



Pantaloon Retail

STOCK INFO.	BLOOMBERG
BSE SENSEX: 12,907	PF IN
	REUTERS CODE
S&P CNX: 3,739	PART.BO

27 October 2006

Buy

Previous Recommendation: Buy

Rs1,860

Equity Shares (m)	26.9
52-Week Range	2,060/1,080
1,6,12 Rel. Perf. (%)	-4/-14/-25
M.Cap. (Rs b)	49.9
M.Cap. (US\$ b)	1.1

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
06/06A	18,678	642	23.9	31.6	77.8	12.6	16.2	15.3	2.9	37.6
06/07E	30,960	1,113	41.4	73.5	44.8	9.6	21.4	16.5	1.8	22.9
06/08E	53,388	2,117	75.3	82.0	24.6	5.8	23.3	20.07	1.1	13.3

- Pantaloon's 1QFY07 results were below expectations, with the company reporting adjusted PAT of Rs162m against our estimate of Rs228m.
- Sales for the quarter grew 65.4% YoY to Rs6b, driven largely by strong growth in the value retailing segment. The company's value retailing ventures (Big Bazaar and Food Bazaar) grew 78% YoY; while its lifestyle retailing ventures (Pantaloon and Central Mall) grew 50% YoY.
- EBITDA margins declined by 80bp YoY to 6.9%, despite 120bp increase in gross margins as staff costs jumped by 144% (to 7.5% of sales from 5.1% in 1QFY06 due to new staff addition in planned formats). Management expects staff cost to decline in the coming quarters, as new stores are commissioned. We expect the retail space addition to accelerate, as the company is likely to add more than 1m sq ft in 2QFY07.
- The company has divested 20% stake in Home Solutions Retail to ICICI Venture and Kotak Private Equity for Rs1.7b, valuing the company at Rs10b. It plans to unlock value from eight more subsidiaries, with a target to raise Rs10b.
- Acceleration in store opening and value unlocking in subsidiaries will act as key triggers in the coming quarters. We believe that the company continues to be the best play on the expected growth in organized retail in India. The stock is currently valued at 44.8x FY07E earnings and 24.6x FY08E earnings. We maintain **Buy**.

QUARTERLY PERFORMANCE

(Rs Million)

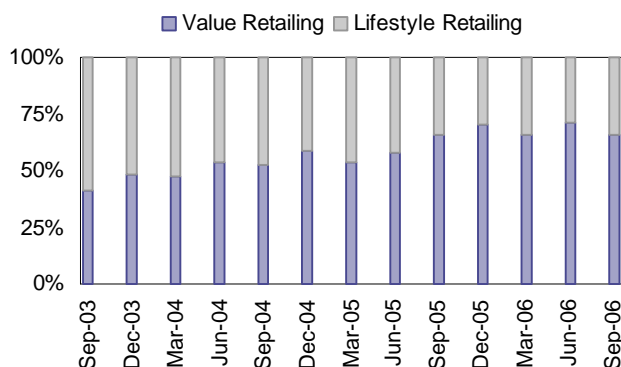
Y/E JUNE	FY06				FY07E				FY06	FY07E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q		
Net Sales	3,648	4,720	4,554	5,752	6,034	7,600	8,000	9,326	18,678	30,960
YoY Change (%)	81.4	81.4	98.0	65.6	65.4	61.0	75.7	62.2	72.3	65.8
Total Exp	3,368	4,341	4,169	5,379	5,618	7,020	7,340	8,512	17,257	28,490
EBITDA	280	379	385	373	415	580	660	815	1,420	2,470
Margins (%)	7.7	8.0	8.5	6.5	6.9	7.6	8.3	8.7	7.6	8.0
Depreciation	-38	-46	-59	-66	-67	-70	-90	-89	-208	-316
Interest	-57	-79	-101	-98	-125	-130	-155	-173	-335	-583
Other Income	7	4	5	30	17	4	5	-8	42	19
PBT	192	258	230	239	241	384	420	545	919	1,590
Tax	-57	-72	-68	-80	-79	-120	-114	-164	-277	-477
Rate (%)	29.7	28.0	27.0	33.6	32.7	31.3	27.1	30.1	30.2	30.0
Adjusted PAT	135	186	162	158	162	264	306	381	642	1,113
	95.0	83.0	52.0	43.5	19.6	42.2	88.5	140.5	65.4	73.5
Exceptional Income	0	0	0	0	224	0	0	0	0	224
Reported PAT	135	186	162	158	386	264	306	381	642	1,337
YoY Change (%)					185.7	42.2	88.5	140.5	65.4	108.4

E: MOST Estimates

Value retailing driving overall revenue growth; margins likely to expand

Pantaloon's 1QFY07 revenues grew 65.4% YoY to Rs6b, driven by the value retailing segment (Big Bazaar and Food Bazaar). Value retailing grew 78% YoY for the quarter, while lifestyle segment revenues grew 50%. Value retailing reported 16bp margin expansion in 1QFY07, reflecting the rising impact of private labels and economies of scale. The trend looks encouraging especially as the store area increase has been relatively higher for the Food Bazaar format (15% gross margins) as against Big Bazaar format (25% gross margin) in value retailing. Lifestyle retailing reported 100bp decline in PBIT margins, indicating the impact of monsoon sales in Pantaloon stores.

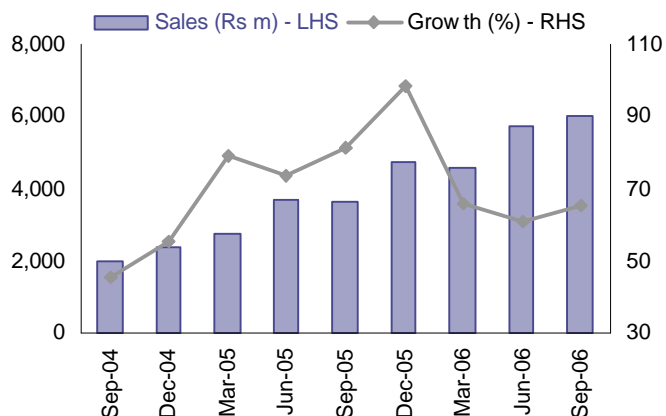
SALES MIX: INCREASING CONTRIBUTION OF VALUE RETAILING



Source: Company/ Motilal Oswal Securities

We expect value retailing to continue driving revenue growth during FY07 due to higher store addition in this format. The company plans to add more than 1m sq ft space in 2QFY07, across formats including Central and Home Town. We expect overall margins to improve in the coming years, as Pantaloon's sales mix tilts towards private labels and brands of associate companies. In addition, higher economies of scale will also enable the company to have better sourcing arrangements, which would boost reported profitability.

QUARTERLY SALES TREND

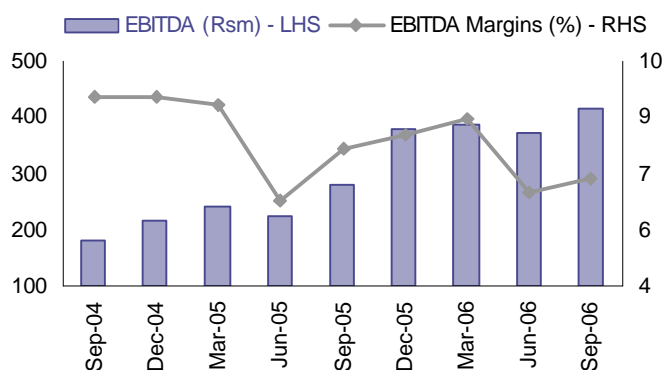


Source: Company/ Motilal Oswal Securities

Higher staff cost hurts EBITDA margins

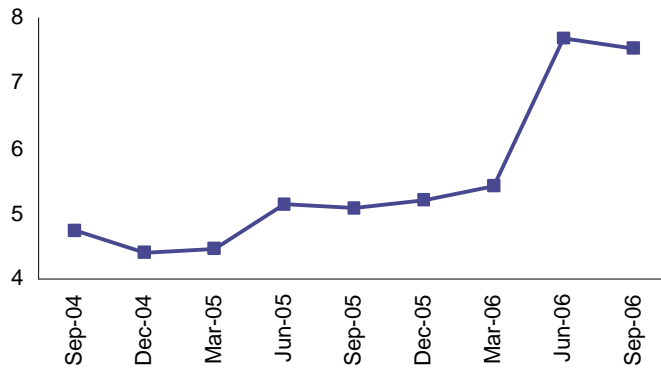
Pantaloon reported 80bp decline in EBITDA margin in 1QFY07 due to 144% jump in staff cost, which increased from 5.1% of sales to 7.5%. Increased hiring of new staff for the upcoming retail stores and new formats (Electronics, Health and Beauty, etc.) contributed to the increase in staff cost. On a sequential basis, staff cost as a percentage of sales declined 20bp but was up marginally in absolute terms. Management expects staff cost as a percentage of sales to decline in the coming quarters, as new store opening is expected to gain momentum.

QUARTERLY EBITDA TREND



Source: Company/ Motilal Oswal Securities

STAFF COST AS A PERCENTAGE OF SALES TRENDING UP



Source: Company/ Motilal Oswal Securities

Subsidiaries to unlock value; capital infusion to aid expansion
Pantaloon undertook value unlocking in its subsidiaries, as it allotted 15% stake to ICICI Venture in Home Solutions Retail. In addition, it divested with 5% of its stake to Kotak Private Equity for Rs500m, valuing the business at Rs10b. The company plans to unlock value in 8 more subsidiaries,

which include Futures Capital and Future Logistics. The management expects to conclude a couple of more deals in 2QFY07. We expect these stake sales to enable the company to expand the core business operations. Value unlocking in subsidiaries (Rs10b) and Rs4.5b issue of shares will fulfill the funds requirement for the coming couple of years. This coupled with already established tie-ups for real estate would hold the company in good stead in the coming years.

Valuation and view

Acceleration in store opening and value unlocking in subsidiaries will act as key triggers in the coming quarters. We believe that the company continues to be the best play on the expected growth in organized retail in India. The stock is currently valued at 44.8x FY07E earnings and 24.6x FY08E earnings. We maintain **Buy**.

Pantaloon Retail: an investment profile

Company description

Pantaloon Retail is the largest organized retailer in India with retail space of more than 2.7m sq. ft. Pantaloon retails multiple categories through different format offerings like departmental stores (Pantaloon), hypermarkets (Big Bazaar), seamless mall (Central) and Food bazaars (Grocery stores).

Key investment arguments

- ☞ Pantaloon is the best play in the fast-growing organized retail market due to rapid scale up in operations, tied up real estate and established retail formats.
- ☞ The Company has set up a clutch of subsidiaries in Real estate and Private equity management, logistics, joint ventures for insurance and various retail formats which unlock substantial value in the coming few years.

Key investment risks

- ☞ High inventory levels, slippages in development of real estate and unrelated diversification into areas like insurance.

Recent developments

- ☞ Announced 5:1 stock split, issue of 12m shares to promoters and Rs2.6b preferential issue.
- ☞ plans to unlock value in subsidiaries by raising Rs5b.

Valuation and view

- ☞ We forecast EPS to be Rs41.4 for FY07E and Rs75.3 for FY08E based on diluted equity after issue to promoters.
- ☞ The stock is currently valued at 44.8x FY07E earnings and 24.6x FY08E earnings. We maintain **Buy**.

Sector view

- ☞ We are positive on the retail sector. We expect the sector to clock revenue growth of 30%-35% CAGR over the next five years.
- ☞ Players such as Pantaloon Retail with a strong hypermarket format and presence in larger number of categories are likely to be bigger winners.
- ☞ Long term prospects appear bright, given low store penetration and rising consumers' incomes.

COMPARATIVE VALUATIONS

		PANTALOOON	SHOPPERS	TITAN
P/E (x)	FY07E	44.8	58.3	33.6
	FY08E	24.6	46.2	22.0
EV/EBITDA (x)	FY07E	22.9	29.1	19.1
	FY08E	13.3	21.4	13.4
EV/Sales (x)	FY07E	1.8	2.4	1.8
	FY08E	1.1	1.8	1.4
P/BV (x)	FY07E	9.6	6.6	14.4
	FY08E	5.8	6.0	11.9

SHAREHOLDING PATTERN (%)

	SEP-06	JUN-06	SEP-05
Promoter	44.2	44.2	43.1
Domestic Inst	6.6	6.7	2.7
Foreign	28.6	28.7	30.7
Others	20.5	20.4	23.5

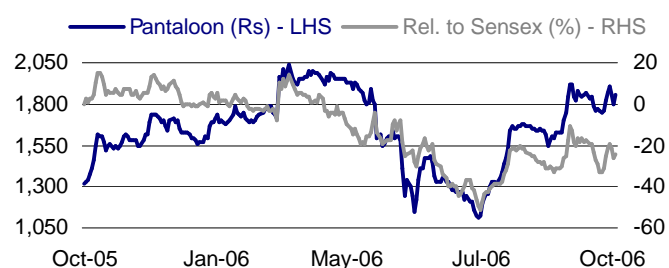
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY07	41.4	46.1	-10.2
FY08	75.3	75.3	-

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
1,860	2,025	8.9	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT		(RS MILLION)				
Y/E JUNE	2005	2006AE	2007E	2008E	2009E	
Net Sales	10,840	18,678	30,960	53,388	82,892	
Change (%)	64.7	72.3	65.8	72.4	55.3	
Total Expenditure	-9,944	-17,257	-28,490	-49,047	-75,897	
EBITDA	896	1,420	2,470	4,341	6,995	
Change (%)	62.9	58.5	73.9	75.8	61.1	
Margin (%)	8.3	7.6	8.0	8.1	8.4	
Depreciation	-133	-208	-316	-463	-621	
Int. and Fin. Charges	-275	-335	-583	-874	-1,155	
Other Income - Recurring	43	42	19	20	22	
Profit before Taxes	531	919	1,590	3,025	5,241	
Change (%)	117.7	73.0	73.0	90.2	73.3	
Margin (%)	4.9	4.9	5.1	5.7	6.3	
Tax	-145	-277	-477	-907	-1,730	
Tax Rate (%)	-27.4	-30.2	-30.0	-30.0	-33.0	
Profit after Taxes	386	642	1,113	2,117	3,512	
Change (%)	94.4	66.4	73.5	90.2	65.9	
Margin (%)	3.6	3.4	3.6	4.0	4.2	
Extraordinary Items	13	0	224	0	0	
Reported PAT	399	642	1,337	2,117	3,512	

BALANCE SHEET		(RS MILLION)				
Y/E JUNE	2005	2006E	2007E	2008E	2009E	
Share Capital	220	269	269	281	281	
Reserves	1,965	3,692	4,939	8,790	12,113	
Net Worth	2,185	3,961	5,208	9,071	12,394	
Loans	2,862	4,019	7,451	9,300	12,793	
Deferred Tax	130	224	510	1,054	2,092	
Capital Employed	5,178	8,204	13,169	19,426	27,280	
Gross Block	2,511	3,739	5,985	8,259	10,848	
Less: Accum. Deprn.	-374	-446	-762	-1,225	-1,846	
Net Fixed Assets	2,137	3,292	5,222	7,033	9,001	
Capital WIP	158	246	268	417	456	
Investments	319	195	195	195	195	
Curr. Assets, L&A	4,039	6,688	11,094	18,312	27,968	
Inventory	2,759	4,590	7,559	12,316	19,150	
Account Receivables	123	251	497	860	1,338	
Cash and Bank Balance	215	249	695	1,079	1,540	
Others	941	1,597	2,343	4,056	5,941	
Curr. Liab. and Prov.	1,448	2,220	3,612	6,533	10,342	
Other Liabilities	1,265	1,928	3,175	5,758	8,952	
Provisions	183	292	437	775	1,389	
Net Current Assets	2,591	4,468	7,482	11,779	17,627	
Miscellaneous Expenditure	3	3	2	1	0	
Application of Funds	5,178	8,204	13,169	19,426	27,279	

E: MOST Estimates

RATIOS						
Y/E JUNE	2005	2006E	2007E	2008E	2009E	
Basic (Rs)						
EPS	18.1	23.9	41.4	75.3	124.9	
Cash EPS	23.6	316	53.2	918	147.0	
BV/Share	99.3	147.3	193.7	322.8	441.0	
DPS	2.5	2.5	3.0	4.0	6.0	
Payout %	13.8	10.5	7.2	5.3	4.8	
Valuation (x)						
P/E	102.3	77.8	44.8	24.6	14.9	
Cash P/E	78.7	58.7	34.9	20.2	12.6	
EV/Sales	4.8	2.9	1.8	1.1	0.7	
EV/EBITDA	58.3	37.6	22.9	13.3	8.7	
P/BV	18.7	12.6	9.6	5.8	4.2	
Dividend Yield (%)	0.1	0.1	0.2	0.2	0.3	
Return Ratios (%)						
RoE	17.6	16.2	21.4	23.3	28.3	
RoCE	15.6	15.3	16.5	20.1	23.4	
Working Capital Ratios						
Debtor (Days)	4	5	6	6	6	
Asset Turnover (x)	2.1	2.3	2.4	2.7	3.0	
Leverage Ratio						
Debt/Equity (x)	13	10	14	10	10	

CASH FLOW STATEMENT		(RS MILLION)				
Y/E JUNE	2005	2006E	2007E	2008E	2009E	
OP/(loss) before Tax	763	1,212	2,154	3,878	6,374	
Int./Div. Received	43	42	19	20	22	
Depreciation and Amort.	133	208	316	463	621	
Interest Paid	-275	-335	-583	-874	-1,155	
Direct Taxes Paid	-145	-277	-477	-907	-1,730	
(Incr)/Decr in WC	-948	-1,843	-2,568	-3,913	-5,387	
CF from Operations	-429	-994	-1,139	-1,333	-1,254	
Extraordinary Items	13	0	224	0	0	
(Incr)/Decr in FA	-677	-1,315	-2,269	-2,423	-2,628	
(Pur)/Sale of Investments	-267	125	0	0	0	
CF from Invest.	-931	-1,191	-2,045	-2,423	-2,628	
Issue of Shares	0	0	0	0	0	
(Incr)/Decr in Debt	501	1,157	3,432	1,849	3,493	
Dividend Paid	-63	-90	-90	-126	-189	
Others	998	1,152	288	2,417	1,039	
CF from Fin. Activity	1,436	2,219	3,630	4,140	4,343	
Incr/Decr of Cash	76	34	446	384	461	
Add: Opening Balance	138	215	249	695	1,079	
Closing Balance	215	249	695	1,079	1,540	

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Disclosure of Interest Statement	Pantaloon Retail
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No

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