Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

# Aditya Birla Fashion & Retail Ltd

## TCNS acquisition in-line with long-term strategy

| Consumer Discretionary | | Sharekhan code: ABFRL | |
|---|---|---|---|
| **Reco/View: Buy** | ↔ | CMP: **Rs. 206** | Price Target: **Rs. 250** ↓ |

↑ Upgrade ↔ Maintain ↓ Downgrade

Stock Update

Company Update

| 3R MATRIX | + | = | - |
|---|---|---|---|
| Right Sector (RS) | ✓ | | |
| Right Quality (RQ) | ✓ | | |
| Right Valuation (RV) | ✓ | | |

\+ Positive = Neutral – Negative

**What has changed in 3R MATRIX**

| | Old | | New |
|---|---|---|---|
| RS | | ↔ | |
| RQ | | ↔ | |
| RV | | ↔ | |

**ESG Disclosure Score** NEW

ESG RISK RATING 12.33

Updated May 08, 2023

**Low Risk**

| NEGL | LOW | MED | HIGH | SEVERE |
|---|---|---|---|---|
| 0-10 | 10-20 | 20-30 | 30-40 | 40+ |

*Source: Morningstar*

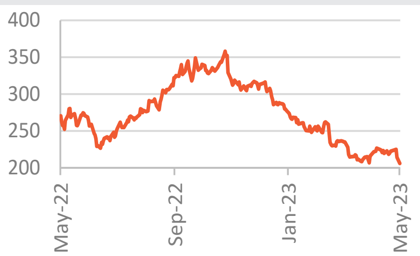
### Company details

| | |
|---|---|
| Market cap: | Rs. 19,559 cr |
| 52-week high/low: | Rs. 359 / 200 |
| NSE volume: (No of shares) | 21.9 lakh |
| BSE code: | 535755 |
| NSE code: | ABFRL |
| Free float: (No of shares) | 42.2 cr |

### Shareholding (%)

| | |
|---|---|
| Promoters | 55.5 |
| FII | 14.9 |
| DII | 18.9 |
| Others | 10.8 |

### Price chart




### Price performance

| (%) | 1m | 3m | 6m | 12m |
|---|---|---|---|---|
| Absolute | -4.5 | -18.1 | -35.7 | -23.7 |
| Relative to Sensex | -7.7 | -20.5 | -36.6 | -36.4 |

*Sharekhan Research, Bloomberg*


**Summary**

- Aditya Birla Fashion and Retail (ABFRL) to acquire TCNS Clothing (TCNS), owner of ethnic brands, including W, Aurelia, Wishful, Folksong and Elleven for Rs. 2,891 crore (2.4x its FY23E EV/Sales).
- The acquired portfolio with ethnic business to scale-up to Rs. 5,000 crore by FY27 (50% will be contributed by TCNS brands); Management expects EBIDTA margins of TCNS to recover to double digits in two years from current single digit (pre-Ind AS).
- Acquisition will be done through mix of debt (Rs. 700-800 crore) and GIC's second tranche of infusion of Rs. 1,425 crore. Management expects acquisition to be marginally EPS accretive from FY25 against the street's assumption of 6-8% earnings dilution.
- After the recent correction, the stock trades at an attractive valuation of 12x/10x its FY24E/25E EV/EBIDTA. As overhang around the acquisition is over and management is providing clarity on earnings prospects, the downside risk is limited. We maintain our Buy rating with revised PT of Rs. 250.


**Aditya Birla Fashion and Retail (ABFRL) has entered into definitive agreements to acquire TCNS Clothing (TCNS), the owner of ethnic brands, including W, Aurelia, Wishful, Folksong and Elleven. The acquisition is line with ABFRL's strategy to become a strong play in the branded ethnic wear space. This transaction will be carried out in two stages 1) acquiring 51% stake for Rs. 1,650 crore and 2) a merger between the two entities at ratio of 11 ABFRL shares for every 6 held by TCNS shareholders. Overall, the acquired company is value at Rs. 2,891 crore at valuation of FY23E EV/annualised sales of 2.4x. Acquisition will be done through mix of debt (Rs. 700-800 crore) and GIC's second tranche of infusion of Rs. 1,425 crore. Management expects ethnic wear business to scale up to Rs. 5,000 crore by FY2027 (50% will be contributed by TCNS brands) from expected close of ~Rs. 600 crore in FY2023. With TCNS' EBIDTA margins expected to improve strongly in next two years, the management expects acquisition to be marginally EPS accretive in FY2025 against street expectation of 6-8% earnings dilution. Integration of TCNS brands under the distribution of ABFRL, fast scale-up in the ethnic business as guided by management and GIC'S infusion happening as per terms to complete the acquisition on time needs to be monitored in the next 6-12 months.**

- **Event: ABFRL acquires TCNS clothing in-line with growth strategy:** ABFRL to acquire TCNS, a strong play in women-ethnic wear, in-line with its long term strategy of becoming one of the strong play in the branded ethnic wear space. This transaction will be carried out in two stages - (1) Acquisition of the founding promoter's stake through a SPA and open offer for Rs. 1,650 crore for 51% stake and (2) Merger between two entities at ratio of 11 shares of ABFRL for every 6 shares held by TNCS shareholders. Overall, the acquired company is value at Rs. 2,891 crore (~Rs. 450 per share) at valuation of FY23E EV/annualised sales of 2.4x. It will be funded through mix of debt of Rs. 700-800 crore and GIC's infusion of Rs. 1,425 crore.
- **Acquisition rationale:** The ethnic wear market is 30% of overall branded apparel market in India. Women ethnic wear market is ~90% of total ethnic wear market with premium ethnic wear having large pie in the share. TCNS, through its brands W, Aurelia, Wishful, Folksong & Elleven, is catering to the Indian women's fashion needs across various price points from occasional wear to daily wear. Each of these brands have strong acceptance among consumers. Thus TCNS' portfolio will complement ABFRL's existing ethnic wear portfolio. Further, ABFRL's strong distribution network and expertise of making successful brands will help the ethnic business to scale-up fast.
- **Acquisition to be earnings accretive from FY25:** With an acquired portfolio, ABFRL's management expects ethnic wear business to scale up to Rs. 5,000 crore by FY2027. Aurelia and W brands are expected to reach revenues of Rs. 1,000-1,500 crore while Tasva (men's ethnic brand) will be Rs. 1,000 crore. This along with TCNS' EBIDTA margins expected to improve strongly in next two years, the management expects acquisition to be marginally EPS accretive in FY2025 against the street's expectation of a 6-8% earnings dilution.

**Our Call**

**Outlook and view:** Post acquisition of TCNS, ABFRL will focus on scaling up recently-acquired businesses in 3-5 years. Excluding TCNS acquisition, ABFRL is well-poised to cross revenues of Rs. 21,000 crore in FY2027. Integration of TCNS brands under the distribution of ABFRL, fast scale-up in the ethnic wear business as guided by management, consistent expansion in margins and the GIC's infusion happening as per terms to complete the acquisition on time need to be monitored in the next 6-12 months. ABFRL's stock price has corrected by 18% in last three months (42% from its high) and is currently trading at attractive valuation of 12x/10x its FY24E/25E EV/EBIDTA. As overhang around acquisition is over and the management is providing clarity on earnings prospects of acquired business, the downside risk is limited. We re-iterate Buy on the stock with a revised PT of Rs. 250.

**Key Risks**

Any late recovery in the EBIDTA margins of TCNS or late infusion of funds by GIC might delay the completion of acquisition, which might act as a risk to earnings growth expectation over the next three to four years.

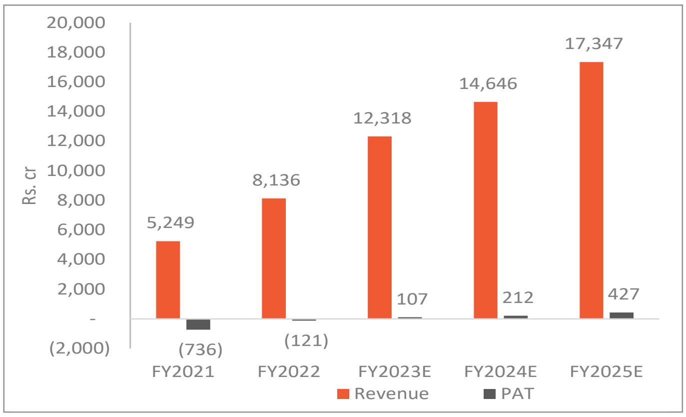
**Valuations (consolidated)** Rs cr

| Particulars | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| Revenue | 5,249 | 8,136 | 12,318 | 14,646 | 17,347 |
| EBITDA Margin (%) | 10.6 | 13.5 | 13.1 | 13.7 | 14.4 |
| Adjusted PAT | -736 | -121 | 107 | 212 | 427 |
| Adjusted EPS (Rs.) | -7.3 | -1.2 | 1.1 | 2.1 | 4.2 |
| P/E (x) | - | - | - | 98.7 | 48.9 |
| P/B (x) | 7.0 | 6.9 | 5.4 | 3.9 | 3.6 |
| EV/EBITDA (x) | 40.0 | 21.2 | 14.6 | 12.3 | 9.6 |
| RoNW (%) | - | - | 3.3 | 4.7 | 7.7 |
| RoCE (%) | - | 3.1 | 7.0 | 7.2 | 9.3 |

*Source: Company; Sharekhan estimates*

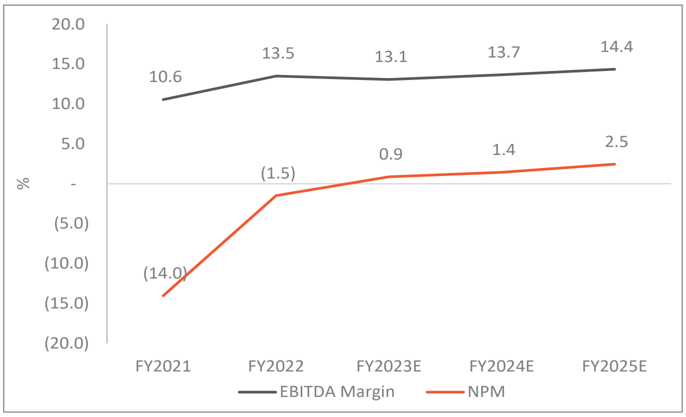
## Financials in charts

### Steady growth in revenue and PAT



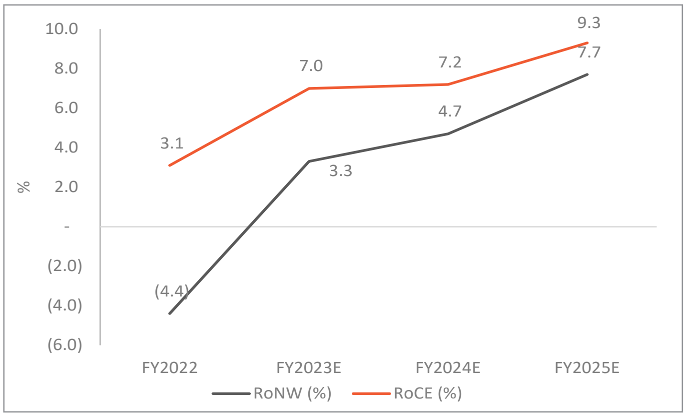

*Source: Company, Sharekhan Research*

### Margins to improve going ahead



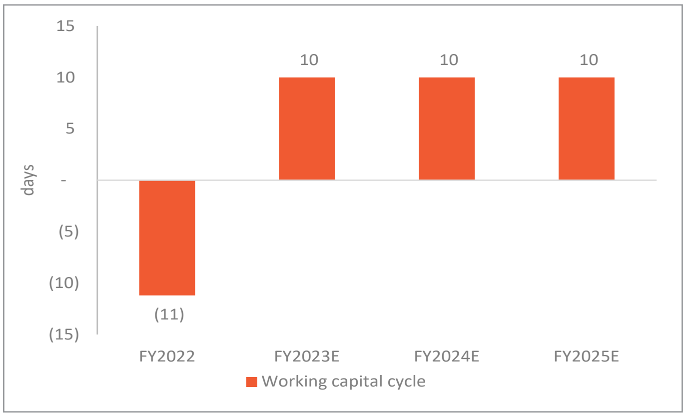

*Source: Company, Sharekhan Research*

### Return ratios to rise from current level



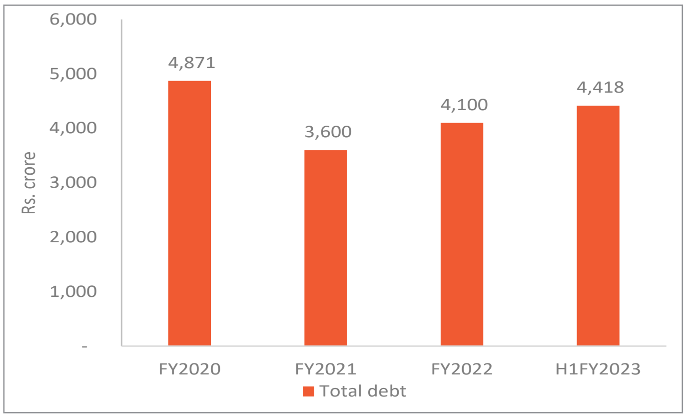

*Source: Company, Sharekhan Research*

### Stable working capital days



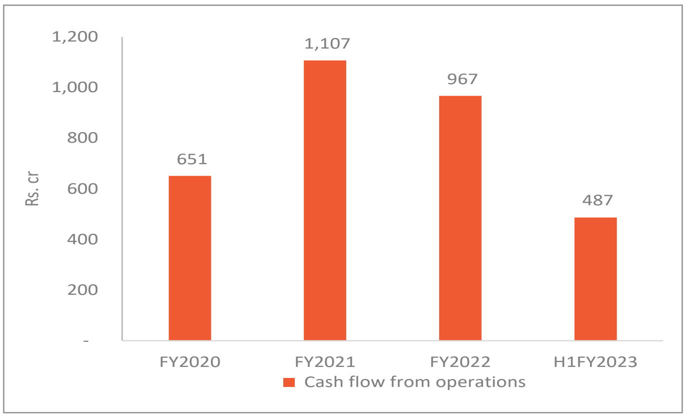

*Source: Company, Sharekhan Research*

### Trend in total debt




*Source: Company, Sharekhan Research*

### Trend in cash flow from operations




*Source: Company, Sharekhan Research*

## Outlook and Valuation

### ■ Sector Outlook – Long term growth prospects intact

Branded retail and apparel companies posted strong performance in FY2023 led by low base of FY2022 impacted by COVID-led disruptions. We expect growth to be muted in H1FY2024 but expect it to recover prior to festive season. Branded retail and apparel companies are likely to benefit from a steady demand for premium products and better consumer sentiments in urban markets/metros in the quarters ahead. In the medium-long term, market share gains, higher traction on the e-Commerce platform, a strong retail space expansion strategy, and sustained expansion of product portfolio will help branded apparel and retail companies to post consistent growth. Better operating leverage and improved efficiencies would help branded apparel and retail companies to post higher margins in the coming years.

### ■ Company Outlook – Revenue to cross Rs. 12,000 crore in FY2023

ABFRL remains focused on leveraging its strong brand portfolio, evolving its product profile in line with changing consumer preferences, and expanding its reach (especially in smaller towns and cities). The company is focusing on strengthening its online platforms to provide comfortable buying options to customers. Overall, we expect ABFRL's revenue and EBITDA to report CAGRs of 26% and 33%, respectively, over FY2022-FY2025.

### ■ Valuation – Retain Buy with a revised PT of Rs. 250

Post acquisition of TCNS, ABFRL will focus on scaling up recently-acquired businesses in 3-5 years. Excluding TCNS acquisition, ABFRL is well-poised to cross revenues of Rs. 21,000 crore in FY2027. Integration of TCNS brands under the distribution of ABFRL, fast scale-up in the ethnic wear business as guided by management, consistent expansion in margins and the GIC's infusion happening as per terms to complete the acquisition on time need to be monitored in the next 6-12 months. ABFRL's stock price has corrected by 18% in last three months (42% from its high) and is currently trading at attractive valuation of 12x/10x its FY24E/25E EV/EBIDTA. As overhang around acquisition is over and the management is providing clarity on earnings prospects of acquired business, the downside risk is limited. We re-iterate Buy on the stock with a revised PT of Rs. 250.

**Peer Comparison**

| Companies | P/E (x) | | | EV/EBITDA (x) | | | RoCE (%) | | |
|---|---|---|---|---|---|---|---|---|---|
| | FY22 | FY23E | FY24E | FY22 | FY23E | FY24E | FY22 | FY23E | FY24E |
| Trent | - | 91.1 | 63.3 | 55.4 | 33.0 | 26.2 | 9.6 | 14.5 | 18.4 |
| Shoppers Stop | - | 61.8 | 51.9 | 21.7 | 13.0 | 11.0 | 2.4 | 9.9 | 10.9 |
| ABFRL | - | - | 98.7 | 21.2 | 14.6 | 12.3 | 3.1 | 7.0 | 7.2 |

*Source: Company; Sharekhan Research*

## About the company

ABFRL is India's largest pure-play fashion and retail entity with a combined retail footprint of 9.2 million square feet across more than 750 cities, which includes 3,848 stores across approximately 32,589 multi-brand outlets with 6,048 point of sales in department stores across India. The company has leading brands under its umbrella, such as Louis Philippe, Van Heusen, Allen Solly, Peter England, and Pantaloons. The international brands' portfolio includes – The Collective, Simon Carter, and select brands such as Ralph Lauren, Hackett London, Ted Baker, Fred Perry, Forever 21, American Eagle, Reebok, and Galeries Lafayette. ABFRL's foray into the branded ethnic wear business includes Jaypore, Tasva, and Marigold Lane and strategic partnerships with designers Shantanu & Nikhil, Tarun Tahiliani, House of Masaba, and Sabyasachi. In addition, to cater to the needs of digitally native consumers, ABFRL is also building a portfolio of digital-first brands under its technology-led 'House of D2C Brands' venture, TMRW.

## Investment theme

ABFRL is one of the largest players in the branded apparel and retail space. The company has built an agile supply chain model to deliver continuous fresh fashion throughout the year with its 12-season model, which will aid in reducing working capital in the coming years. The company has entered into strategic partnerships with designers such as Shantanu & Nikhil, Tarun Tahiliani, Sabyasachi, and House of Masaba, to tap the ethnic and wedding segments, which has a large unorganised presence. Going ahead, the company's growth would be driven by capex across brands, marketing expenses incurred on brands, IT and digital enhancement, and strengthening the overall digital play through organic and inorganic routes. The company is confident of achieving its target of Rs. 21,000 crore revenue with EBITDA of over Rs. 2,350 crore by FY2026.

## Key Risks

- Any slowdown in the discretionary demand environment would impact same store sales growth (SSSG), affecting revenue growth.
- Heightened competition, especially in the form of private labels by other branded players, would act as a threat to revenue growth.

## Additional Data

**Key management personnel**

| | |
|---|---|
| Kumar Mangalam Birla | Chairman |
| Ashish Dikshit | Managing Director |
| Jagdish Bajaj | Chief Financial Officer |
| Anil Malik | Company Secretary |

*Source: BSE; Company*

**Top 10 shareholders**

| Sr. No. | Holder Name | Holding (%) |
|---|---|---|
| 1 | Flipkart Inv Pvt Ltd | 7.7 |
| 2 | Nippon Life India Asset Management Company | 2.3 |
| 3 | UTI Asset Management Co Ltd | 2.1 |
| 4 | ICICI Prudential Life Insurance Co. | 2.0 |
| 5 | Franklin Resources Inc | 2.0 |
| 6 | Vanguard Group Inc | 1.5 |
| 7 | Tata AMC | 1.4 |
| 8 | SBI Life Insurance Co Ltd | 1.3 |
| 9 | Axis AMC | 1.1 |
| 10 | PGIM India AMC | 0.9 |

*Source: Bloomberg*

## Understanding the Sharekhan 3R Matrix

| | |
|---|---|
| **Right Sector** | |
| Positive | Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies |
| Neutral | Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies |
| Negative | Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability. |
| **Right Quality** | |
| Positive | Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance. |
| Neutral | Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable |
| Negative | Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet |
| **Right Valuation** | |
| Positive | Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment. |
| Neutral | Trading at par to historical valuations and having limited scope of expansion in valuation multiples. |
| Negative | Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple. |

*Source: Sharekhan Research*

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