Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

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 Updated Jul 08, 2023				13.06
Low Risk				
NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

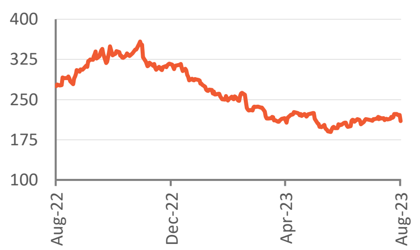
Company details

Market cap:	Rs. 19,949 cr
52-week high/low:	Rs. 359 / 184
NSE volume: (No of shares)	33.2 lakh
BSE code:	535755
NSE code:	ABFRL
Free float: (No of shares)	42.3 cr

Shareholding (%)

Promoters	55.5
FII	14.5
DII	17.1
Others	12.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-0.2	-1.8	-16.1	-23.6
Relative to Sensex	-0.6	-9.5	-24.1	-36.3

Sharekhan Research, Bloomberg

Stock Update

Result Update

Aditya Birla Fashion & Retail Ltd

Weak Q1; long way to go for margin recovery; Downgrade to Hold

Consumer Discretionary		Sharekhan code: ABFRL		
Reco/View: Hold	↓	CMP: **Rs. 210**	Price Target: **Rs. 225**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- ABFRL posted yet another weak quarter impacted by slowdown in discretionary spends resulting low single digit growth in branded apparel category in Q1FY24. Revenues of Lifestyle brand grew by 5% while Pantaloons saw just 1% growth (SSSG declined by 8%).
- Consolidated EBIDTA margins stood at 9% in Q1 (standalone EBIDTA margins stood at 12%). With large investment in ethnic business and new acquired businesses, we expect recovery in the profitability to take time.
- Net debt is expected to be at Rs. 2,800 crore at FY2024-end post the acquisition of controlling stake in TCNS clothing. This will lead to an increase in the interest costs in the next two years.
- Stock has corrected by 41% from its high and is trading at 18x/14x its FY2024E/25E EV/EBITDA. In view of weak earning visibility in the near term, we downgrade our rating on the stock to Hold from Buy earlier with an unchanged PT of Rs. 225.

Aditya Birla Fashion & Retail Limited's (ABFRL's) consolidated results (including ethnic business) was weak in Q1FY2024 mainly on account of weak consumer discretionary demand, resulting in moderate revenue growth and lower profitability in Q1FY2024. Revenue grew by 11.2% y-o-y to Rs. 3,196.1 crore driven by strong double-digit growth in super premium and luxury brand, acquisition of Reebok and 34% y-o-y growth in ethnic business on low base. The company posted a loss of Rs. 161 crore in Q1FY2024 versus a PAT of Rs. 94.4 crore in Q1FY2023. Consolidated EBIDTA margins came at 9.1% in Q1FY2024 versus 16.3% in Q1FY2023. Overall, Q1FY2024 was the third consecutive quarter of weak operating performance led by decline in the consumer spendings. Net debt increased to Rs. 2,100 crore due to working capital requirement, capital expenditure and losses in emerging businesses.

Key positives

- Super premium brands registered sales growth of 16% y-o-y, while the American Eagle brand registered 49% y-o-y growth.
- Recently acquired Reebok brand registered 43% y-o-y revenue growth with 11% LTL growth.

Key negatives

- Consolidated EBIDTA margins decreased by 715 bps y-o-y to 9.1%
- Pantaloons retail LTL sales declined by 8%.

Management Commentary

- Weak consumer sentiments hit the performance of all key businesses (including Lifestyle and Pantaloons) resulting in sluggish growth. Q2FY24 is expected to muted as well and a recovery is eyed from Q3FY2024 as festive season and wedding season is likely to provide some uptick in demand.
- EBIDTA margins are expected to remain under pressure in the near term due to expected sluggish sales and sustained high investments in the ethnic and TMRW business.
- Amid a slowdown in discretionary environment, the management has decided to go slow with the store additions in the coming quarters. It will increase the store addition pace once the recovery is witnessed in the discretionary environment.
- Net debt on books increased to Rs. 2,100 crore to take working capital requirement, capital expenditure and losses in the emerging businesses. The same is expected to go up to Rs. 2,800 crore by FY2024-end post the acquisition of controlling stake in TCNS clothing.

Revision in earnings estimates: We have reduced estimates for FY2024 and FY2025 to factor in slow recovery in the profitability of core businesses and break-even in some of the new businesses. Interest cost is expected to increase due to expected increase in the debt in the coming quarters.

Our Call

View – Downgrade to Hold with unchanged PT of Rs. 225: ABFRL's Q1FY24 performance was affected by sluggish sales growth due to weak demand in the branded apparel space. Management is expecting good recovery prior to start of festive season and expects strong recovery in the performance in H2FY2024. However, recovery in the EBIDTA margins will take time considering the enhanced competition in core businesses and slower improvement in profitability/break-even in the new businesses. Further, integration of the TCNS brands under the distribution chain of ABFRL, a fast scale-up in the ethnic wear business, consistent expansion in margins and GIC's infusion happening as per terms to complete the acquisition on time need to be monitored in the next 6-12 months. The stock has corrected by 41% from its high and is currently trading at valuation of 18x/14x its FY24E/25E EV/EBIDTA. In view of weak earning visibility in the near term, we downgrade our rating on the stock to Hold from Buy earlier with an unchanged PT of Rs. 225.

Key Risks

Any sustained slowdown in recovery due to weak demand environment in the branded apparel space in the coming quarters would act as a risk to our estimates in the near term.

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23	FY24E	FY25E
Revenue	8,136	12,418	14,386	17,322
EBITDA Margin (%)	13.5	12.0	11.5	12.2
Adjusted PAT	-121	-53	-224	31
Adjusted EPS (Rs.)	-1.2	-0.6	-2.2	0.3
P/B (x)	7.1	6.0	4.6	4.6
EV/EBITDA (x)	21.5	18.6	18.0	14.1
RoNW (%)	-	-	-	0.7
RoCE (%)	3.1	4.1	2.4	4.3

Source: Company; Sharekhan estimates

Weak Q1

ABFRL's consolidated revenue (including ethnic business) grew by 11.2% y-o-y to Rs. 3,196.1 crore, largely in line with ours and the average street's expectation of Rs. 3,161-3,174 crore. Standalone business grew by 7.7% y-o-y, with Madhura Fashion's (including Lifestyle brand) revenues growing by 11.2% y-o-y to Rs. 2,012 crore, while Pantaloons' revenue growth was muted at 1.1% y-o-y to Rs. 1,030 crore. Ethnic business grew by 33% y-o-y to Rs. 134 crore. Gross margins declined by 109 bps y-o-y to 54.8%, while EBITDA margin decreased by 715 bps y-o-y to 9.1% due to subdued demand and higher investments in subsidiaries. EBITDA margin slightly lagged our and average street expectation of 9.5-9.9%. EBITDA declined by 37.6% y-o-y to Rs. 292.3 crore. The company reported a loss of Rs. 162 crore against a PAT of Rs. 94 crore in Q1FY2023. We and the street had estimated a loss of Rs. 107-125 crore. Branded business added 28 stores (net), ethnic businesses added 12 stores and Pantaloons added 3 stores (net) during Q1, taking the store count to 4,008 at Q1FY2024-end.

All businesses impacted by weak demand environment

- **Madura Fashion & Lifestyle brands (MFL) - Business grew by 11% y-o-y:** MFL business (branded business of ABFRL) grew by 11% y-o-y with sales at Rs. 2,012 crore. EBITDA margin of MFL declined to 14.2% from 15.9% in Q1FY2023 impacted by negative operating leverage due to sluggish sales.
    - **Lifestyle business grew by 5% y-o-y:** Revenue grew by 5% y-o-y to Rs. 1,594 crore. EBITDA grew by 10% y-o-y to Rs. 292 crore with EBITDA margin at 18.3% (expansion of 80 bps y-o-y). During the quarter, brands strengthened their influence and leadership position through several impactful marketing campaigns. Brands added a net 28 stores to its network in Q1FY2024. The women's wear business maintained strong growth, with a 9% y-o-y increase. E-commerce registered 12% y-o-y growth. Wholesale revenues grew by 20% y-o-y to Rs. 376 crore led by departmental stores, while the retail business declined by 2% y-o-y to Rs. 809 crore, with LTL of -3%.
    - **Other businesses continued good trajectory:** Other businesses posted 44% y-o-y growth to Rs. 418 crore, driven by strong performance across segments. The segment reported a loss of Rs. 7 crore as against a profit of Rs. 21 crore in Q1FY2023. Inner wear & athleisure segment advanced with its aggressive growth strategy, recording a 3% retail LTL growth, despite the ongoing slowdown in the athleisure and activewear segment. During the quarter, the brand expanded its reach by adding over 700 Multi Brand Outlets (MBOs), bringing its total presence to ~32,700 trade outlets. In the Youth Fashion segment, American Eagle achieved a 49% y-o-y revenue growth, expanding its availability to 40 exclusive stores and over 65+ department stores, while, Forever 21 continued to prioritise operational efficiency and network rationalisation. Super premium brands, which include the multi-brand format 'The Collective' and other super-premium brands, delivered a solid performance in Q1, with a y-o-y revenue growth of 16%. The network posted a 16% retail LTL growth in Q1, led by strong connect with consumers, wide assortment of brands and products and high-quality service. Reebok revenue grew by 43% y-o-y, driven by a retail LTL of 11% and continued distribution expansion. The brand opened 10 new stores in Q1 and also continued to broaden its department store collaborations and marketplace partnerships. Management expects Reebok to be another large brand in core portfolio. Rebok is currently at break-even and is expected to be a profitable business in FY2024.

Madura Fashion and Lifestyle brands Rs cr

Particulars	Q1FY24	Q1FY23	y-o-y (%)	Q4FY23	q-o-q (%)
Lifestyle brands (a)	1,594.0	1,519.0	4.9	1,535.0	3.8
Other businesses (b)	418.0	290.0	44.1	392.0	6.6
Revenues (a+b)	**2,012.0**	**1,809.0**	**11.2**	**1,927.0**	**4.4**
EBITDA	285.0	287.0	-0.7	195.0	46.2
EBITDA Margin (%)	14.2	15.9	-170	10.1	405

Source: Company; Sharekhan Research

- **Pantaloons – Muted revenue growth at 1% y-o-y:** Pantaloons recorded sales of Rs. 1,030 crore, registering muted growth of 1% y-o-y with retail LTL at -8% impacted by a subdued demand environment across various markets. The private label portfolio showed promising results, with its overall share increasing to 65% from 62% in Q1FY2023. Pantaloons added 3 stores (net) during Q1. EBITDA stood at Rs. 138 crore with EBITDA margin at 13.4%.

Pantaloons' performance Rs cr

Particulars	Q1FY24	Q1FY23	y-o-y (%)	Q4FY23	q-o-q (%)
Revenues	1,030.0	1,019.0	1.1	798.0	29.1
EBITDA	138.0	220.0	-37.3	71.0	94.4
EBITDA Margin (%)	13.4	21.6	-819	8.9	450

Source: Company; Sharekhan Research

- **Ethnic wear business (part of the consolidated business) continued growth momentum –** The business grew 33% y-o-y to Rs. 134 crore driven by network expansion and brand development initiatives. Sabyasachi grew 18% y-o-y led by strong performance in jewelry & accessories segments (Jewelry grew 33% y-o-y). Men's premium ethnic wear brand TASVA added 7 stores in Q1, the brand is now available at 58 EBOs across 30+ cities. Shantnu & Nikhil posted 20% y-o-y growth as its bridge business 'S&N' grew to 1.6x of Q1FY2023. Shantnu & Nikhil added two new stores to the network in Q1, taking the total to 16 stores. House of Masaba added 3 stores to the network (total 11 stores at Q1FY2024-end), with retail business growing by 31% y-o-y. House of Masaba registered 32% y-o-y revenue growth led by 18% y-o-y growth in the fashion business.

Ethnic business performance Rs cr

Particulars	Q1FY24	Q1FY23	y-o-y (%)	Q4FY23	q-o-q (%)
Revenues	134.0	101.0	32.7	174.0	-23.0
EBITDA	-35.0	4.0	-	3.0	-

Source: Company; Sharekhan Research

Key conference call highlights

- **Demand to revive in H2FY24:** ABFRL witnessed gradual softening of demand after October 2022 (post festive season), with value segment being impacted severely. In terms of categories, wedding related consumption slowed due to fewer wedding dates and athleisure & lounge wear continued to drag. Overall, the company is seeing softness in the market and expects to start seeing recovery prior to festive season.
- **Margin recovery to take time:** EBIDTA margins would remain under pressure in the near term due to expected sluggish sales and sustained high investments in the ethnic and TMRW business.
- **Store addition pace lowered:** The management has decided to lower the pace of store additions in the coming quarters due to slowdown in the discretionary environment. The company will increase the store addition pace once the recovery is witnessed in the discretionary environment.
- **Debt to remain high:** Net debt on books increased to Rs. 2,100 crore to take working capital requirement, capital expenditure and losses in the emerging businesses. The same is expected to go up to Rs. 2,800 crore by FY2024-end post the acquisition of controlling stake in TCNS clothing.
- **Value fashion segment seeing good traction:** Management indicated that its value fashion segment, Styleup, is seeing good traction since its launch (7-8 months) Styleup added 5 new stores in Q1, taking the count to 15-16 stores at present. ABFRL is targeting 30-35 Styleup stores by FY2024-end.

Results (Consolidated) Rs cr

Particulars	Q1FY24	Q1FY23	Y-o-Y %	Q4FY23	Q-o-Q %
Total revenue	**3,196.1**	**2,874.8**	**11.2**	**2,879.7**	**11.0**
Cost of goods sold	1,446.0	1,269.4	13.9	1,273.8	13.5
Employee cost	437.6	347.4	26.0	414.0	5.7
Rent Expenses	226.8	208.9	8.5	214.7	5.6
Other expenditure	793.4	580.6	36.6	784.4	1.1
Total expenditure	**2,903.7**	**2,406.3**	**20.7**	**2,686.9**	**8.1**
EBITDA	**292.3**	**468.4**	**-37.6**	**192.8**	**51.6**
Other income	60.3	31.1	93.7	36.4	65.6
Interest & other financial cost	187.3	94.4	98.4	142.2	31.7
Depreciation	367.0	270.3	35.8	348.5	5.3
PBT	**-201.7**	**134.9**	**-**	**-261.5**	**-**
Tax	-39.7	41.1	-	-64.6	-
Adjusted PAT	-162.0	93.8	-	-196.9	-
Extraordinary items	0.4	0.6	-	2.4	-
Reported PAT	**-161.6**	**94.4**	**-**	**-194.5**	**-**
EPS (Rs)	**-1.7**	**1.0**	**-**	**-2.1**	**-**
			bps		**bps**
GPM (%)	54.8	55.8	-109	55.8	-101
EBITDA margin (%)	9.1	16.3	-715	6.7	245
NPM (%)	-5.1	3.3	-833	-6.8	177
Tax rate (%)	19.7	30.4	-	24.7	-503

Source: Company; Sharekhan Research

Results (Standalone) Rs cr

Particulars	Q1FY24	Q1FY23	Y-o-Y %	Q4FY23	Q-o-Q %
Total revenue	**2,987.2**	**2,774.0**	**7.7**	**2,651.3**	**12.7**
Cost of goods sold	1,395.4	1,252.2	11.4	1,231.4	13.3
Employee cost	351.4	302.1	16.3	343.3	2.3
Rent Expenses	222.9	206.5	7.9	210.3	6.0
Other expenditure	653.2	538.1	21.4	641.0	1.9
Total expenditure	**2,622.9**	**2,298.9**	**14.1**	**2,426.0**	**8.1**
EBITDA	**364.3**	**475.1**	**-23.3**	**225.3**	**61.7**
Other income	58.5	28.7	-	33.0	77.2
Interest & other financial cost	164.7	88.8	85.6	123.9	32.9
Depreciation	323.3	251.8	28.4	309.8	4.3
PBT	**-65.2**	**163.2**	**-**	**-175.4**	**-**
Tax	-16.6	39.6	-	-46.9	-
Adjusted PAT	-48.6	123.6	-	-128.5	-
EPS (Rs)	**-0.5**	**1.3**	**-**	**-1.4**	**-**
			bps		**bps**
GPM (%)	53.3	54.9	-157	53.6	-27
EBITDA margin (%)	12.2	17.1	-493	8.5	370
NPM (%)	-1.6	4.5	-608	-4.8	322
Tax rate (%)	25.5	24.3	118	26.7	-128

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Long-term growth prospects intact

Organic same-store-sales of retail companies is likely to be muted due to weak consumer sentiments as higher inflationary pressures affected demand, while revenue growth is expected to be largely driven by strong store expansion. We expect growth to be muted in H1FY2024 but expect it to gradually recover prior to the festive season. Branded retail & apparel companies are likely to benefit from 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 – Margin recovery will take time

ABFRL delivered weak performance in Q1FY2024 impacted by weak demand environment. Management expects demand to revive in H2FY2024 prior to the festive season, while margin improvement at the consolidated level will take time due to continued investments. Further, the net debt on books is expected to rise to Rs. 2,800 crore to fund the future capex, working capital requirement and acquire controlling stake in TCNS clothing. The company 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).

■ Valuation – Downgrade to Hold with an unchanged PT of Rs. 225

ABFRL's Q1FY24 performance was affected by sluggish sales growth due to weak demand in the branded apparel space. Management is expecting good recovery prior to start of festive season and expects strong recovery in the performance in H2FY2024. However, recovery in the EBIDTA margins will take time considering the enhanced competition in core businesses and slower improvement in profitability/break-even in the new businesses. Further, integration of the TCNS brands under the distribution chain of ABFRL, a fast scale-up in the ethnic wear business, consistent expansion in margins and GIC's infusion happening as per terms to complete the acquisition on time need to be monitored in the next 6-12 months. The stock has corrected by 41% from its high and is currently trading at valuation of 18x/14x its FY24E/25E EV/EBIDTA. In view of weak earning visibility in the near term, we downgrade our rating on the stock to Hold from Buy earlier with an unchanged PT of Rs. 225.

Peer Comparison

Particulars	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E
Trent	-	55.8	43.5	39.5	31.1	25.3	14.5	22.8	24.6
Shoppers Stop	72.7	94.9	37.5	14.8	13.8	10.7	9.9	9.3	15.3
ABFRL	-	-	-	18.6	18.0	14.1	4.1	2.4	4.3

Source: Company, Sharekhan estimates

About company

ABFRL is India's largest pure-play fashion and retail entity with a combined retail footprint of 10.8 million square feet, which includes 4,008 stores across approximately 33,874 multi-brand outlets with 6,837 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 FY2027.

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 & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Flipkart Inv Pvt Ltd	7.71
2	Nippon Life India Asset Management Company	2.53
3	ICICI Prudential Life Insurance Co.	2.06
4	Franklin Resources Inc	1.79
5	SBI Life Insurance Co Ltd	1.60
6	Tata AMC	1.48
7	Vanguard Group Inc	1.32
8	CALADIUM INVESTMENT PTE LTD	1.08
9	Aditya Birla AMC	1.05
10	Griffin Growth Fund	1.03

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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by BNP PARIBAS

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