

Company

17 November 2009 | 7 pages

Pantaloon (PART.BO)

Equity

Buy: Organisational Restructuring — Broad Contours Outlined

- What's new?** — PRIL management outlined a broad scheme for the de-merger of non retail assets. In brief: 1) Big Bazaar and Food Bazaar (~70% of FY09 PRIL parent revenues) will be transferred into a 100% subsidiary of PRIL. 2) The insurance ventures and Future Capital Holdings will be placed in a separate finance vertical. The holding company (for the insurance businesses) will be duly listed. 3) Three support businesses (IT, brand development and learning) have been carved out for a consideration of Rs1.9bn.
- Implications** — a) Positive for parent balance sheet – cash intensive financial services business can chart growth path without dependence on PRIL for capital infusion; b) Creates possibility for separate listing and infusion of FII into Big Bazaar + Food Bazaar at a later juncture (PRIL is at FII limit at present); and c) PRIL's resources to be conserved to meet growth aspirations.
- Other analyst meeting takeaways** — a) Timeline for restructuring of financial services business is 30-45 days; b) Balance sheet restructuring should result in debt to equity levels improving – management targets debt equity levels of ~0.8x (vs. ~1.2x now); c) Target to increase retail space to 25m sq ft by FY14, which includes 10m sq ft capex in PRIL (capital outlay of ~US\$350-400m); and d) Guidance on key metrics maintained – (i) management targets reducing inventory to ~Rs1600/sq ft, (ii) revenues of ~Rs9000/sq ft.
- Maintain Buy (1M)** — We expect the stock to remain buoyant as more clarity on the de-merger emerges. Improvement in retail business (solid SSS growth trends in October) also buttresses our thesis that PRIL is well positioned to capture the rebound in urban consumption.

Buy/Medium Risk	1M
Price (17 Nov 09)	Rs323.10
Target price	Rs370.00
Expected share price return	14.5%
Expected dividend yield	0.1%
Expected total return	14.6%
Market Cap	Rs56,346M US\$1,225M

Price Performance (RIC: PART.BO, BB: PF IN)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
30 Jun	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2007A	1,200	8.18	68.2	39.5	4.3	14.8	0.2
2008A	1,260	7.91	-3.3	40.9	2.8	8.6	0.1
2009E	1,402	7.37	-6.8	43.8	2.7	6.8	0.1
2010E	2,404	12.63	71.4	25.6	2.5	10.1	0.2
2011E	3,501	18.40	45.6	17.6	2.2	13.2	0.2

Source: Powered by dataCentral

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Figure 1. Pantaloon Retail (Consolidated) – Balance Sheet Summary (RsM)

As of June 30	2008	2009
SOURCE OF FUNDS		
Net-Worth	22,270	25,000
Loans Funds	27,670	38,580
Minority Interest	4,060	3,850
Deferred Tax	350	40
TOTAL	54,360	67,470
APPLICATION OF FUNDS		
Fixed Assets	16,710	22,010
CWIP	3,840	4,300
Investment	7,260	8,980
Current Assets	38,330	46,230
Current Liability	11,780	14,050
Net Current Assets	26,550	32,180
TOTAL	54,360	67,470
Net Working Capital	26,550	32,180
Debt/Equity (X)	1.24	1.54

Source: Company Reports

Figure 2. Pantaloon Retail (Consolidated) – Income Statement Summary (RsM)

	FY08	FY09	% Change Y/Y
Net Sales	58,405	76,690	31.3
Total Expenditure	-55,366	-71,569	29.3
EBITDA	3,039	5,122	68.5
<i>EBITDA Margin (%)</i>	<i>5.2</i>	<i>6.7</i>	<i>147 bps</i>
Interest	-2,236	-4,185	87.2
Depreciation	-1,182	-2,066	74.7
Other Income	557	958	71.8
PBT	179	-172	nm
Tax	-473	100	nm
<i>Tax Rate (%)</i>	<i>264.6</i>	<i>57.9</i>	<i>nm</i>
PAT	-294	-72	-75.4
Minority Interest, Share of Associates and prior period items	514	173	-66.3
Reported Profit	219	101	-54.1

Source: Company Reports

Figure 3. Pantaloon – Performance of Key Subsidiaries in FY09

	PRIL Stake (%)	Net Sales (RsM)	EBITDA (RsM)	EBITDA Margin (%)	Capital Employed (RsM)	EBITDA/Capital Employed
Future Capital	54.8%	1,360	428	31.5%	12,170	3.5%
Home Solutions	66.9%	10,710	(364)	-3.4%	6,740	-5.4%
Future Agrovet	96.2%	3,910	16	0.4%	610	2.6%
Future Logistics	94.2%	1,940	103	5.3%	350	29.4%
Future Media	84.2%	460	(60)	-13.0%	420	-14.2%
Future Knowledge Services	100.0%	470	14	3.0%	450	3.1%
Future e-Commerce Infrastructure	72.0%	1,180	(242)	-20.5%	540	-44.8%

Source: Company Reports

Pantaloon

Company description

Pantaloon is the largest organized modern-format retailer in India, with a presence in apparel, general merchandise, home products and food retailing. It has retail space of about 9m sq. ft. (including Home Retail) with plans to expand to 25m sq. ft. by FY11. Pantaloon retails fashion apparel and accessories through its Pantaloon stores, and general merchandise and food through discount department stores Big Bazaar and Food Bazaar. It has a presence in retail property management services through Central Malls, managing retail space for concessionary fees and a share of sales. It has recently launched Home Town for home interiors, which it plans to expand aggressively. Its real estate investment subsidiary, Kshitij Retail Destinations plans to set up 51 malls across India spanning 14.5m sq. feet in the next three years. Pantaloon also has interests in media, logistics, brand management and e-tailing, through subsidiaries.

Investment strategy

We rate Pantaloon Retail (India) Buy/Medium Risk (1M). The sequential improvements in same store sales trends in both value and lifestyle retailing have been encouraging and are signs of improving discretionary consumption. Concerns relating to paucity of capital have abated as fresh infusion of capital will lower high gearing ratios and aid PRIL's expansion plans. Operationally, PRIL will benefit from management's strategy of outsourcing non-core operations, lower employee costs and lower rentals rates. Improving operating leverage and cost efficiencies should lead to healthy margin expansion of ~150bps and strong net profit growth of ~58% over FY09-11E, on our estimates.

Valuation

Our Rs370 target price is based on a sum of the parts approach. We value Pantaloon at 20x Dec-10E PE, which gives us Rs310/share. Our target multiple of 20x is set at around a c.20% premium to the average for the regional peer group, to reflect the higher earnings growth profile for Pantaloon. Home Solutions is valued at Rs23/share (based on 0.6x Dec-10E EV/sales - in line with global peers), and Future Capital is valued at Rs20/share (at 1.3x FY09 P/B). A 20% holding company discount has been ascribed for both Home Solutions and Future Capital. We add Rs17/share for Future Logistics, applying a 20% discount to the valuation of the recent transaction by Li & Fung.

Risks

We assign a Medium Risk rating to Pantaloon Retail based on our quantitative risk-rating system. The main downside risks to our target price include: 1) Initial trend of encouraging sales growth fades away; 2) Delay in store opening plans; 3) Increase in competitive intensity and/or irrational competition; and 4) Any pressure on rentals, which could result in lower than expected margins. The main upside risks to our target price and estimates include: 1) Value unlocking in subsidiaries through listing / stake sales, 2) Any significant acquisitions, JVs or partnerships perceived to be creating value; and 3) Legislative changes that allow FDI in retail could be perceived as a sentiment positive from a funding perspective.

Appendix A-1

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Pantaloen (PART.BO)

Ratings and Target Price History

Fundamental Research

Analyst: Jamshed Dadabhoy

Covered since May 6 2008



Chart current as of 14 November 2009

Date	Rating	Target Price	Closing Price
1 20-Apr-07	*1M	*500.00	400.70
2 5-Jun-07	1M	*545.00	437.90
3 13-Sep-07	1M	*626.00	507.10
4 23-Jan-08	*3M	*520.00	644.95
5 14-Jan-09	3M	*184.00	189.70
6 26-Apr-09	3M	*180.00	202.05
7 18-Aug-09	*1M	*370.00	299.10

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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Data current as of 30 Sep 2009

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