, Axis Capital

### Exhibit 3: Company – SSSg



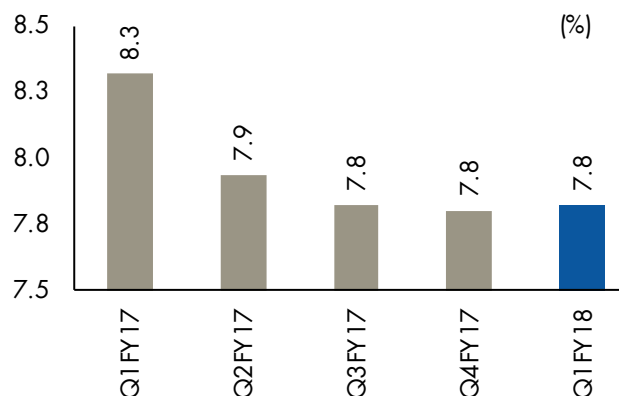
Source: Company, Axis Capital

### Exhibit 4: Staff costs/ sales

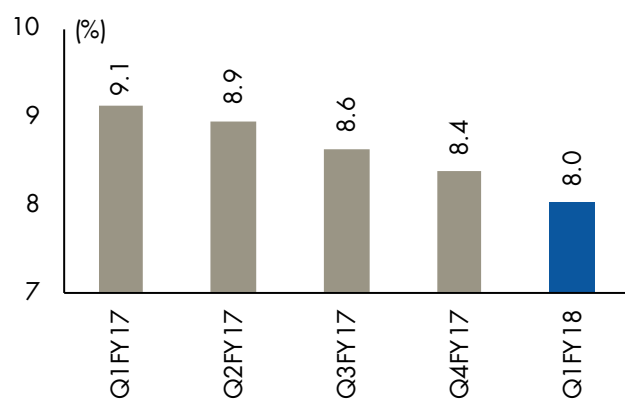


Source: Company, Axis Capital

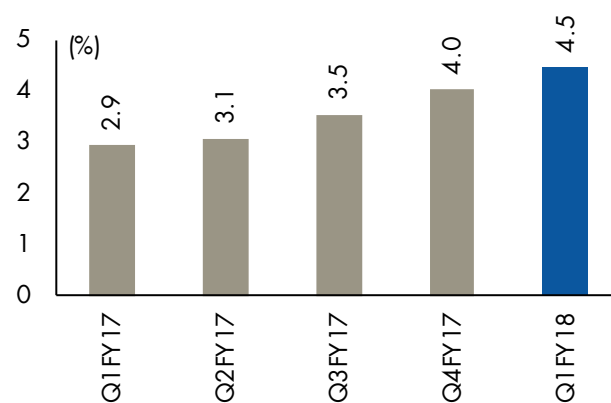
### Exhibit 5: Lease costs/ sales



Source: Company, Axis Capital \*includes rent for stores and rent paid to FEL for furniture and fixtures

**Exhibit 6: Other operating costs/ sales**

Source: Company, Axis Capital

**Exhibit 7: EBITDA margin**

Source: Company, Axis Capital

## Financial summary (Standalone)

### Profit & loss (Rs mn)

| Y/E March                     | FY17           | FY18E          | FY19E          | FY20E          |
|-------------------------------|----------------|----------------|----------------|----------------|
| Net sales                     | 170,751        | 206,517        | 250,701        | 292,787        |
| Other operating income        | -              | -              | -              | -              |
| <b>Total operating income</b> | <b>170,751</b> | <b>206,517</b> | <b>250,701</b> | <b>292,787</b> |
| Cost of goods sold            | (128,344)      | (155,638)      | (190,034)      | (221,636)      |
| Gross profit                  | 42,407         | 50,879         | 60,668         | 71,151         |
| <i>Gross margin (%)</i>       | <i>24.8</i>    | <i>24.6</i>    | <i>24.2</i>    | <i>24.3</i>    |
| Total operating expenses      | (36,595)       | (42,756)       | (49,976)       | (57,152)       |
| <b>EBITDA</b>                 | <b>5,813</b>   | <b>8,123</b>   | <b>10,691</b>  | <b>13,999</b>  |
| <i>EBITDA margin (%)</i>      | <i>3.4</i>     | <i>3.9</i>     | <i>4.3</i>     | <i>4.8</i>     |
| Depreciation                  | (326)          | (326)          | (326)          | (326)          |
| <b>EBIT</b>                   | <b>5,487</b>   | <b>7,797</b>   | <b>10,365</b>  | <b>13,674</b>  |
| Net interest                  | (2,042)        | (1,565)        | (538)          | -              |
| Other income                  | 238            | 270            | 415            | 1,047          |
| <b>Profit before tax</b>      | <b>3,683</b>   | <b>6,501</b>   | <b>10,243</b>  | <b>14,721</b>  |
| Total taxation                | -              | -              | -              | (2,282)        |
| <i>Tax rate (%)</i>           | <i>-</i>       | <i>-</i>       | <i>-</i>       | <i>15.5</i>    |
| Profit after tax              | 3,683          | 6,501          | 10,243         | 12,439         |
| Minorities                    | -              | -              | -              | -              |
| Profit/ Loss associate co(s)  | -              | -              | -              | -              |
| <b>Adjusted net profit</b>    | <b>3,683</b>   | <b>6,501</b>   | <b>10,243</b>  | <b>12,439</b>  |
| <i>Adj. PAT margin (%)</i>    | <i>2.2</i>     | <i>3.1</i>     | <i>4.1</i>     | <i>4.2</i>     |
| Net non-recurring items       | -              | -              | -              | -              |
| <b>Reported net profit</b>    | <b>3,683</b>   | <b>6,501</b>   | <b>10,243</b>  | <b>12,439</b>  |

### Balance sheet (Rs mn)

| Y/E March                     | FY17          | FY18E         | FY19E         | FY20E         |
|-------------------------------|---------------|---------------|---------------|---------------|
| Paid-up capital               | 944           | 996           | 996           | 996           |
| Reserves & surplus            | 24,593        | 32,587        | 42,829        | 60,865        |
| Net worth                     | 25,537        | 33,583        | 43,826        | 61,861        |
| Borrowing                     | 12,590        | 8,276         | -             | -             |
| Other non-current liabilities | -             | -             | -             | -             |
| <b>Total liabilities</b>      | <b>38,127</b> | <b>41,859</b> | <b>43,826</b> | <b>61,861</b> |
| Gross fixed assets            | 6,083         | 5,134         | 5,134         | 5,134         |
| Less: Depreciation            | (546)         | (871)         | (1,197)       | (1,523)       |
| Net fixed assets              | 5,538         | 4,262         | 3,937         | 3,611         |
| Add: Capital WIP              | 119           | 119           | 119           | 119           |
| Total fixed assets            | 5,656         | 4,381         | 4,055         | 3,729         |
| Total Investment              | -             | -             | -             | -             |
| Inventory                     | 37,352        | 43,959        | 50,803        | 58,394        |
| Debtors                       | 2,281         | 2,546         | 3,091         | 3,610         |
| Cash & bank                   | 1,560         | 4,429         | 5,950         | 21,971        |
| Loans & advances              | 17,074        | 17,074        | 17,074        | 17,074        |
| Current liabilities           | 31,249        | 35,982        | 42,599        | 48,369        |
| Net current assets            | 32,471        | 37,478        | 39,771        | 58,132        |
| Other non-current assets      | -             | -             | -             | -             |
| <b>Total assets</b>           | <b>38,127</b> | <b>41,859</b> | <b>43,826</b> | <b>61,861</b> |

Source: Company, Axis Capital

### Cash flow (Rs mn)

| Y/E March                        | FY17           | FY18E          | FY19E          | FY20E          |
|----------------------------------|----------------|----------------|----------------|----------------|
| Profit before tax                | 3,683          | 6,501          | 10,243         | 14,721         |
| Depreciation & Amortisation      | 326            | 326            | 326            | 326            |
| <i>Chg in working capital</i>    | <i>(3,901)</i> | <i>(2,139)</i> | <i>(772)</i>   | <i>(2,340)</i> |
| <b>Cash flow from operations</b> | <b>1,735</b>   | <b>6,253</b>   | <b>10,335</b>  | <b>10,425</b>  |
| <i>Capital expenditure</i>       | <i>-</i>       | <i>950</i>     | <i>-</i>       | <i>-</i>       |
| <b>Cash flow from investing</b>  | <b>-</b>       | <b>950</b>     | <b>-</b>       | <b>8,586</b>   |
| <i>Equity raised/ (repaid)</i>   | <i>1</i>       | <i>45</i>      | <i>-</i>       | <i>-</i>       |
| <i>Debt raised/ (repaid)</i>     | <i>1,231</i>   | <i>(2,814)</i> | <i>(8,276)</i> | <i>-</i>       |
| <i>Dividend paid</i>             | <i>-</i>       | <i>-</i>       | <i>-</i>       | <i>(2,989)</i> |
| <b>Cash flow from financing</b>  | <b>(810)</b>   | <b>(4,334)</b> | <b>(8,814)</b> | <b>(2,989)</b> |
| Net chg in cash                  | 925            | 2,869          | 1,521          | 16,021         |

### Key ratios

| Y/E March                  | FY17 | FY18E | FY19E | FY20E |
|----------------------------|------|-------|-------|-------|
| <b>OPERATIONAL</b>         |      |       |       |       |
| FDEPS (Rs)                 | 7.8  | 13.0  | 20.6  | 25.0  |
| CEPS (Rs)                  | 8.5  | 13.7  | 21.2  | 25.6  |
| DPS (Rs)                   | -    | -     | -     | 5.0   |
| Dividend payout ratio (%)  | -    | -     | -     | 20.0  |
| <b>GROWTH</b>              |      |       |       |       |
| Net sales (%)              | -    | 20.9  | 21.4  | 16.8  |
| EBITDA (%)                 | -    | 39.7  | 31.6  | 30.9  |
| Adj net profit (%)         | -    | 76.5  | 57.5  | 21.4  |
| FDEPS (%)                  | -    | 67.2  | 57.5  | 21.4  |
| <b>PERFORMANCE</b>         |      |       |       |       |
| RoE (%)                    | 16.6 | 22.0  | 26.5  | 23.5  |
| RoCE (%)                   | 16.8 | 20.2  | 25.2  | 27.9  |
| <b>EFFICIENCY</b>          |      |       |       |       |
| Asset turnover (x)         | 5.2  | 5.6   | 6.7   | 7.5   |
| Sales/ total assets (x)    | 2.7  | 2.8   | 3.1   | 3.0   |
| Working capital/ sales (x) | 0.2  | 0.2   | 0.1   | 0.1   |
| Receivable days            | 4.9  | 4.5   | 4.5   | 4.5   |
| Inventory days             | 82.7 | 80.9  | 77.3  | 76.5  |
| Payable days               | 61.5 | 59.9  | 59.5  | 58.8  |
| <b>FINANCIAL STABILITY</b> |      |       |       |       |
| Total debt/ equity (x)     | 0.6  | 0.3   | -     | -     |
| Net debt/ equity (x)       | 0.5  | 0.1   | (0.2) | (0.4) |
| Current ratio (x)          | 2.0  | 2.0   | 1.9   | 2.2   |
| Interest cover (x)         | 2.7  | 5.0   | 19.3  | -     |
| <b>VALUATION</b>           |      |       |       |       |
| PE (x)                     | 69.1 | 41.3  | 26.2  | 21.6  |
| EV/ EBITDA (x)             | 47.3 | 33.0  | 24.1  | 17.3  |
| EV/ Net sales (x)          | 1.6  | 1.3   | 1.0   | 0.8   |
| PB (x)                     | 10.0 | 8.0   | 6.1   | 4.3   |
| Dividend yield (%)         | -    | -     | -     | 0.9   |
| Free cash flow yield (%)   | -    | -     | -     | -     |

Source: Company, Axis Capital

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