



Pantaloon Retail

STOCK INFO.	BLOOMBERG
BSE SENSEX: 17,016	PF IN
	REUTERS CODE
S&P CNX: 5,090	PART.BO

28 April 2008

Buy

Previous Recommendation: Buy

Rs506

		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
Equity Shares (m)	151.0	06/07A	32,367	611	4.2	-11.2	121.7	6.8	5.6	7.4	2.6	39.6
52-Week Range (Rs)	875/380	06/08E	53,536	1,309	8.9	114.4	56.8	5.7	10.0	10.2	1.7	20.7
1,6,12 Rel. Perf. (%)	12/-5/0	06/09E	80,324	2,138	14.2	59.0	35.7	5.1	14.2	13.1	1.1	14.6
M.Cap. (Rs b)	76.5	06/10E	109,904	3,585	21.0	48.0	24.1	3.0	12.4	14.3	0.8	10.1
M.Cap. (US\$ b)	1.9											

- ✎ The 3QFY08 results are below estimates with sales (Rs13.6b v/s est. of Rs14.2b) and adj. PAT (Rs321m v/s est. of Rs359m). Gross margin declined 280bp to 29.7% while EBIDTA margin expanded 140bp to 8.4% (est. 8%) due to 340bp decline in overheads and 80bp decline in staff costs. EBIDTA at Rs1.14b is in line but higher depreciation (Rs223m v/s est. 185m) and tax rate (36.6% v/s est. of 34%) limited PAT growth to 71.5% (est. of 91.6%).
- ✎ Lifestyle retailing (30% of sales) and Value retailing (70% of sales) had same-store sales growth in high single digits and below teens. Same-store sales growth is expected to stabilize in mid-to-high single digits due to more store openings in existing cities and faster store rollouts.
- ✎ The company opened 20 stores in various formats adding 0.6m sq. ft. of retail space, taking total retail space to 7.3m sq. ft. Pantaloon has indicated acceleration in new real estate bookings due to softening of lease rentals.
- ✎ The company is expected to provide for one-time exceptional expense (Rs700m-800m) for higher inventory value of past years. The change in valuation method (from MRP less discounts to cost price) will have an EBIDTA margin impact 30bp in FY09. We are factoring in 20bp higher EBIDTA margin and higher depreciation for FY08. We are reducing FY08 and FY09 PAT estimates by 3.7% and 11.2% to Rs1.31b and Rs2.14b respectively. Our revised EPS for FY08 and FY09 stands at Rs8.9 (v/s Rs9.3 earlier) and Rs14.2 (v/s Rs16.0 earlier).
- ✎ We believe Pantaloon is in a sweet spot based on: (1) having tied up real estate at a reasonable cost, which will ensure fast expansion for coming two years; (2) fully funded for up to 2-3 years of expansion plans. We expect sales and PAT to increase at 44% and 65% over FY08-10. We value the retail business at Rs433 per share and other business stakes at Rs206 per share. Potential value unlocking in insurance (which might require further capital) is not captured in our estimates. We maintain **Buy** with a target price of Rs639, a 33% upside.

QUARTERLY PERFORMANCE

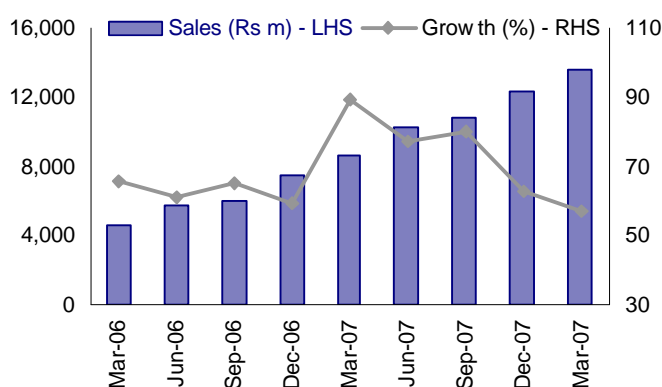
Y/E JUNE									(Rs Million)	
	FY07				FY08				FY07	FY08E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Net Sales	6,034	7,527	8,610	10,196	10,864	12,268	13,543	16,860	32,367	53,536
YoY Change (%)	65.4	59.5	89.1	77.3	80.1	63.0	57.3	65.4	73.3	65.4
Total Exp	5,618	6,957	8,008	9,629	9,908	11,171	12,402	15,707	30,211	49,188
EBITDA	415	570	603	568	956	1,096	1,141	1,153	2,156	4,347
Margins (%)	6.9	7.6	7.0	5.6	8.8	8.9	8.4	6.8	6.7	8.1
Depreciation	67	82	93	126	153	204	223	221	369	801
Interest	125	207	229	337	352	418	429	421	898	1,619
Other Income	17	5	9	0	7	13	17	20	32	57
PBT	241	286	290	105	459	487	506	531	921	1,983
Tax	79	94	103	36	162	171	185	156	311	674
Rate (%)	32.7	33.0	35.5	34.0	35.3	35.1	36.6	29.4	33.7	34.0
Adjusted PAT	162	191	187	69	297	317	321	375	611	1,309
YoY Change (%)	19.6	3.1	15.3	-56.2	82.9	65.3	71.5	440.3	-3.0	114.4
Exceptional Income	224	249	0	117	0	0	0	0	589	0
Repoorted PAT	386	440	187	187	297	317	321	375	1,200	1,309

E: MOSSt Estimates

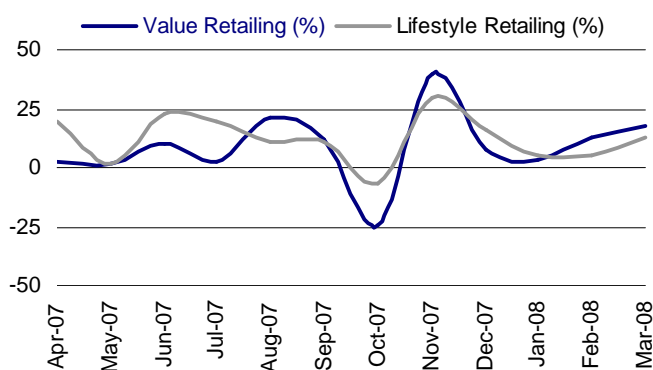
Same-store sales to settle at high single digits; food margins under pressure

3QFY08 revenues grew 57.3% YoY to Rs13.5b, although short of our estimates of Rs14.2b. Same-store sales in lifestyle retailing grew in high single digits while value retailing increased in low teens. Lifestyle retailing accounted for 30% of sales while value retailing accounted for 70% of sales. Gross margins declined 280bp YoY and 70bp QoQ to 29.7% due to margin pressure in food and grocery although apparel profitability has improved. We expect gross margins to come under further pressure due to sharp rise in prices of food articles. Although same store sales growth is indicating an increasing trend from past two months; it is expected to stabilize in high single digits due to more store openings in existing cities and expected increase in store openings.

FOCUS ON PROFITABLE GROWTH IMPACT REVENUES

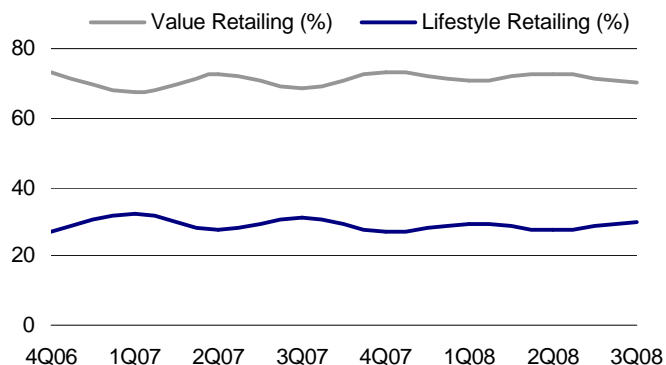


PICKUP IN SAME STORES SALES GROWTH

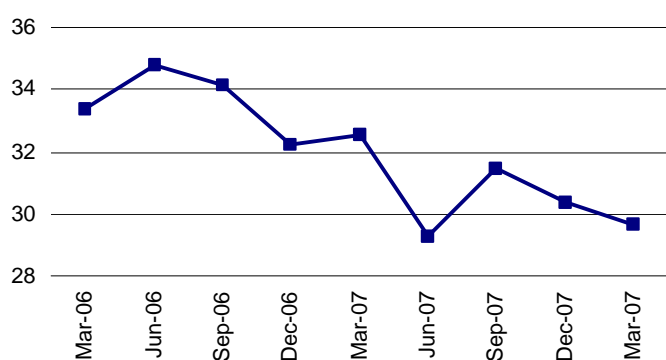


Source: Company/Motilal Oswal Securities

SALES MIX VALUE RETAILING AND LIFE STYLE



DECLINING GROSS MARGINS (%)



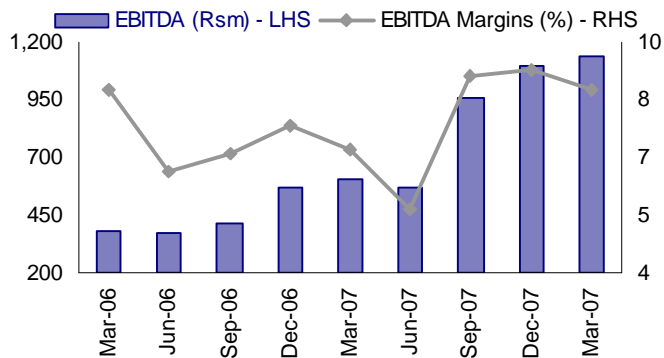
Source: Company/Motilal Oswal Securities

Operating leverage to sustain; store openings remain steady

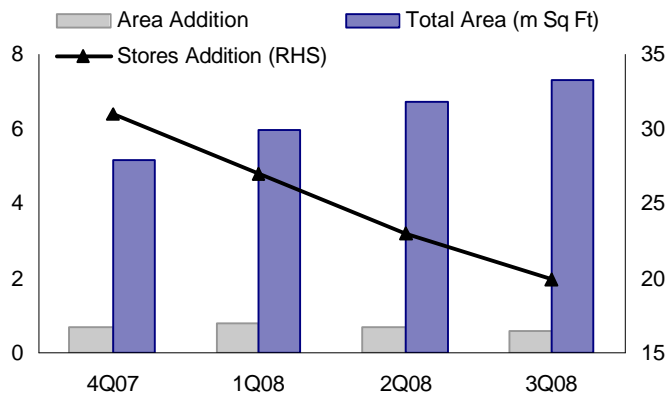
Pantaloon reported 140bp increase in EBIDTA margins despite 280bp decline in gross margins, as operating leverage due to rising scale resulted in 80bp and 340bp decline in staff and overhead costs. Staff costs declined 30bp QoQ while overheads increased 20bp QoQ. New store sales have been declining as a percentage of total sales, which indicates the chief reason for the buoyancy in operating leverage.

Pantaloon added 0.6m sq. ft. of retail space in 3QFY08 taking total retail space to 7.3m sq. ft. The company added 22 stores in the quarter. We expect the company to end the current year with 8m sq. ft. of retail space. The company has added 2.1m sq. ft. in 9mFY08, which indicates that even at the current rate the company would achieve close to 11m sq. ft. by FY09. Sharp increase in retail space will provide economies of scale in sourcing and distribution.

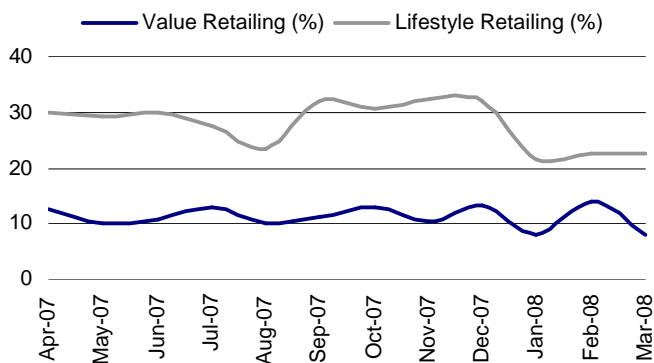
EBITDA MARGIN SHOWS STEADY GROWTH



STEADY TREND IN AREA ADDITION



NEW STORE SALES (% OF TOTAL SALES)



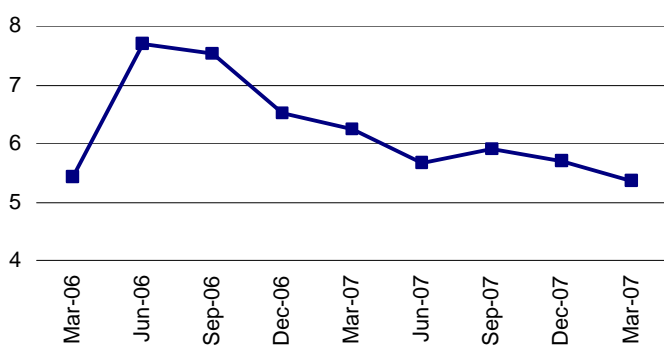
Source: Company/Motilal Oswal Securities

Inventory valuation to be changed; real estate bookings might accelerate

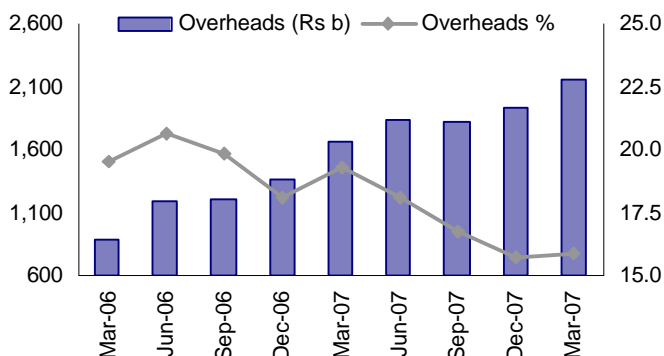
Pantaloon values the closing stock at market price less discounts rather than the cost price which overvalues the closing stock and shows higher profits. The company is expected to start following the cost method from FY09 and will provide for one-time exceptional expense for higher inventory value of past years, which is expected to be Rs700-800m. The change in valuation method will have an EBITDA margin impact of 30-50bp from FY09, a part of this impact would be neutralized from operating leverage.

Pantaloon had gone slow on new bookings of real estate (5 bookings in 6 months) as the lease rentals had increased to Rs80-100per sq. ft. The company has indicated its intention to increase the bookings, as real estate deals are becoming more favorable much earlier than their expectations.

TREND IN STAFF COSTS (%)



TREND IN OVERHEADS EXPENSES



Outlook: Reducing estimates; maintain Buy with SOTP-based target price of Rs639

We are incorporating 30bp EBITDA margin contraction in FY09 due to change in method of inventory valuation. In addition we are factoring in 20bp higher EBITDA margin and higher depreciation for FY08. We are reducing FY08 and FY09 PAT estimates by 3.7% and 11.2% to Rs1.31b and Rs2.14b. Our revised EPS for FY08 and FY09 stands at Rs8.9 (v/s Rs9.3 earlier) and Rs14.2 (v/s Rs16.0 earlier).

Source: Company/Motilal Oswal Securities

We believe that Pantaloon is in a sweet spot due to: (1) having tied up real estate at a reasonable cost, which will ensure fast expansion for coming two years and enable the company to maintain market leadership; (2) the company being fully funded for the 2-3 years of expansion plans versus most other retailers who are yet to tie up their funds. We expect PRIL sales and PAT to increase at 44% and 65% over FY08-10. We value the retail business at Rs433 per share and other business stakes at Rs206 per share. Moreover success in large businesses like insurance (which might require further capital) can unlock value over the coming 3-4 years, which is not captured in our estimates. We maintain **Buy** with a target price of Rs639, a 33% upside.

SOTP (RS M)				
	STAKE (%)	TOTAL VALUE	PRIL SHARE	RS/ SHARE
Retailing	100	73,797	73,797	433
Home Solutions	85	19,533	16,603	97.1
Future Capital	55	24,143	13,278	77.7
Future Media	90	2,000	1,800	10.5
Future Bazaar	75	3,200	2,400	14.0
Future Generali Life	58	1,000	580	3.4
Future Generali General	58	1,000	580	3.4
Total			109,038	639

Source: Motilal Oswal Securities

Pantaloon Retail: an investment profile

Company description

Pantaloon Retail is the largest organized retailer in India with a retail space of more than 2m square feet under its belt. Pantaloon retails multiple categories through different format offerings like departmental stores (Pantaloon), hypermarkets (Big Bazaar), seamless mall (Central) and standalone stores. The company is targeting revenues of US\$2b in FY09, a 68% CAGR over FY05-09.

Key investment arguments

- ✍ Pantaloon is the best play on organized retail play and is planning to increase retail space under its coverage from 5.5m sq ft to more than 11m sq ft by FY08.
- ✍ The company is in the process of unlocking value from listing of shares in Future Capital and Future Ventures. It has already sold minority stakes in Home Solutions and Future Bazaar. We estimate the value of its investments at Rs284 per share.

Key investment risks

- ✍ Pantaloon has an aggressive expansion plan where a timely and profitable execution is a critical issue.
- ✍ Pantaloon has a aggressive inventory valuation practice where in-store inventory at 'retail price less mark-up' as opposed to the usual 'lower of cost or market price'.

COMPARATIVE VALUATIONS

		PANTALOOON	SHOPPERS	TITAN
P/E (x)	FY09E	35.7	139.3	27.4
	FY10E	24.1	40.4	20.8
EV/EBITDA (x)	FY09E	14.6	16.3	16.3
	FY10E	10.1	10.6	12.6
EV/Sales (x)	FY09E	1.1	1.0	1.3
	FY10E	0.8	0.8	1.1
P/BV (x)	FY09E	5.1	4.7	8.7
	FY10E	3.0	4.4	6.5

SHAREHOLDING PATTERN (%)

	MAR-08	DEC-07	MAR-07
Promoter	45.0	43.5	42.3
Domestic Inst	13.1	12.0	11.6
Foreign	24.7	25.3	27.3
Others	17.2	19.3	18.8

Recent developments

- ✍ Huge response to the IPO of Future Capital.
- ✍ Pantaloon will convert various retail formats into separate companies to increase operational efficiency.

Valuation and view

- ✍ Our revised EPS for FY08 and FY09 stands at Rs8.9 (v/s Rs9.3 earlier) and Rs14.2 (v/s Rs16.0 earlier).
- ✍ We maintain **Buy** with revised SOTP-based target price of Rs639, a 33% upside.

Sector view

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

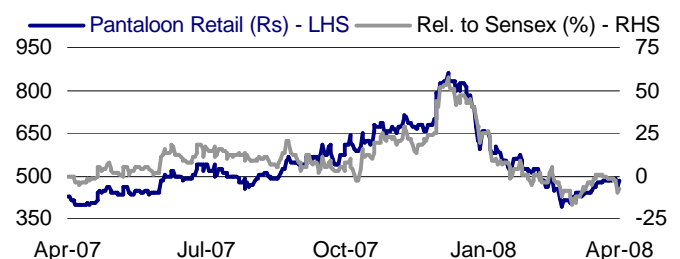
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY09	14.2	13.2	7.8
FY10	21.0	18.9	10.9

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
480	639	33.1	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT					
(RS MILLION)					
Y/E JUNE	2006	2007	2008E	2009E	2010E
Net Sales	18,678	32,367	53,536	80,324	109,904
Change (%)	77.4	73.3	65.4	50.0	36.8
Total Expenditure	-17,257	-30,211	-49,188	-74,026	-101,207
EBITDA	1,420	2,156	4,347	6,298	8,697
Change (%)	56.3	51.8	116	44.9	38.1
Margin (%)	7.6	6.7	8.1	7.8	7.9
Depreciation	-208	-369	-801	-1,012	-1,256
Int. and Fin. Charges	-335	-898	-1,619	-2,151	-2,147
Other Income - Recurring	30	32	57	70	80
Profit before Taxes	907	921	1,983	3,205	5,375
Change (%)	70.7	1.6	15.3	61.6	67.7
Margin (%)	4.9	2.8	3.7	4.0	4.9
Tax	-277	-311	-674	-1,067	-1,790
Tax Rate (%)	-30.6	-33.7	-34.0	-33.3	-33.3
Profit after Taxes	630	611	1,309	2,138	3,585
Change (%)	63.2	-3.0	114.4	63.3	67.7
Margin (%)	3.4	1.9	2.4	2.7	3.3
Extraordinary Items	10	589	0	0	0
Reported PAT	640	1,200	1,309	2,138	3,585

BALANCE SHEET					
(RS MILLION)					
Y/E JUNE	2006	2007	2008E	2009E	2010E
Share Capital	269	294	294	302	342
Reserves	5,000	10,628	12,858	14,789	28,620
Net Worth	5,269	10,921	13,151	15,091	28,962
Loans	6,014	12,996	21,200	24,200	21,100
Deferred Tax	279	558	963	1,603	2,677
Capital Employed	11,562	24,476	35,314	40,894	52,739
Gross Block	3,660	7,671	9,945	12,534	15,372
Less: Accum. Deprn.	-566	-925	-1,726	-2,738	-3,993
Net Fixed Assets	3,094	6,746	8,218	9,796	11,378
Capital WIP	861	1,311	1,836	2,387	1,790
Investments	1,617	2,520	5,803	5,803	5,803
Curr. Assets, L&A	8,445	17,495	25,880	32,381	46,551
Inventory	5,070	8,860	12,810	14,086	22,764
Account Receivables	170	652	693	1,043	1,427
Cash and Bank Balance	218	1,630	1,782	3,103	3,921
Others	2,987	6,354	10,594	14,149	18,439
Curr. Liab. and Prov.	2,454	3,596	6,424	9,473	12,782
Other Liabilities	2,298	3,439	6,202	9,136	12,293
Provisions	156	157	222	336	490
Net Current Assets	5,991	13,899	19,456	22,908	33,769
Miscellaneous Expenditur	0	0	1	0	0
Application of Funds	11,562	24,476	35,314	40,894	52,740

E: MOSI Estimates

RATIOS					
Y/E JUNE	2006	2007	2008E	2009E	2010E
Basic (Rs)					
EPS	4.7	4.2	8.9	14.2	21.0
Cash EPS	6.2	6.7	14.4	20.9	28.3
BV/Share	39.2	74.4	89.6	100.1	169.4
DPS	0.5	0.5	0.8	12	16
Payout %	10.7	12.0	9.0	8.5	7.6
Valuation (x)					
P/E	108.1	121.7	56.8	35.7	24.1
Cash P/E	81.3	75.9	35.2	24.2	17.9
EV/Sales	4.3	2.6	17	1.1	0.8
EV/EBITDA	56.8	39.6	20.7	14.6	10.1
P/BV	12.9	6.8	5.7	5.1	3.0
Dividend Yield (%)	0.1	0.1	0.2	0.2	0.3
Return Ratios (%)					
RoE	11.9	5.6	10.0	14.2	12.4
RoCE	10.7	7.4	10.2	13.1	14.3
Working Capital Ratios					
Debtor (Days)	3	7	5	5	5
Asset Turnover (x)	16	13	15	2.0	2.1
Leverage Ratio					
Debt/Equity (x)	1.1	12	16	16	0.7

CASH FLOW STATEMENT					
(RS MILLION)					
Y/E JUNE	2006	2007	2008E	2009E	2010E
OP/(loss) before Tax	1,212	1,787	3,546	5,286	7,441
Int./Div. Received	30	32	57	70	80
Depreciation and Amort.	208	369	801	1,012	1,256
Interest Paid	-335	-898	-1,619	-2,151	-2,147
Direct Taxes Paid	-277	-311	-674	-1,067	-1,790
(Incr)/Decr in WC	-3,397	-6,496	-5,405	-2,132	-10,042
CF from Operations	-2,560	-5,517	-3,294	1,018	-5,202
Extraordinary Items	10	889	0	0	0
(Incr)/Decr in FA	-1,852	-4,461	-2,798	-3,140	-2,241
(Pur)/Sale of Investments	-1,298	-903	-3,283	0	0
CF from Invest.	-3,139	-4,476	-6,081	-3,140	-2,241
Issue of Shares	2,519	4,541	1,277	8	10,598
(Incr)/Decr in Debt	3,152	6,982	8,204	3,000	-3,100
Dividend Paid	-77	-88	-134	-206	-312
Others	108	-30	180	641	1,075
CF from Fin. Activity	5,702	11,405	9,528	3,443	8,261
Incr/Decr of Cash	3	1,412	152	1,320	818
Add: Opening Balance	218	218	1,630	1,782	3,103
Closing Balance	218	1,630	1,782	3,103	3,921

N O T E S



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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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