AXIS DIRECT

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

(Continued on Page 2...)

Financial summary (Standalone)

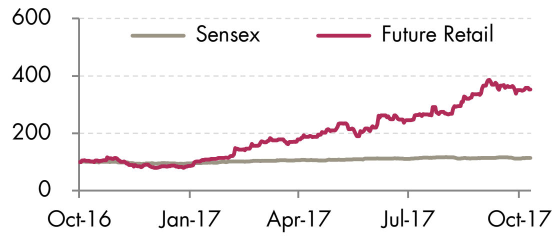
Y/E March	FY17	FY18E	FY19E	FY20E
Sales (Rs mn)	170,751	206,517	250,701	292,787
Adj PAT (Rs mn)	3,683	6,501	10,243	12,439
Con. EPS* (Rs)	-	18.1	20.7	-
EPS (Rs)	7.8	13.0	20.6	25.0
Change YOY (%)	-	67.2	57.5	21.4
P/E (x)	69.1	41.3	26.2	21.6
RoE (%)	16.6	22.0	26.5	23.5
RoCE (%)	16.8	20.2	25.2	27.9
EV/E (x)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



(...continued from Page 1)

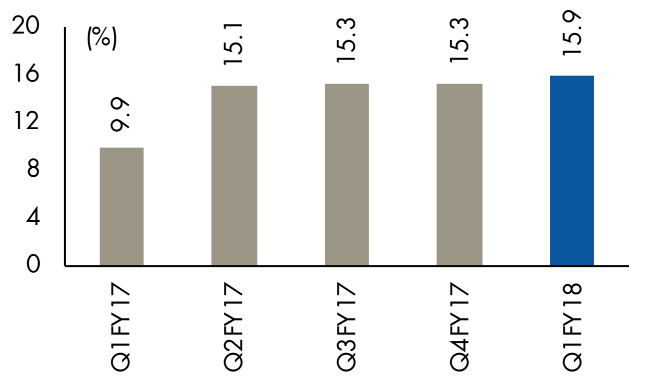
Q2FY18 preview: We estimate growth momentum to continue (mid-teen SSSg) as FRL benefits from implementation of GST and shift from unorganized to organized. EBITDA margin is to improve by 120 bps at 4.2% in Q2 driven by positive operating leverage and operational efficiencies.

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
fbb	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
Total	398	402	401	738	743	751	794	901	893

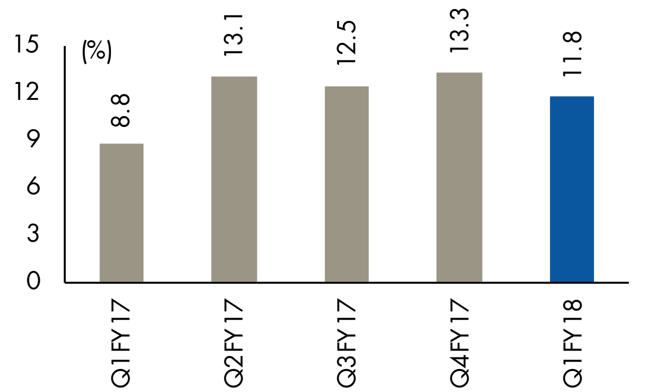
Source: Company

Exhibit 2: Big Bazaar – SSSg



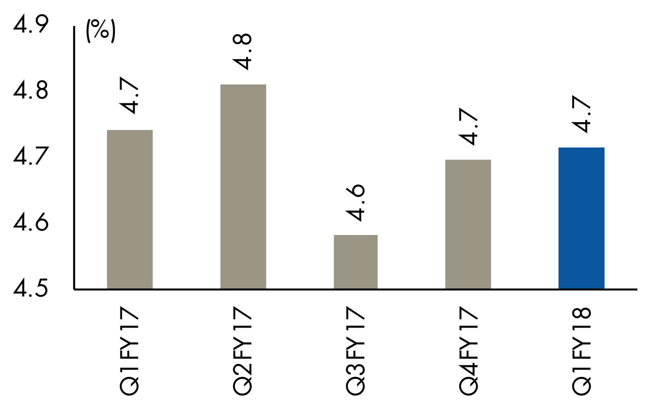
Source: Company, Axis Capital

Exhibit 3: Company – SSSg



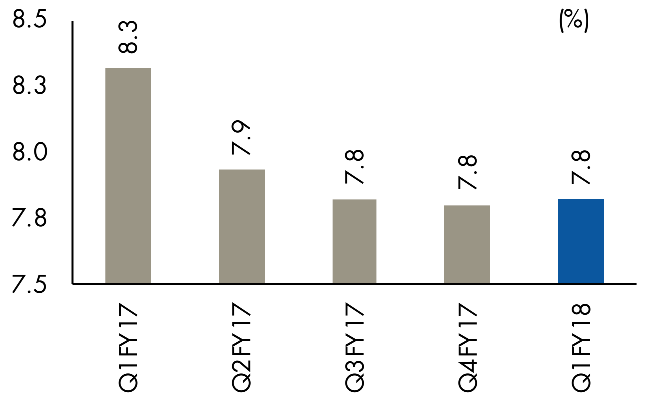
Source: Company, Axis Capital

Exhibit 4: Staff costs/ sales



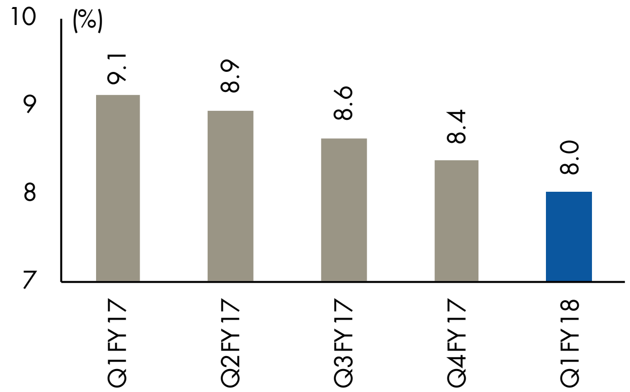
Source: Company, Axis Capital

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

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	-	-	-	-
Total liabilities	**38,127**	**41,859**	**43,826**	**61,861**
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	-	-	-	-
Total assets	**38,127**	**41,859**	**43,826**	**61,861**

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
Chg in working capital	*(3,901)*	*(2,139)*	*(772)*	*(2,340)*
Cash flow from operations	**1,735**	**6,253**	**10,335**	**10,425**
Capital expenditure	-	*950*	-	-
Cash flow from investing	**-**	**950**	**-**	**8,586**
Equity raised/ (repaid)	*1*	*45*	-	-
Debt raised/ (repaid)	*1,231*	*(2,814)*	*(8,276)*	-
Dividend paid	-	-	-	*(2,989)*
Cash flow from financing	**(810)**	**(4,334)**	**(8,814)**	**(2,989)**
Net chg in cash	925	2,869	1,521	16,021

Key ratios

Y/E March	FY17	FY18E	FY19E	FY20E
OPERATIONAL				
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
GROWTH				
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
PERFORMANCE				
RoE (%)	16.6	22.0	26.5	23.5
RoCE (%)	16.8	20.2	25.2	27.9
EFFICIENCY				
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
FINANCIAL STABILITY				
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	-
VALUATION				
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

Disclosures:

The following Disclosures are being made in compliance with the SEBI Research Analyst Regulations 2014 (herein after referred to as the Regulations).

1. Axis Securities Ltd. (ASL) is a SEBI Registered Research Analyst having registration no. INH000000297. ASL, the Research Entity (RE) as defined in the Regulations, is engaged in the business of providing Stock broking services, Depository participant services & distribution of various financial products. ASL is a subsidiary company of Axis Bank Ltd. Axis Bank Ltd. is a listed public company and one of India's largest private sector bank and has its various subsidiaries engaged in businesses of Asset management, NBFC, Merchant Banking, Trusteeship, Venture Capital, Stock Broking, the details in respect of which are available on www.axisbank.com.
2. ASL is registered with the Securities & Exchange Board of India (SEBI) for its stock broking & Depository participant business activities and with the Association of Mutual Funds of India (AMFI) for distribution of financial products and also registered with IRDA as a corporate agent for insurance business activity.
3. ASL has no material adverse disciplinary history as on the date of publication of this report.
4. I/We, authors (Research team) and the name/s subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect my/our views about the subject issuer(s) or securities. I/We also certify that no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. I/we or my/our relative or ASL does not have any financial interest in the subject company. Also I/we or my/our relative or ASL or its Associates may have beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of the Research Report. Since associates of ASL are engaged in various financial service businesses, they might have financial interests or beneficial ownership in various companies including the subject company/companies mentioned in this report. I/we or my/our relative or ASL or its associates do not have any material conflict of interest. I/we have not served as director, officer or employee in the subject company.

Research Team

Sr. No	Name	Designation	E-mail
1	Hiren Trivedi	Research Associate	hiren.trivedi@axissecurities.in
2	Kiran Gawle	Associate	kiran.gawle@axissecurities.in

5. ASL or its associates has not received any compensation from the subject company in the past twelve months. ASL or its Research Analysts has not been engaged in market making activity for the subject company.

6. In the last 12-month period ending on the last day of the month immediately preceding the date of publication of this research report, ASL or any of its associates may have:

i. Received compensation for investment banking, merchant banking or stock broking services or for any other services from the subject company of this research report and / or;
ii. Managed or co-managed public offering of the securities from the subject company of this research report and / or;
iii. Received compensation for products or services other than investment banking, merchant banking or stock broking services from the subject company of this research report;

ASL or any of its associates have not received compensation or other benefits from the subject company of this research report or any other third-party in connection with this report

Term& Conditions:

This report has been prepared by ASL and is meant for sole use by the recipient and not for circulation. The report and information contained herein is strictly confidential and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ASL. The report is based on the facts, figures and information that are considered true, correct, reliable and accurate. The intent of this report is not recommendatory in nature. The information is obtained from publicly available media or other sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. The report is prepared solely for informational purpose and does not constitute an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments for the clients. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ASL will not treat recipients as customers by virtue of their receiving this report.

DEFINITION OF RATINGS	
Ratings	Expected absolute returns over 12-18 months
BUY	More than 10%
HOLD	Between 10% and -10%
SELL	Less than -10%

Axis Securities Limited, Corporate office: Unit No. 2, Phoenix Market City, 15, LBS Road, Near Kamani Junction, Kurla (west), Mumbai-400070, Tel No. – 18002100808/022-61480808, Regd. off.- Axis House, 8th Floor, Wadia International Centre, PandurangBudhkarMarg, Worli, Mumbai – 400 025. Compliance Officer: AnandShaha, Email: compliance.officer@axisdirect.in, Tel No: 022-42671582. SEBI-Portfolio Manager Reg. No. INP000000654