

Avenue Supermarts (AVESUP)

CMP: ₹ 3690

Target: ₹ 4000 (8%)

Target Period: 12 months

HOLD

January 16, 2023

Delay in recovery of GM, apparel subdues margins...

About the stock: Avenue Supermarts (ASL) operates supermarket chain under the 'D-Mart' brand with core focus on value retailing. D-Mart, through its proven business model, has been able to maintain consistent profitability and remains an exceptional performer in its peer group.

- D-Mart has progressively enhanced its return ratios (RoIC: 20%+) despite being capital intensive (follows ownership model)
- Robust store operating metrics (breakeven in 18-24 months of its operations and one of industry best revenue/sq ft: ₹ 30000+)

Q3FY23: D-Mart reported a weak operational performance with profitability coming below our/consensus estimates. Discretionary non-FMCG business (general merchandise & apparel), which yields better margins, continued to perform below expectations and led to a moderation of profitability.

- Sales grew 25% YoY to ₹ 11504 crore (three year CAGR: 19%)
- Discretionary product mix continues to be lower vs. pre-Covid levels leading to lower gross margins (down 60 bps YoY to 14.8%). Higher opex further impacted EBITDA margins, which were at 8.3% (I-direct estimate: 8.8%)
- PAT for the quarter came in at ₹ 589.6 crore (up mere 7% YoY)
- The company added four new D-Mart outlets taking the total store count to 306 with total business area now at 12.6 million sq ft

What should investors do? ASL has been a consistent compounder with the stock price increasing at 27% CAGR in the last five years. However, since the last one year, the stock has delivered negative returns (~12%) owing to revenue trajectory tapering down a bit to 19-20% (vs. 25-30%) and product mix change leading to lower than expected margins. D-Mart continues to remain India's most profitable low cost retailer, a strong play on India's retail growth story and a key beneficiary of unorganised to organised segment shift. We introduce FY25E estimates and bake in earnings CAGR of 22% in FY23-25E (vs. CAGR of 24% witnessed in FY20-23E).

- We maintain **HOLD** recommendation on the stock

Target Price and Valuation: We value ASL at ₹ 4000 i.e. 4x FY25E EV/Sales

Key triggers for future price performance:

- We anticipate store addition trajectory will accelerate and bake in 115 incremental store additions (addition of ~ 6.2 mn sq. ft.) in FY23-25E
- Robust liquidity position and healthy operating cashflows to provide impetus to store addition pace (H1FY23 cash & investments: ₹ 1200+ crore)
- Recovery in GM & apparel segment (~25% of revenues) to shore up margins with subsequent improvement in RoIC: 24% (up 260 bps)

Alternate Stock Idea: Apart from ASL, in our retail coverage, we also like Trent

- We have a BUY rating with target price of ₹ 1730/share

Key Financial Summary

Financials	FY19	FY20	FY21	FY22	FY23E	4 year CAGR (FY19-23E)	FY24E	FY25E	2 year CAGR (FY23-25E)
Net Sales	20,004.5	24,870.2	24,143.1	30,976.3	43,230.1	21.2%	52,933.7	64,303.4	22.0%
EBITDA	1,633.3	2,128.3	1,743.1	2,498.5	3,778.3	23.3%	4,753.4	5,915.3	25.1%
PAT	902.4	1,301.0	1,099.4	1,492.4	2,483.7	28.8%	3,003.8	3,715.6	22.3%
P/E (x)	255.2	183.7	217.4	160.2	96.2		79.6	64.3	
EV/Sales (x)	11.5	9.5	9.8	7.7	5.5		4.5	3.7	
EV/EBITDA (x)	141.3	110.8	135.7	95.0	62.8		49.9	40.0	
RoCE (%)	23.4	16.4	12.5	15.5	20.1		21.4	22.1	
RoE (%)	16.2	11.7	9.0	10.9	15.4		15.7	16.2	

Source: Company, ICICI Direct Research



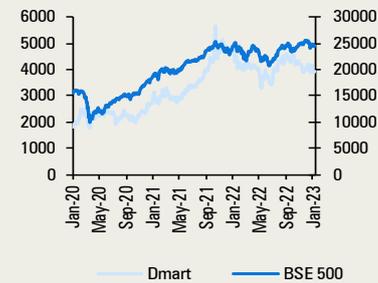
Particulars

Particulars	Amount
Market Capitalisation (₹ crore)	2,39,027.1
Total Debt (FY22) (₹ crore)	-
Cash & Investment (FY22) (₹ crore)	1,575.1
EV (₹ crore)	2,37,452.1
52 Week H / L	4609 / 3185
Equity Capital (₹ crore)	647.8
Face Value (₹)	10.0

Shareholding pattern

	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
Promoter	75.0	75.0	75.0	74.9	74.9
FII	9.4	8.3	8.6	8.7	8.6
DII	6.7	6.8	6.9	7.1	7.1
Others	8.8	9.9	9.5	9.3	9.3

Price Chart



Recent event & key risks

- Added four new stores in Q3

Key Risk: (i) Slower ramp up of store network (ii) Faster recovery in GM & apparel to aid margin improvement

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Key takeaways of Q3FY23 results

- As guided by the management in its pre-quarterly update, Avenue Supermarts reported revenue growth of 25.5% YoY to ₹ 11569.1 crore (three-year CAGR: 19%). The company added four new D-Mart outlets (22 in 9MFY23) taking the total store count to 306 with total business area of 12.6 million sq ft. Average square feet of new stores added is around 50000 (vs. FY22 average of ~41000). D-Mart ready (online business) continues to perform well with revenue growth of 72% YoY to ₹ 264 crore
- Revenue per sq ft did witness a marginal improvement on a YoY basis (~3% YoY) to ₹ 9182. However, it continued to remain below pre-Covid levels (Q3FY20: ₹ 9768). We believe new larger stores added over the past two years have never got an opportunity to function in normal circumstances, which is leading to lower throughput per store. Also, the rationale behind opening larger stores was to stock higher discretionary categories such as GM & apparel, which yields better gross margins. However, Covid led disruptions materially impacted the performance of this category, which, in turn, impacted gross margins and RoCE for the stores
- The management highlighted FMCG and staples continued to outperform general merchandise and apparel segment. With the discretionary product mix being impacted, gross margins for the quarter came in below our estimate at 14.8% (I-direct estimate: 15.2%, Q3FY22: 15.4%, Q3FY20: 15.3%). **On the back of festive purchases in the GM & apparel segment, Q3 generally tends to yield gross margins in excess of 15%. However multi-year low margins recorded in Q3FY23 reflects some grave challenges, which could possibly be on account of heightened competitive intensity over the past two years and inflationary stress still pertaining in the discretionary value segment**
- Opex also grew at a faster clip (~36%) than revenue growth (25%). Subsequently, EBITDA margins declined by 110 bps YoY to 8.3% (I-direct estimate: 8.8%). Absolute EBITDA grew 11% YoY to ₹ 965 crore (I-direct estimate: ₹ 1012 crore, three-year CAGR: 17%). Higher depreciation expenses (owing to addition of new rented stores, up 31% YoY) and finance cost (lease liability, up 22% YoY) further impacted profitability. Ensuing PBT was at ₹ 811.8 crore (I-direct estimate: ₹ 864 crore, up 8% YoY). Consequently, PAT for the quarter came in at ₹ 589.6 crore (up 7% YoY, I-direct estimate: ₹ 646.5 crore)
- Over the last three years, the company has expanded its square feet addition by an impressive three-year CAGR of ~ 22% with average size of new stores being bigger (~60000+ vs. average 35000 sq ft). However, the revenue trajectory has grown at a slower pace (~20%) resulting in lower sales per store. We expect the company to exit FY23E with RoIC of 22% (up 500 bps YoY but still ~500 bps below FY19 levels). We anticipate **RoIC will improve, going forward, driven by dual triggers of enhanced margins (bake in 50 bps improvement in FY23-25E) and better store throughput (asset turn at 3.6x). We build in average SSSG of 11% in FY20-24E with revenue per sq ft of ₹ 36000 in FY25E (FY23: ₹ 32500)**

Exhibit 1: Variance Analysis

	Q3FY23	Q3FY23E	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	Comments
Revenue	11,569.1	11,504.0	9,217.8	25.5	10,638.3	8.7	3-year CAGR: 19%. Revenue/sq. ft. at ₹ 9180 (~93% of pre-covid levels)
Raw Material Expense	9,851.3	9,755.4	7,796.6	26.4	9,029.2	9.1	
Gross Profit	1,717.7	1,748.6	1,421.2	20.9	1,609.1	6.8	
Gross Profit Margin	14.8	15.2	15.4	-57 bps	15.1	-28 bps	Gross margins came in below our estimates owing sustained pressure on GM & apparel segment
Employee exp	192.3	195.6	161.8	18.9	188.6	2.0	
Other Exp	560.2	540.7	392.9	42.6	528.5	6.0	
EBITDA	965.3	1,012.4	866.5	11.4	892.0	8.2	Significantly higher other expenses further impacted profitability (3-year EBITDA CAGR: 17%)
EBITDA Margin (%)	8.3	8.8	9.4	-106 bps	8.4	-4 bps	
Depreciation	168.1	166.8	128.3	31.0	162.0	3.8	
Other Income	31.6	36.6	26.0	21.6	35.6	-11.3	
Interest	17.0	17.9	14.0	21.7	17.7	-4.0	
Exceptional Income	-	-	-	-	-	-	
PBT	811.8	864.3	750.2	8.2	748.0	8.5	
Tax Outgo	222.1	217.8	197.6	12.4	62.2	256.9	
PAT	589.6	646.5	552.5	6.7	685.7	-14.0	

Source: Company, ICICI Direct Research

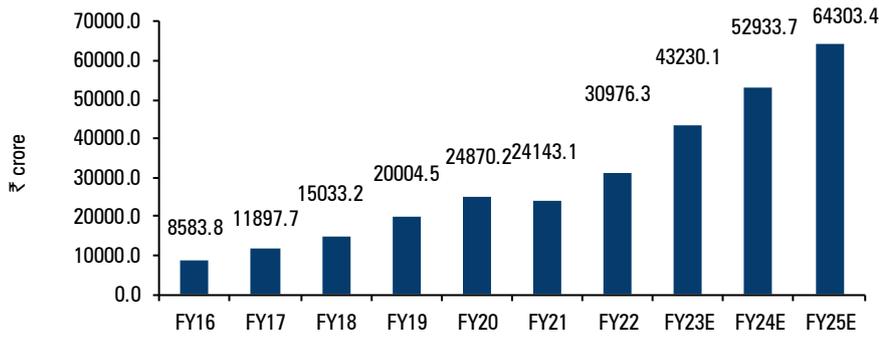
Exhibit 2: Change in estimates

(₹ Crore)	FY 23E			FY 24E			FY 25E
	Old	New	% Change	Old	New	% Change	Introduced
Revenue	43,572.1	43,230.1	-0.8	54,182.2	52,933.7	-2.3	64,303.4
EBITDA	3,912.8	3,778.3	-3.4	5,031.4	4,753.4	-5.5	5,915.3
EBITDA Margin (%)	9.0	8.7	-24 bps	9.3	9.0	-31 bps	9.2
PAT	2,597.3	2,483.7	-4.4	3,205.2	3,003.8	-6.3	3,715.6
EPS (₹)	40.1	38.3	-4.4	49.5	46.4	-6.3	57.4

Source: Company, ICICI Direct Research

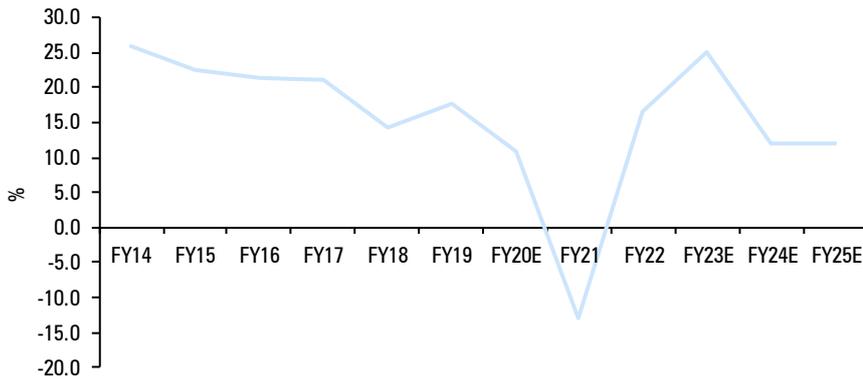
Financial story in charts

Exhibit 3: Revenue growth trend



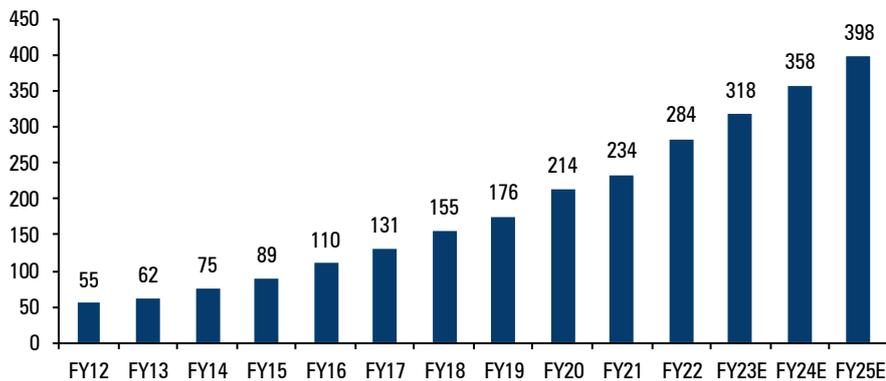
Source: Company, ICICI Direct Research

Exhibit 4: Same stores sales growth (SSSG) trend



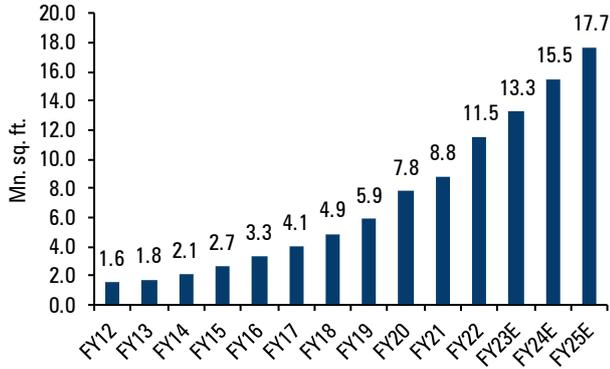
Source: Company, ICICI Direct Research

Exhibit 5: Store addition trend



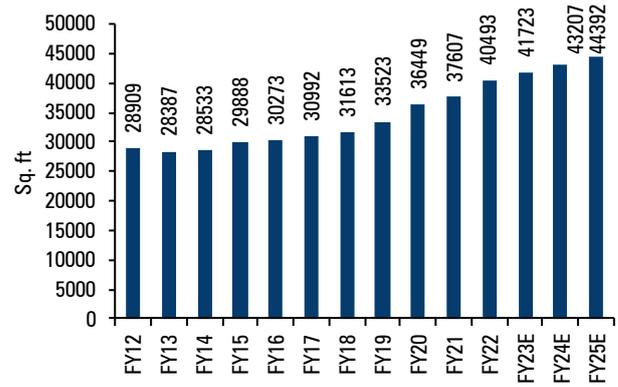
Source: Company, ICICI Direct Research.

Exhibit 6: Total carpet area grows at much faster clip...



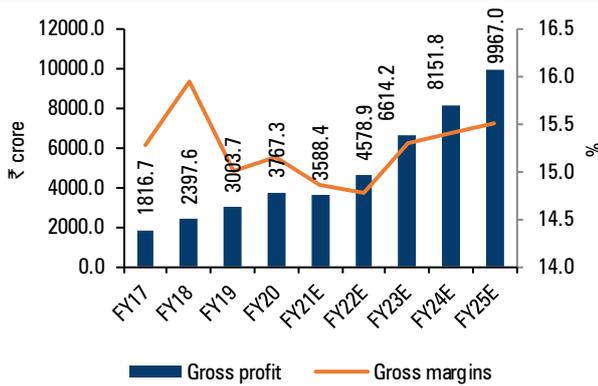
Source: Company, ICICI Direct Research

Exhibit 7: ...with gradual increase in average store size



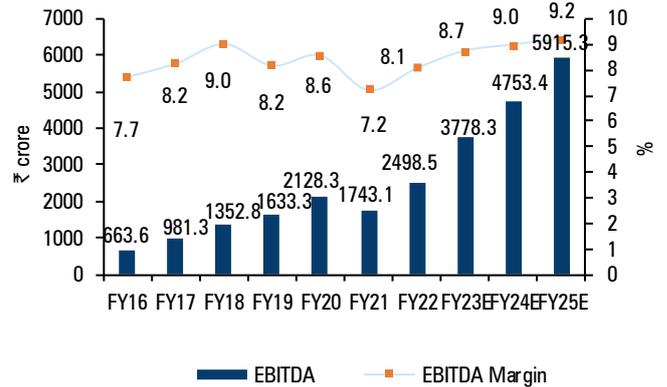
Source: Company, ICICI Direct Research

Exhibit 8: Gross margins trend



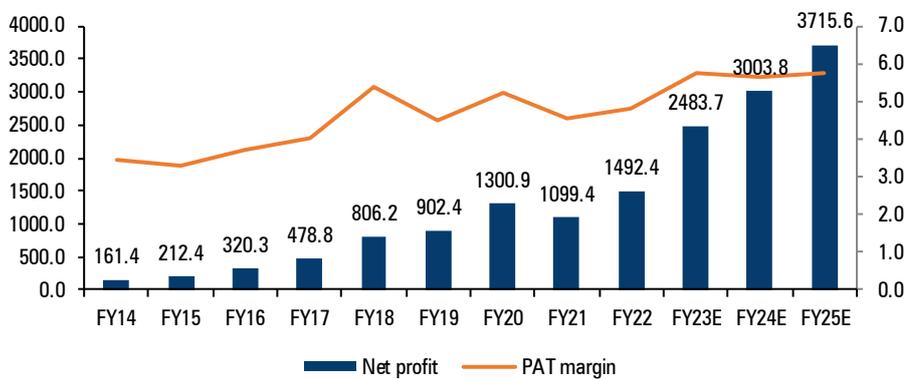
Source: Company, ICICI Direct Research

Exhibit 9: EBITDA margin trend



Source: Company, ICICI Direct Research

Exhibit 10: Net profit trend



Source: Company, ICICI Direct Research.

Financial Summary

Exhibit 11: Profit and loss statement ₹ crore

(Year-end March)	FY22	FY23E	FY24E	FY25E
Net Sales	30,976.3	43,230.1	52,933.7	64,303.4
Growth (%)	28.3	39.6	22.4	21.5
Total Raw Material Cost	26,397.4	36,615.9	44,781.9	54,336.3
Gross Margins (%)	14.8	15.3	15.4	15.5
Employee Expenses	616.2	752.2	899.9	1,157.5
Other Expenses	1,464.2	2,083.7	2,498.5	2,894.3
Total Operating Expenditure	28,477.8	39,451.8	48,180.2	58,388.1
EBITDA	2,498.5	3,778.3	4,753.4	5,915.3
EBITDA Margin	8.1	8.7	9.0	9.2
Interest	53.8	64.7	77.7	89.3
Depreciation	498.1	639.8	777.0	952.2
Other Income	117.5	110.4	117.1	93.7
Exceptional Expense	-	-	-	-
PBT	2,064.1	3,184.3	4,015.8	4,967.3
Total Tax	571.7	700.5	1,012.0	1,251.8
Profit After Tax	1,492.4	2,483.7	3,003.8	3,715.6

Source: Company, ICICI Direct Research

Exhibit 12: Cash flow statement ₹ crore

(Year-end March)	FY22	FY23E	FY24E	FY25E
Profit/(Loss) after taxation	1,492.4	2,483.7	3,003.8	3,715.6
Add: Depreciation	498.1	639.8	777.0	952.2
Net Increase in Current Assets	-446.3	-1,015.7	-752.1	-1,016.1
Net Increase in Current Liabilities:	55.9	240.7	186.9	218.9
CF from operating activities	1,600.0	2,348.5	3,215.7	3,870.6
(Inc)/dec in Investments	-155.9	381.5	133.5	113.5
(Inc)/dec in Fixed Assets	-2,410.0	-2,159.7	-2,970.0	-2,970.0
Others	-56.9	0.0	0.0	0.0
CF from investing activities	-2,622.8	-1,778.2	-2,836.5	-2,856.5
Inc / (Dec) in Equity Capital	0.0	0.0	0.0	0.0
Inc / (Dec) in Loan	0.0	0.0	0.0	0.0
Others	-125.5	-152.8	-194.4	-233.3
CF from financing activities	-125.5	-152.8	-194.4	-233.3
Net Cash flow	-1,148.2	417.5	184.8	780.8
Opening Cash	1,445.6	297.4	714.9	899.7
Closing Cash	297.4	714.9	899.7	1,680.5

Source: Company, ICICI Direct Research

Exhibit 13: Balance Sheet ₹ crore

(Year-end March)	FY22	FY23E	FY24E	FY25E
Equity Capital	647.8	647.8	647.8	647.8
Reserve and Surplus	13,028.3	15,512.1	18,515.9	22,231.5
Total Shareholders funds	13,676.1	16,159.8	19,163.7	22,879.2
Total Debt	-	-	-	-
Non Current Liabilities	712.0	712.0	712.0	712.0
Source of Funds	14,388.1	16,871.8	19,875.6	23,591.2
Gross block	9,256.4	11,595.4	14,565.4	17,535.4
Less: Accum depreciation	1,485.9	1,972.9	2,555.5	3,274.5
Net Fixed Assets	7,770.5	9,622.5	12,009.9	14,260.9
Capital WIP	1,129.3	950.0	950.0	950.0
Intangible assets	91.9	91.9	91.9	91.9
Investments	1,277.7	896.1	762.6	649.1
Inventory	2,742.7	3,671.6	4,350.7	5,285.2
Cash	297.4	714.9	899.7	1,680.5
Debtors	66.9	118.4	145.0	176.2
Loans & Advances & Other	328.8	345.2	352.1	359.2
Total Current Assets	3,435.7	4,850.1	5,747.6	7,501.1
Creditors	589.2	829.1	1,015.2	1,233.2
Provisions & Other CL	494.2	495.0	495.8	496.7
Total Current Liabilities	1,083.4	1,324.1	1,511.0	1,729.9
Net Current Assets	2,352.4	3,526.1	4,236.6	5,771.2
LT L& A, Other Assets	1,766.4	1,785.2	1,824.7	1,868.1
Other Assets	0.0	0.0	0.0	0.0
Application of Funds	14,388.1	16,871.8	19,875.6	23,591.2

Source: Company, ICICI Direct Research

Exhibit 14: Key ratios

(Year-end March)	FY22	FY23E	FY24E	FY25E
Per share data (₹)				
EPS	23.0	38.3	46.4	57.4
Cash EPS	30.7	48.2	58.4	72.1
BV	211.1	249.5	295.8	353.2
Cash Per Share	4.6	11.0	13.9	25.9
Operating Ratios (%)				
EBITDA margins	8.1	8.7	9.0	9.2
PBT margins	6.7	7.4	7.6	7.7
Net Profit margins	4.8	5.7	5.7	5.8
Inventory days	32.3	31.0	30.0	30.0
Debtor days	0.8	1.0	1.0	1.0
Creditor days	6.9	7.0	7.0	7.0
Return Ratios (%)				
RoE	10.9	15.4	15.7	16.2
RoCE	15.5	20.1	21.4	22.1
RoIC	16.5	21.6	22.7	24.2
Valuation Ratios (x)		5.0		
P/E	160.2	96.2	79.6	64.3
EV / EBITDA	95.0	62.8	49.9	40.0
EV / Sales	7.7	5.5	4.5	3.7
Market Cap / Revenues	7.7	5.5	4.5	3.7
Price to Book Value	17.5	14.8	12.5	10.4
Solvency Ratios				
Debt / Equity	0.0	0.0	0.0	0.0
Debt/EBITDA	0.0	0.0	0.0	0.0
Current Ratio	2.9	3.1	3.2	3.4
Quick Ratio	0.4	0.4	0.3	0.3

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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