Morgan Stanley

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ASIA/PACIFIC

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Stock Rating
Overweight

Industry View
In-Line

Pantaloon Retail

Highest ever EBITDA margin in seven years - Overweight

What's Changed	
Price Target	**Rs751.00 to Rs568.00**

Strong underlying performance: PRIL reported 56%, 114%, and 107% growth in revenues, operating profit, and adjusted net profit for F2008. This compares with our expectations of 77%, 90% and 112% growth, respectively. EBITDA growth surprised positively as Q4F08 EBITDA was 58% higher than our estimate. Even though a number of subsidiaries are in investment mode, consolidated revenues and EBITDA grew by 68% and 130%, respectively; however, the company continued to incur a loss at the net profit level.

Highlights of the results: 1. Changed the inventory accounting policy to 'lower of cost (including cost of bringing the goods to the store) and net realizable value'. 2. F08 EBITDA margin improved from 6.7% to 9.1%, translating into 114% growth 3.Promoters have already converted over 60% of the outstanding warrants at Rs500 per share. 4. Year-end inventory has increased around 70%, in line with year-end space, which has increased around 60%. 5. SSG was around 11% in F08. 6. Over 85% of rental contracts specify that liability of service tax on rentals to be borne by mall developer.

Our target price implies 83% upside: We have reduced our target price from Rs751 to Rs568 due a combination of increase in WACC from 10% to 11.5%, use of fully diluted equity capital, 12% increase in EBITDA for the next 4 years and we have also rolled our DCF value one year forward and introduced F2013 in our earnings forecast.

Key triggers: 1. Future ventures IPO by end of C2008 2. SEBI approval for issue of non voting shares to FIIs and 3. Margin expansion in the Q1F2009.

Key Ratios and Statistics

Reuters: PART.BO Bloomberg: PF IN
India Retail

Price target	Rs568.00
Upside to price target (%)	83
Shr price, close (Sep 19, 2008)	Rs310.00
52-Week Range	Rs875.00-283.10
Sh out, dil, curr (mn)	134
Mkt cap, curr (mn)	Rs41,675
EV, curr (mn)	Rs52,610
Avg daily trading volume (mn)	Rs32

Fiscal Year ending	06/07	06/08e	06/09e	06/10e
ModelWare EPS (Rs)	4.14	7.90	11.00	18.70
Prior ModelWare EPS (Rs)	-	8.16	12.44	16.74
Consensus EPS (Rs)§	4.41	7.05	11.57	16.96
Revenue, net (Rs mn)	32,367	50,489	77,375	112,099
EBITDA (Rs mn)	2,156	4,605	6,654	9,641
ModelWare net inc (Rs mn)	607	1,259	1,841	3,223
P/E	119.7	44.3	28.2	16.6
P/BV	6.7	3.0	2.2	1.8
RNOA (%)	11.3	11.2	9.3	10.7
ROE (%)	11.5	11.5	10.0	13.5
EV/EBITDA	38.8	16.4	10.6	8.3
Div yld (%)	0.1	0.2	0.2	0.5
FCF yld ratio (%)	(13.8)	(27.4)	(16.7)	(18.0)
Leverage (EOP) (%)	104.1	110.0	107.2	114.2

Unless otherwise noted, all metrics are based on Morgan Stanley ModelWare framework (please see explanation later in this note).
§ = Consensus data is provided by FactSet Estimates.
e = Morgan Stanley Research estimates

Financial Summary

PRIL: Income Statement

(Rs mn, Year Ending June)	2008E	2009E	2010E	2011E	2012E
Net sales	**50,489**	**77,375**	**112,099**	**154,968**	**203,679**
Growth (%)	56.0	53.3	44.9	38.2	31.4
Cost of Goods Sold	35,122	54,549	79,030	109,252	143,594
Gross Profit	15,366	22,826	33,069	45,716	60,085
Margin (%)	30.4	29.5	29.5	29.5	29.5
Employee costs	2,741	4,178	6,053	8,368	10,999
General Expenses	8,020	11,993	17,375	23,788	30,756
Total Operating costs	**10,761**	**16,171**	**23,429**	**32,156**	**41,754**
EBITDA	**4,605**	**6,654**	**9,641**	**13,560**	**18,331**
Margin (%)	9.1	8.6	8.6	8.8	9.0
Depreciation/ amortization	834	1,162	1,616	2,088	2,562
Interest	1,853	2,676	3,081	3,467	4,216
Other Income	38	15	15	15	15
Profit before Tax	1,956	2,832	4,959	8,020	11,569
Income Tax	697	991	1,736	2,807	4,049
Extra Ordinary Expense	0	0	0	0	0
Net Profit	1,259	1,841	3,223	5,213	7,520
Net Profit (adjusted)	**1,259**	**1,841**	**3,223**	**5,213**	**7,520**
Net Margin (%)	*2.5*	*2.4*	*2.9*	*3.4*	*3.7*
Modelware EPS	**7.9**	**11.0**	**18.7**	**30.2**	**43.6**
DPS	0.6	0.7	1.5	2.0	4.0

E = Morgan Stanley Research estimates Source: Company data, Morgan Stanley Research

PRIL: Balance Sheet

(Rs mn, Year Ending June)	2008E	2009E	2010E	2011E	2012E
Shareholders' Funds	18,487	23,809	29,024	33,841	40,568
Share Capital	319	335	345	345	345
Warrants	653	253	-0	0	0
Reserves & Surplus	17,515	23,221	28,679	33,496	40,223
Loan Funds	20,727	28,227	33,727	43,727	50,227
Deferred tax liabilities	558	558	558	558	558
TOTAL LIABILITIES	**39,772**	**52,594**	**63,309**	**78,126**	**91,352**
Net Fixed Assets	13,179	17,750	23,701	29,487	34,824
Investments	7,840	8,340	8,840	9,340	9,840
Long term investments	7,840	8,340	8,840	9,340	9,840
Cash and Cash Equivalents	815	3,129	1,011	3,641	5,504
Debtors	692	424	614	849	1,116
Inventory	14,216	20,827	29,837	39,695	50,751
Loans & advances	9,339	11,839	13,639	15,139	16,139
Other Assets	15	15	15	15	15
Current assets	24,261	33,105	44,105	55,698	68,020
Sundry creditors	5,774	8,967	12,991	17,959	23,604
Others (incl. provisions)	550	762	1,356	2,080	3,231
Current liabilities	6,323	9,729	14,348	20,040	26,836
Net Current Assets	17,938	23,376	29,757	35,658	41,185
TOTAL ASSETS	**39,772**	**52,594**	**63,309**	**78,126**	**91,352**

E = Morgan Stanley Research estimates Source: Company data, Morgan Stanley Research

PRIL: Cash Flow Statement

(Rs m, Year Ending June)	2008E	2009E	2010E	2011E	2012E
Net income reported	1,259	1,841	3,223	5,213	7,520
Depreciation	834	1,162	1,616	2,088	2,562
Chg in Working cap	-5,669	-5,438	-6,381	-5,901	-5,526
Net decrease in inventories	-5,357	-6,611	-9,010	-9,858	-11,056
Net decrease in debtors	-40	268	-190	-235	-267
Net decrease in Other Receivables	-3,000	-2,500	-1,800	-1,500	-1,000
Net increase in creditors	2,335	3,193	4,024	4,968	5,645
Net increase in other liabilities	393	212	594	724	1,151
Change in deferred tax liabilities	0	0	0	0	0
Cash flow from operations	**-3,576**	**-2,435**	**-1,543**	**1,400**	**4,555**
Capital expenditure	-5,956	-5,732	-7,567	-7,873	-7,899
Strategic investments	-5,750	-500	-500	-500	-500
Cash flow from investing	**-11,706**	**-6,232**	**-8,067**	**-8,373**	**-8,399**
Equity raised	6,416	3,616	2,289	-0	0
LT Debt raised	7,731	7,500	5,500	10,000	6,500
ST debt raised	0	0	0	0	0
Dividend (incl. tax)	-110	-135	-297	-396	-793
Others					
Cash flow from financing	**14,037**	**10,981**	**7,492**	**9,604**	**5,707**
Net chg in cash	**-1,245**	**2,314**	**-2,117**	**2,630**	**1,863**

E = Morgan Stanley Research estimates Source: Company data, Morgan Stanley Research

PRIL: Ratio Analysis

	2008E	2009E	2010E	2011E	2012E
Net sales growth (%)	56.0	53.3	44.9	38.2	31.4
EBITDA growth ()	113.6	44.5	44.9	40.7	35.2
Net Profit Growth ()	107.4	46.2	75.1	61.7	44.2
EPS Growth ()	91.0	39.2	70.0	61.7	44.2
Gross Margin ()	30.4	29.5	29.5	29.5	29.5
Operating Margin ()	9.1	8.6	8.6	8.8	9.0
Net Margin (	2.5	2.4	2.9	3.4	3.7
Return on Avg Equity ()	8.6	8.7	12.2	16.6	20.2
RNOA ()	8.1	8.2	9.4	11.0	12.9
Sales/Total Assets (x)	1.3	1.5	1.8	2.0	2.2
Sales/Net FA (x)	3.8	4.4	4.7	5.3	5.8
Total debt/Equity (x)	1.12	1.19	1.16	1.29	1.24
Net debt/Equity (x)	1.1	1.1	1.1	1.2	1.1

E = Morgan Stanley Research estimates Source: Company data, Morgan Stanley Research

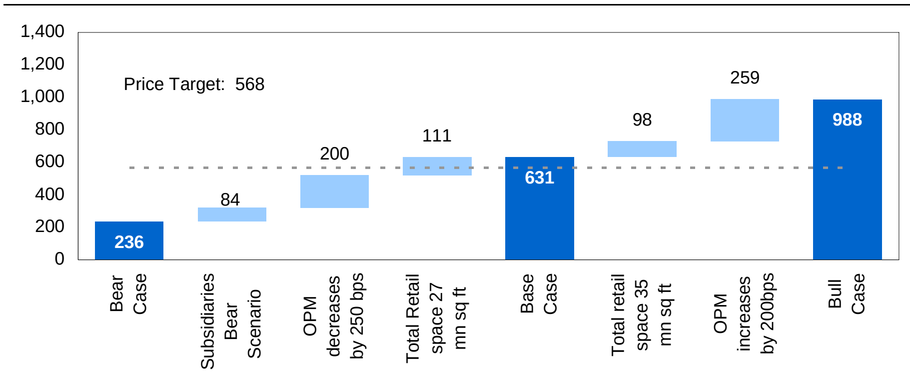
Risk-Reward Snapshot: Pantaloon Retail (PART.BO, Rs310, OW, PT Rs568)

Risk-Reward View: Favorable Long-term Outlook

Source: Company data, Morgan Stanley Research

Price Target Rs568		Derived by applying a 10% discount (conglomerate discount) to our Base Case assumptions.
Bull case Rs988	52.8x base case 2010E EPS	**Benign competition: Accelerated store roll-out and margin expansion:** Retail space increases to 35 msf. Operating profit margin increases to 11% by F2012. Subsidiaries add Rs153 per share.
Base case Rs631	33.7x base case 2010E EPS	**Good execution/real-estate advantage:** Retail space increases to 27msf. Operating profit margin increases to 9% by F2013. Subsidiaries add Rs153 per share.
Bear case Rs236	12.6x base case 2010E EPS	**Severe competition: Slowdown in store expansion and margin pressures:** Retail space at 15msf. Operating profit margin decreases to 6.5% by F2013. Subsidiaries add just Rs68 per share.

Profit Margins and Store Rollouts to Be Key Value Drivers



Source: Morgan Stanley Research estimates, FactSet

Investment Thesis

- We believe PRIL has secured sufficient capital to finance its planned growth for the next 2-3 years with the recent infusion of equity capital.
- PRIL's current stock price does not fully capture the value of its subsidiaries.
- PRIL's cost management has been effective in the past two quarters, which could augur well for margin improvement and strong top-line growth.

Key Value Drivers

- Successful rollout of new stores.
- Margin expansion because of scale benefits and improving profitability of older stores.
- Developing the subsidiaries into independent profitable companies with the ability to raise their own funding requirements.
- Successful rollout of new formats and deriving scale benefits from the extensive roll out of existing formats.

Potential Catalysts

- Increase in visibility for achieving target store rollouts.
- Monetizing its subsidiaries via independent-capital raising plans.

Risks

- Execution risk in terms of store roll-outs.
- Heightened competitive pressures hurt margins.
- Inability to fund growth plans.
- An unfavorable macro and political environment

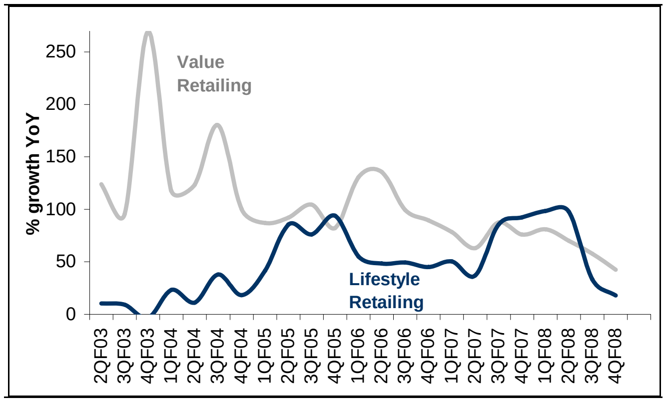
INVESTMENT THESIS

We strongly recommend investors accumulate PRIL stock at current levels. The stock is trading at 14.2x F2009e core earnings, and we expect the company to deliver an EPS CAGR of 49.5% over the next five years.

Highlights of the results: 1. Changed the inventory accounting policy to ‘lower of cost (including cost of bringing the goods to the store) and net realizable value’. A huge positive as this was one of investors’ most significant concerns. Cumulative inventory mark- down is Rs743.7mn (includes Rs180mn-200mn for F08). 2. F08 EBITDA margin improved from 6.7% to 9.1%, translating into 114% growth. Adjusting for inventory markdown in F08, growth would be 105%. Adjusting for the employees transferred to new subsidiaries formed in F08, growth would have been 98%. Total net loss of subsidiaries created in F08 was less than Rs50mn. 3. Operating leverage in play as surplus organizational capacities created during the last 2 years are being utilized effectively, staff cost down 100 bps, and other operational expenses including rent down 280 bps. 4. Promoters have already converted over 60% of the outstanding warrants at Rs500 per share. 5. Year-end inventory has increased around 70%, in line with year-end space, which has increased around 60%. 6. Interest cost increased 106% vs. around 60% increase in total debt due to rising funding cost. 7. SSG was around 11% in F08. 8. Over 85% of rental contracts specify that liability of service tax on rentals to be borne by mall developer.

Steady revenue growth – focus on profitable revenue growth: The company reported revenue growth of 35% in Q4F2008 and 56% in F2008. Based on monthly data, sales growth in value and lifestyle formats was 51% and 48% YoY, respectively. Total retailing space in PRIL stand-alone increased by 60%. The company delivered SSG of around 11% in F2008. The company is clearly shifting its focus from ‘revenue growth at any cost’ to ‘profitable revenue growth.’

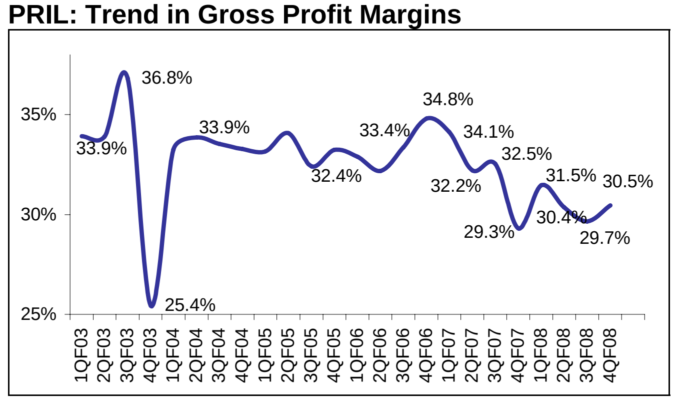
Exhibit 1
PRIL: Trend in Revenue Growth (YoY)



Source: Company data, Morgan Stanley Research

Q4F2008 gross margins improve: PRIL’s Q4F08 reported performance indicates nearly 120bps yoy increase in the gross profit margin. The company has been able to improve gross margins due to its renewed focus on its apparel business. The company’s apparel business margins in both the value and lifestyle segments improved significantly during the quarter. A part of the gross margin improvement also reflected the change in inventory valuation methodology wherein the cost of bringing the goods to the store is also included in the inventory (common retailers methodology of valuing inventory). F2008 gross margin does not include the Rs180-Rs200mn hit on account of the change in inventory valuation methodology during the year. Hence, it is likely that the company’s gross margin will decline in F2009E.

Exhibit 2
PRIL: Trend in Gross Profit Margins



Source: Company data, Morgan Stanley Research

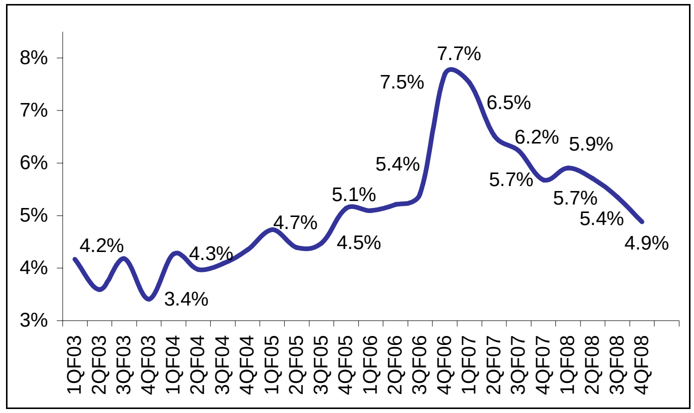
Change in Inventory accounting - a positive: One of the key concerns most investors had was PRIL’s relatively aggressive inventory accounting practice. PRIL has changed its inventory accounting policy to "at lower of cost (including cost of bringing the goods to the store) and net realizable value" from "retail price less mark up" in compliance with Indian Gaap (AS -2). The net effect of this change was taken on the balance sheet with a reduction of Rs491 mn in the reserves. The cumulative inventory markdown was Rs743.7mn, which includes around Rs180-200mn for F2008.

Operating leverage in play – staff costs fall significantly: The company's employee cost to sales ratio improved significantly in Q4F08, driven largely by a combination of moving part of the staff costs to its subsidiaries and better revenue growth. The company's employee cost as percentage of sales declined from 5.7% in Q4F07 to 4.9% in Q4F08. We estimate that the company transferred around 800 employees to its subsidiaries Future Logistics and Future Knowledge Services. Even adjusting for these transfers, the company's employee cost fell by 60 bps in F2008. Total net loss of subsidiaries that were created in F2008 was less than Rs50 mn. The company has improved employee productivity significantly as well as frozen raises for senior management. We believe that the company is likely to continue to benefit from a reduction in employee costs in F2009E.

According to management, it is planning to cut back on advertisements, recruitment costs, and reduce travel expenses to save as much as Rs1.65 bn in the years 2008-09. PRIL plans to cut employee costs by Rs650 mn in F2009 by redeploying people in its various businesses and reducing new hirings. Instead of external hiring, it plans to redeploy some of its people resources from mature businesses to the new ventures.

Exhibit 3

PRIL: Trend in Staff Cost as % of Sales



Source: Company data, Morgan Stanley Research

Other expenses declined significantly: The company's other expenses as a percentage of sales declined 280 bps in F2008. We believe that a large part of the decline in other expenses reflects improved SSG and the benefits of the huge cost savings exercise initiated by the company. The back-ends of both Home Solutions and Big Bazaar are collapsed into one, which will help save on separate IT departments, sourcing divisions. Similarly, in F2009 the company aims to cut 20 per cent of its advertising and communication costs. It plans to save nearly Rs1 bn by cutting these expenses. PRIL is also encouraging tele-conferencing instead of travel to manage costs and improve margins.

Highest ever EBITDA margin in seven years: PRIL's Q4F08 operating profit grew 149% and OPM stood at 10.2%, an improvement of 465 bps yoy. For F08 OPM stood at 9.1% an improvement of 250 bps yoy. A focus on better-margin products, better human resource planning, and operating leverage contributed to improved margins. F2008 EBITDA margin improved from 6.7% to 9.1%, translating into 114% growth. Adjusting for inventory markdown in F2008, growth would have been 105%. Adjusting for the employees transferred to new subsidiaries formed in F2008, EBITDA growth would have been 98%.

Exhibit 4

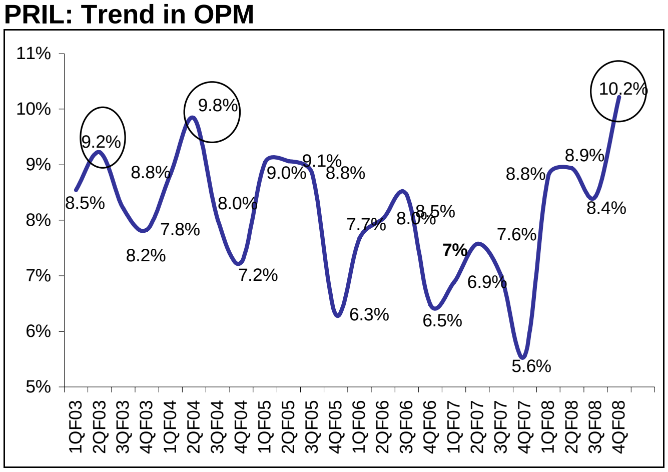
PRIL 4Q08: Stand-alone Financial Result Analysis

Rs mn	4QF08	4QF07	YoY % change	3QF08	QoQ % change	F2008	F2007	YoY % change
Net Sales	**13,814**	**10,196**	**35%**	**13,543**	**2%**	**50,489**	**32,367**	**56%**
Other Income	0.6	0.3	95%	16.5		38	32	19%
Total Expenditure	12,402	9,629	29%	12,402	0%	45,884	30,211	52%
(a) Increase/ Decrease in Stock Trade	(2,070)	(1,346)	54%	(1,097)	89%	(6,144)	(3,674)	67%
(b) Consumption of Raw Material	11,676	8,555	36%	10,624	10%	41,266	25,768	60%
Gross profit	**4,207**	**2,988**	**41%**	**4,017**	**5%**	**15,367**	**10,273**	**50%**
Gross profit margin (%)	*30.5*	*29.3*	*1.1*	*29.7*	*0.79*	*30.4*	*31.7*	
(c) Staff Cost	674	579	17%	725	-7%	2741	2061	33%
(d) Other Expenditure	2121	1842	15%	2151	-1%	8021	6056	32%
Staff cost as % of sales	4.9	5.7		5.4				
Operating profit	**1412**	**568**	**149%**	**1141**	**24%**	**4605**	**2156**	**114%**
Operating profit Margin (%)	*10.2*	*5.6*		*8.4*		*9.1*	*6.7*	*37*
Interest and Financial Charges	655	337	94%	429	53%	1853	898	106%
Depreciation	254	126	101%	223	14%	834	369	126%
Profit before tax	**504**	**105**	**379%**	**506**	**0%**	**1956**	**921**	**112%**
Provision for Taxation	178	9	1852%	185	-4%	697	314	122%
(a) Fringe Benefit Tax	9	-17		9		32	23	40%
(b) Current Tax	60	44		78		292	307	-5%
(c) Deferred Tax	109	44		98		373	-17	
Earlier years income tax	-	0.6		-		0.3	0.6	
Net Profit	**325**	**69**	**373%**	**321**	**1%**	**1259**	**607**	**107%**
Net Margin (%)	2.4	0.7		2.4		2	2	
Exceptional Income net of tax	0	118		0		-	593	
Reported Net profit	**325**	**187**	**74%**	**321**	**1%**	**1259**	**1200**	**5%**

Source: Company data, Morgan Stanley Research

Exhibit 5

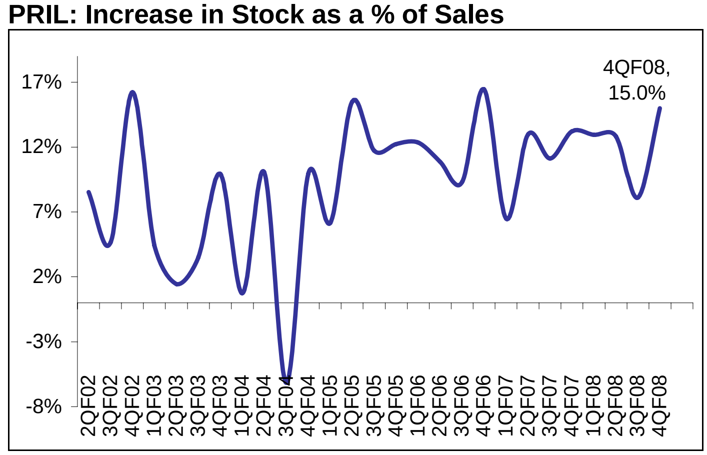
PRIL: Trend in OPM



Source: Company data, Morgan Stanley Research

Exhibit 6

PRIL: Increase in Stock as a % of Sales



Source: Company data, Morgan Stanley Research

Inventory increase in line with space: Year-end inventory increased around 70%, in line with year-end space, which increased around 60%. The inventory to sales ratio stood at 15% compared with 13.2% in Q4F07.

Strong operational performance at the consolidated level: Revenues and operating profit grew by 68% and 130%, respectively, and adjusted net loss for F08 came in at Rs113 mn (vs. Rs241 mn for F07). Losses at subsidiaries were Rs1294 mn for F08 (vs. Rs778 mn for F07). Even though a number of subsidiaries/businesses are in investment mode, consolidated revenues and EBITDA grew by 68% and 130%, respectively; however, the company continued to incur a loss at the net profit level.

PRIL reported consolidated total sales of Rs58.4 bn and net loss (adjusted for exceptionals) of Rs113 mn.

Exhibit 7

PRIL: Consolidated Financial Result Analysis

Rs mn	F2008	F2007	YoY
Net Sales	**58,405**	**34,686**	**68%**
Other Income	259	79	227%
Total Expenditure	**55,400**	**33,378**	**66%**
(a) Increase/ Decrease in Stock Trade	(7,311)	(4,670)	57%
(b) Consumption of Raw Material	46,404	27,980	66%
(c) Staff Cost	4,456	2,705	65%
(d) Other Expenditure	11,851	7,330	62%
(e) Goodwill written off	-	32	-100%
Gross profit	**19,312**	**11,375**	**70%**
Gross profit margin (%)	33	33	
Operating profit	**3,005**	**1,308**	**130%**
Operating profit Margin (%)	5.1	3.8	
Interest and Financial Charges	2,236	1,001	123%
Depreciation	1,182	482	145%
Profit before tax	**(153)**	**(96)**	**59%**
Provision for Taxation	473	299	58%
(a) Fringe Benefit Tax	59	34	74%
(b) Current Tax	314	27	1065%
(c) Deferred Tax	100	238	-58%
Earlier years income tax	(0.3)	0.6	-152%
Prior Period items	(10.4)	1.8	-676%
Less Minority Interest	(512)	(156)	227%
Add: Share of Loss in Associate company	(9)		
Adjusted Net Profit	**(113)**	**(241)**	**-53%**
Net profit		-	
Extraordinary item	332	597	-44%
Reported Net Profit	**219**	**355**	**-38%**
Basic EPS	1.45	2.58	-44%
Diluted EPS	1.45	2.58	-44%

Source: Company data, Morgan Stanley Research

Start-up Costs Explain Subsidiary Losses

In our view, the bulk of the losses incurred by PRIL at the consolidated level relate to start-up costs at its subsidiaries. The company has already raised private equity capital in Home Solutions, Future Bazaar, and Future Media and hence these companies are likely to be self-funded in the foreseeable future.

Most of the losses that incurred in Future Bazaar are related to the start-up and launch expenses of the company. Similarly, Future Media losses are related to the start-up cost of the company. Losses in its JV Footmart are a result of the poor performance of the business.

Exhibit 8

PRIL: Subsidiary losses (Rs mn)

Subsidary	F2008	F2007	Stake Held
Home Solutions	600	400	73%
Future Capital	280	NA	55%
Future Media	65	40	85%
Future Bazaar	94	170	80%
Footmart	92	98	51%
Insurance JV	47	50	74%
Future Logistics	24	20	100%
Knowledge Services	16	NA	100%
Others	75	NA	
	1294	**778**	

Source: Company data, Morgan Stanley Research

Earnings change – long-term earnings revised upwards

We have increased our EBITDA forecast for PRIL by around 12% during the next 4 years. We have increased F2010-12E earnings by around 14% largely on account of expectations for an improvement in EBITDA margin. However, F2009E earnings have been reduced because of a significant increase in funding costs due to rising interest costs and higher-than-anticipated depreciation cost in F2008.

Exhibit 9

PRIL: Changes in Key Estimates

Rs mn	New	Old	% change
Revenues			
F2009	77,375	86,438	-10.5%
F2010	112,099	121,273	-7.6%
F2011	154,968	167,795	-7.6%
F2012	203,679	220,696	-7.7%
Operating profits			
F2009	6,654	6,224	6.9%
F2010	9,641	8,489	13.6%
F2011	13,560	11,997	13.0%
F2012	18,331	16,332	12.2%
Adjusted Net Profit			
F2009	1,841	2,051	-10.3%
F2010	3,223	2,886	11.7%
F2011	5,213	4,485	16.2%
F2012	7,520	6,617	13.6%
EPS			
F2009	11.0	12.4	-11.6%
F2010	18.7	16.7	11.7%
F2011	30.2	26.0	16.2%
F2012	43.6	38.4	13.6%

Source: Company data, Morgan Stanley Research

Valuation

We maintain that the tangible growth represented by the company's retail space expansion, healthy top-line growth, and improved earnings have reduced potential execution risk in this business. We expect the company to deliver strong top-line CAGR of 38.6% over the next five years. We believe that PRIL's retail space can record a CAGR of 27.7% over the next five years and reach 27 msf by F2013, excluding Home Solutions Retail (HSRIL). With better cost management and efficiencies from scale creeping in, we expect the company to deliver a strong EPS CAGR of 53.8% over the next two years and around 49.5% CAGR over the next five years. We assume the operating margin will be at 8.6% and stable for next two years. We expect the operating margin to improve further to 9% in F2013, with older stores becoming more profitable as the retail model expands further to reap efficiencies of scale.

Key triggers for the stock

1) The unlocking of value in Future Ventures, which has already filed its DRHP, and its other subsidiaries such as Home Solutions, Future Media, Future Bazaar, Future Logistics and Future Brands; and
2) Better-than-expected new space rollout.
3) Better-than-expected margin expansion

Downside Risks

1) Execution risk in terms of store rollouts
2) Heightened competitive pressures could hurt margins
3) Inability to fund growth plans
4) An unfavorable macro and political environment

SOTP and Price Target

In our view, PRIL is creating significant long-term value in its core business and in its subsidiaries. Our discounted cash flow (DCF) value for the company's core business is Rs478. We expect operating profit CAGR of 38.2% between F2009 and F2013. Our price target of Rs. 568 is based on a 10% discount to the sum-of-the-parts valuation (Exhibit 11).

We have reduced the DCF value of the core business from Rs625 to Rs478 for the following reasons:

1. Increase in WACC from 10% to 11.5% due to 100bps rise in risk-free rate, 100bps rise in risk premium, and 150 bps rise in cost of debt.

2. We now use fully diluted equity capital for our DCF calculation, which has impacted DCF value by 3%.

However, we have increased the company's EBITDA by 12% for the next 4 years, which has contributed to the increase in DCF value.

We have also rolled our DCF value one year forward and introduced F2013 in our earnings forecast, which contributes positively to our DCF value calculations.

Exhibit 10

PRIL: Assumptions Underlying Our DCF Model

Growth rate during F2014-24E (%)	15.0
Growth rate post F2024E (%)	6.0
ROIC during F2014E-24E (%)	13.0
ROIC after F2024E (%)	12.5
WACC (%)	11.5

Source: Company data, Morgan Stanley Research

Company Description

Pantaloon Retail owns and operates retail stores throughout India. It has around 2.75 million square feet of retail space and the company operates its stores under "Pantaloons," "Big Bazaar" and "Food Bazaar" names. Pantaloon also manufactures men's read- made garments, which are marketed under the Pantaloon and Bare Necessities Brands.

India Retail

Industry View: In-Line

In our view, the structural growth story of the industry continues to be robust. However, we believe that cost pressures and pressures on cash flow due to increased working capital investments are likely to affect earnings and free cash flow for the companies in the foreseeable future.

MSCI Country: India

Asia Strategist's Recommended Weight: 4.0%
MSCI Asia/Pac All Country Ex Jp Weight: 7.8%

Exhibit 11

Sum-of-the-Parts DCF Value and Price Target (Rs)

DCF Value for Core Business	478
Subsidiaries Valuation	
Home Solutions (73.32% stake)	60
Future capital (55% stake)	68
Future Bazaar (80% stake)	14
Future Media (85% stake)	12
Total Value	**631**
Discount (%)	10
Price target	**568**

Note: All per share calculations are based on the expected number of shares outstanding as of F010E to account for the anticipated dilution in equity.
Source: Company data, Morgan Stanley Research

Sum-of-the-parts Increases with Subsidiaries Generating Additional Value

Our price target of Rs568 is based on a 10% discount to our sum-of-the-parts value of Rs. 631 per share. We value Future Capital Holdings Limited based on its market cap at Rs21.2 billion. PRIL's stake in the business, post IPO, is 55%, which leads to a valuation of Rs11.7 billion, or Rs68 per share.

PRIL's stake in its subsidiary Home Solutions is valued at Rs 10.3 billion. Similarly, we have assumed PRIL's stake in Future Bazaar and Future Media is valued at Rs2,400 million and Rs2,125 million, respectively. The company has several other subsidiaries that have not been included in the valuation.

Exhibit 12

PRIL: PER for Stand-alone and Reported

	F2009	F2010	F2011
Standalone Implied PER*	14.2	8.4	5.2
Reported PER	28.2	16.6	10.2

Source: Company data, Morgan Stanley Research
*After excluding our valuations for HSRIL, FCHL, Future Bazaar & Future Media (Rs153 per share) from the current stock price

MORGAN STANLEY ModelWare	**Morgan Stanley ModelWare is a proprietary analytic framework that helps clients uncover value, adjusting for distortions and ambiguities created by local accounting regulations.** For example, ModelWare EPS adjusts for one-time events, capitalizes operating leases (where their use is significant), and converts inventory from LIFO costing to a FIFO basis. ModelWare also emphasizes the separation of operating performance of a company from its financing for a more complete view of how a company generates earnings.

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(as of August 31, 2008)

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Stock Rating Category	Count	% of Total	Count	% of Total IBC	% of Rating Category
Overweight/Buy	**892**	**41%**	**299**	**45%**	**34%**
Equal-weight/Hold	**936**	**43%**	**277**	**42%**	**30%**
Underweight/Sell	**367**	**17%**	**87**	**13%**	**24%**
Total	**2,195**		**663**		

Data include common stock and ADRs currently assigned ratings. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations. Investment Banking Clients are companies from whom Morgan Stanley or an affiliate received investment banking compensation in the last 12 months.

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Overweight (O or Over) - The stock's total return is expected to exceed the total return of the relevant country MSCI Index, on a risk-adjusted basis over the next 12-18 months.
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Underweight (U or Under) - The stock's total return is expected to be below the total return of the relevant country MSCI Index, on a risk-adjusted basis, over the next 12-18 months.
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Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

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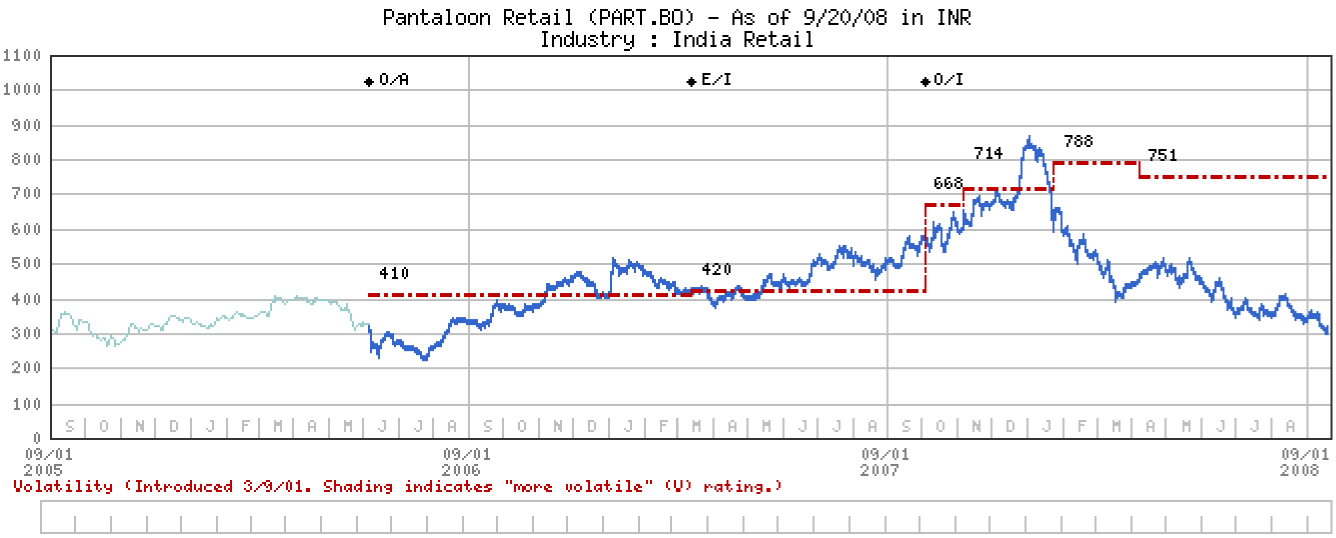
Stock Price, Price Target and Rating History (See Rating Definitions)



Stock Rating History: 6/6/06 : O/A; 3/14/07 : E/I; 10/3/07 : O/I

Price Target History: 6/6/06 : 410; 3/14/07 : 420; 10/3/07 : 668; 11/6/07 : 714; 1/23/08 : 788; 4/7/08 : 751

Source: Morgan Stanley Research   Date Format : MM/DD/YY   Price Target   No Price Target Assigned (NA)
Stock Price (Not Covered by Current Analyst)   Stock Price (Covered by Current Analyst)
Stock Ratings abbreviated as below (Effective 3/18/02, ratings appear as Stock Ratings/Industry View) ◆
Stock Ratings as of 3/18/02: Overweight (O) Equal-weight (E) Underweight (U) More Volatile (V) No Rating Available (NAV)
Stock Ratings prior to 3/18/02: Strong Buy (SB) Outperform (OP) Neutral (N) Underperform (UP) No Rating Available (NAV)
Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)

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Industry Coverage:India Retail

Company (Ticker)	Rating (as of)	Price (09/19/2008)
Hozefa Topiwalla		
Pantaloon Retail (PART.BO)	O (09/22/2008)	Rs310
Shoppers' Stop (SHOP.BO)	U (11/06/2007)	Rs260
Titan Industries Ltd (TITN.BO)	E (08/12/2008)	Rs1,198.1

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