

KOUTONS RETAIL INDIA LTD

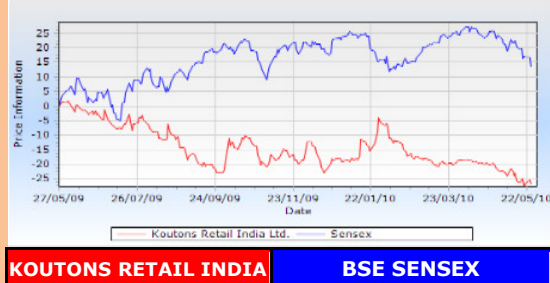
BUY

May 27, 2010

C.M.P:
Rs.315.00

Target Price:
Rs.378.00

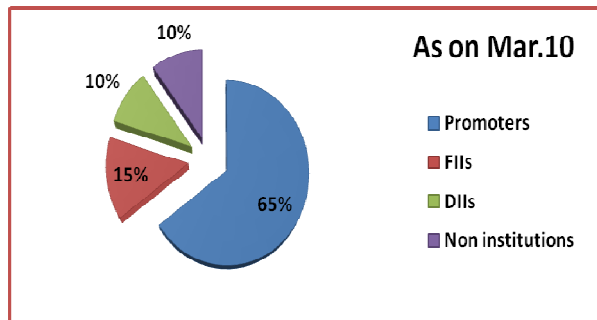
1 Year Comparative Graph



Stock Data

Sector	Retail
Face Value (Rs)	Rs.10.00
52 wk. High/Low (Rs.)	Rs.452.00/276.40
Volume (2 wk. Avg.)	31563
BSE Code	532901
Market Cap (Rs.mn.)	9623.57

Share Holding Pattern



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SYNOPSIS

- Koutons Retail India Ltd is an integrated apparel manufacturing and retailing company.
- The company has a network of 1,150 outlets (including Koutons and Charlie Outlaw outlets) across the country.
- During the quarter the company launched women's wear and kids wear in its existing outlets.
- The company plans to grow through the inorganic route by acquiring premium brands.
- Koutons Retail added 68 new family stores during the year. It closed 57 stores during the quarter.
- The total area under operations increased to 13.6 lakh sq ft at the end of the quarter from 12.67 lakh sq ft at the end of Q4FY09, a growth of 7%.
- To capture the increasing demand, the company has unveiled an aggressive rollout plan for the next 2 years.
- The integrated business model helps the company maintain strong margins despite the discount pricing.
- Net sales and PAT of the company are expected to grow at a CAGR of 13% and 11% over 2009 to 2012E respectively.

Financials

(Rs.mn.)	FY10A	FY11E	FY12E
Net Sales	12054.45	13500.98	15121.10
EBIDTA	2344.80	2435.79	2728.53
PAT	836.01	936.62	1090.33
EPS (Rs)	26.95	30.66	35.69
P/E (x)	11.69	10.27	8.83

Peer Group Comparison

Name of the company	CMP(Rs.)	Market Cap.(Rs.Mn.)	EPS(Rs.)	P/E(x)	P/BV(x)	Dividend (%)
Koutons Retail India	315.00	9623.57	26.95	11.69	2.26	10
Pantaloon Retail	370.70	76419.8	7.93	46.75	3.39	30
Trent	815.05	16329.6	17.65	46.18	2.69	55
Provogue	43.00	4917.4	2.88	14.93	0.73	15

Investment Highlights

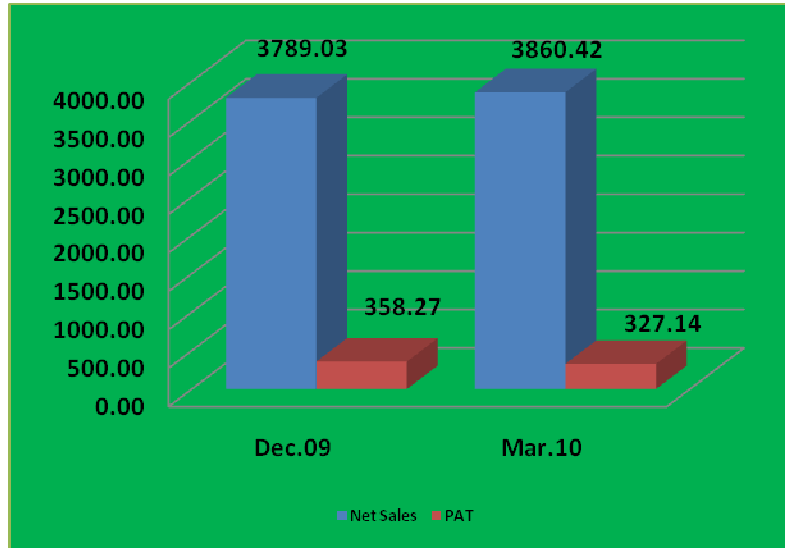
- Results Update (Q4 FY10)**

Koutons Retail India Ltd reported a decline in standalone net profit for the quarter ended March 2010. During the quarter, the profit of the company decline 8.69% to Rs 327.14 million from Rs 358.27 million in the same quarter previous year. Net sales for the quarter rise marginally 1.88% to Rs 3860.42 million, while total income for the quarter marginally increased 1.93% to Rs 3862.34 million, when compared with the prior year period. Company posted earnings of Rs 10.71 a share during the quarter, registering 8.69% decline over prior year period.

Quarterly Results - Standalone (Rs in mn)			
As at	Mar - 10	Mar - 09	%Change
Net Sales	3860.42	3789.03	1.88
PAT	327.14	358.27	(8.69)
Basic EPS	10.71	11.73	(8.69)

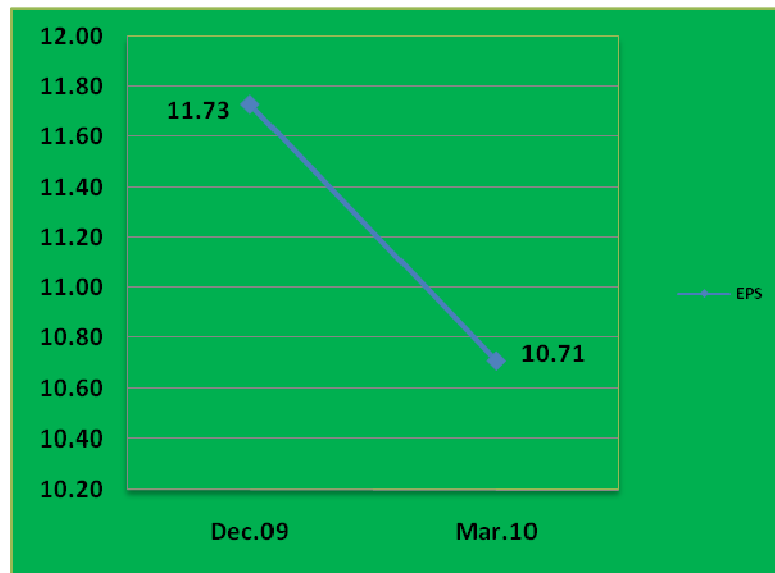
Net Sales & PAT

During the quarter, Net sales rise marginally by 1.88% to Rs.3860.42 million from Rs.3789.03 million in the same quarter last year and the Total Profit for the quarter ended March 2010 was Rs.327.14 million decline by 8.69% from Rs.358.27 million compared to same quarter last year.



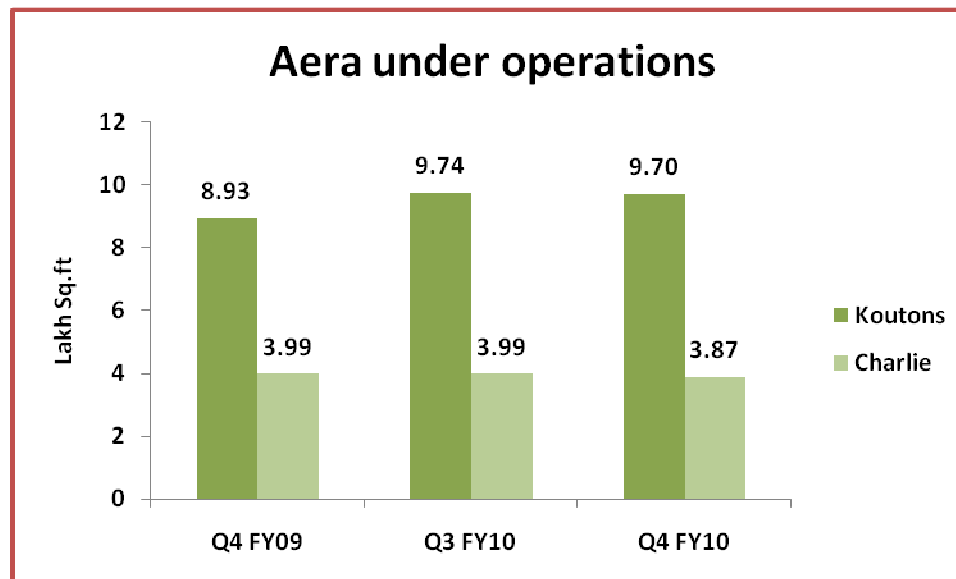
EPS

The basic EPS of the company stood at Rs.10.71 for the quarter ended Mar 2010 from Rs.11.73 for the quarter ended Mar 2009.



- **Area under operations**

The total area under operations increased to 13.6 lakh sq ft at the end of the quarter from 12.67 lakh sq ft at the end of Q4FY09, a growth of 7%. For the full year, the company was in a consolidation phase, wherein it increased the space while reducing the number of stores simultaneously.



- **To raise Rs 1 bn through QIP**

Koutons is looking to raise around Rs 1 billion through qualified institutional placement (QIP) for expansion even as Fidelity is preparing to exit its 5.6% investment.

- **Open more family stores**

Apparel retailer Koutons Retail has said it is keen on opening more family stores where clothing lines co-exist with accessories and footwear. The company is focusing on converting its existing stores to cover larger retail space rather than opening new stores.

- **Pledged shares**

The risk of losing control over Koutons Retail India Ltd, the apparel manufacturer and retailer, has forced its promoters to offer real estate assets in lieu of Koutons shares they pledged with lenders to raise funds.

- **Plans foray into innerwear**

Apparel and fashion wear chain Koutons India Retail is planning to foray into inner-wear segment and to expand its leather accessories portfolio as it eyes a growth of 30-35 per cent in 2009-10.

- **Launches Feel Me shirt collection**

Koutons Retail India Ltd., Retail apparel giant has launched its Feel Me shirt collection for men to their existing brands. The apparel has added the Feel Me collection to strengthen its menswear range. This range of premium quality segment shirts are designed to satisfy the growing needs of fashion conscious youth of today.

Company Profile

Koutons Retail India Ltd is an integrated apparel manufacturing and retailing company. It designs, manufactures and retails apparels under the “Koutons” and “Charlie Outlaw” brands. The company has a network of 1,150 outlets (including Koutons and Charlie Outlaw outlets) across the country. It has manufacturing capacity of 12.36 million pieces per annum and finishing capacity of 22.92 million pieces per annum. The company is expanding aggressively across the country with both of its brands, and is in the process of launching women’s brand “Les Femme” and kid’s brand “Koutons Junior”. It is increasing its product categories to include men’s apparels, women’s apparels and kids wear. It is also undergoing inorganic expansion route through acquisition of regional brands, thereby increasing the number of brands in its portfolio.

Company Brands



Business Area

Company has set out their business processes for: (a) their manufacturing; and (b) their sales operations.

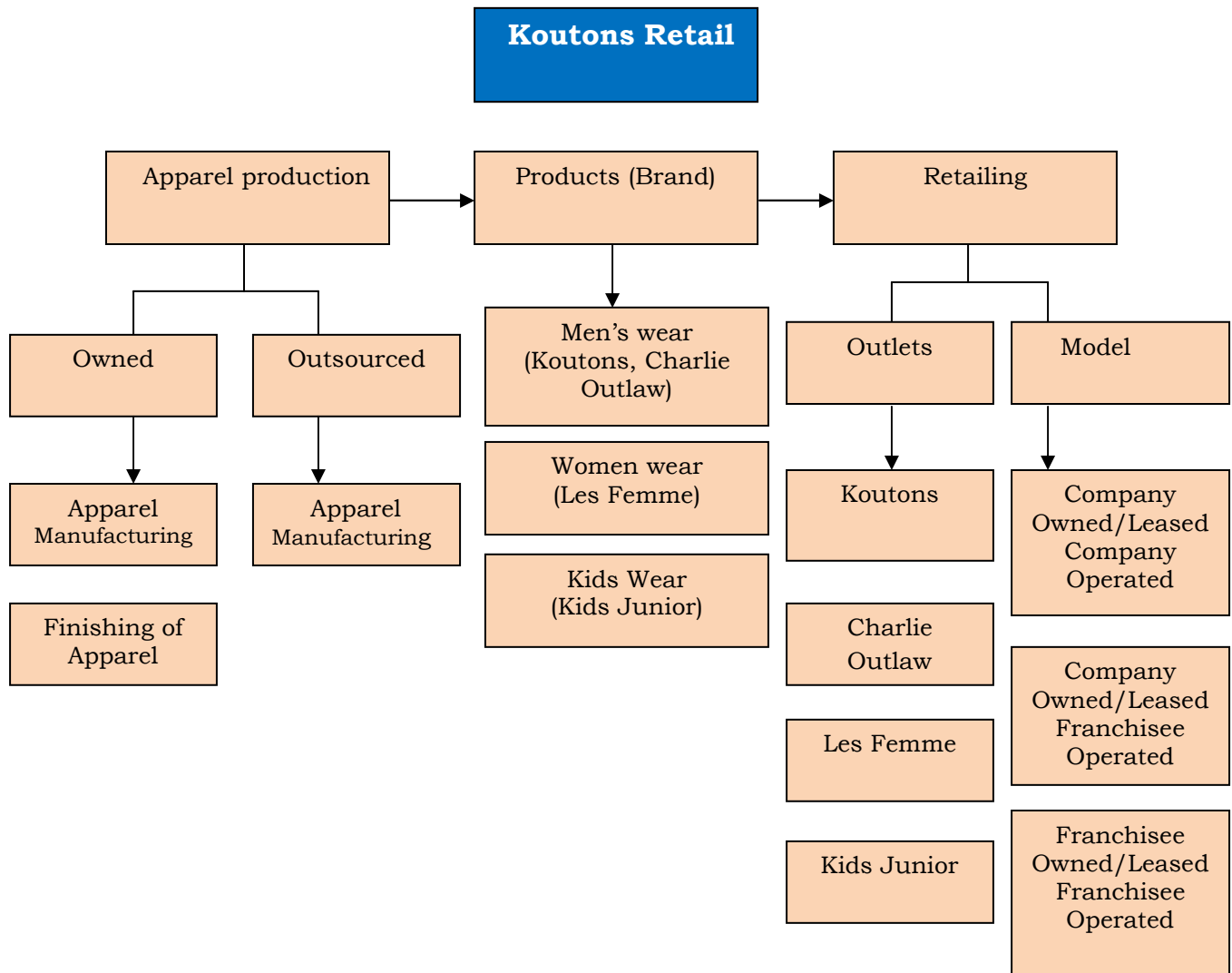
Manufacturing processes

Their business model for manufacturing of apparels consists of conceptualization and designing, procuring raw material, finalization of product and design, manufacturing

apparels either internally or outsourcing, finishing and packaging and storing in warehouse.

Sale process

Company started shifting to the franchisee model for retailing their apparels. Prior to that, they were following the traditional distribution set up through a chain of distributors and retailers. In that structure, the manufacturer sells to the distributor who in turn sells to the retailer. Fear of unsold stocks kept both the distributor and retailer margins high which in turn led to high retail costs and these in turn slowed down sales and resulted in dead stocks. Thus, it resulted in a cycle leading to inefficient selling, high costs and a long realization period.



Products

Trousers	Formal trousers
	Chinos
	Casual
	Cargo's
	Capri
Denim wear	Jeans
	Shirts
	Jackets
Shirts	Formal
	Semi – formal
	Casual
	Party wear in a wide range of fabrics and designs
Knit wear	T-Shirts
	Sweaters
	Pullovers
	Track suits
	Sweat shirts

SWOT Analysis

STRENGTHS

- Exclusive Brand Outlets.
- Wide network of Exclusive Brand Outlets.
- Integrated player with low-cost sourcing capabilities.
- Unique brand positioning.
- Experienced and efficient management.
- Design and merchandising expertise, with a pulse on fashion.
- Wide apparel range.

WEAKNESSES

- High dependency on franchisee for sales of the products.
- Caters only to men's category.
- Outsource manufacturing of some products; Manufacturing facilities are set up only in North India.
- The business of the company is largely depends on the economic conditions of US and European countries as it export a large portion of its products to those countries.

OPPORTUNITIES

- The growing retail market in India.
- KRIL is planning to foray into garments for kids & ladies.
- Expanding into new geographies.
- Brand image and Market Size.
- The revolution in organized retailing would increase the consumption of apparel and made-ups.

THREATS

- Although it has excellent implementation expertise, external risks like non-availability of adequate location, delay in delivery of outlets, etc. may affect the company.
- Inventory management.
- Since the company is in fashion business, there is risk of obsolescence if the fashion trends change.

Financial Results

12 Months Ended Profit & Loss Account (Standalone)

Value(Rs. in million)	FY09A	FY10A	FY11E	FY12E
Description	12m	12m	12m	12m
Net Sales	10,467.00	12,054.45	13500.98	15121.10
Other Income	164.00	3.74	5.61	6.73
Total Income	10,631.00	12,058.19	13506.59	15127.83
Expenditure	-8,384.73	-9,713.39	-11070.81	-12399.30
Operating Profit	2,246.27	2,344.80	2435.79	2728.53
Interest	-885.34	-909.00	-836.28	-878.09
Gross Profit	1,360.93	1,435.80	1599.51	1850.44
Depreciation	-153.00	-163.99	-180.39	-198.43
Profit before Tax	1,207.93	1,271.81	1419.12	1652.01
Tax	-412.71	-435.80	-482.50	-561.68
Profit after Tax	795.22	836.01	936.62	1090.33
Extraordinary Items	0.00	-12.76	0.00	0.00
Net Profit	795.22	823.25	936.62	1090.33
Equity Capital	305.51	305.51	305.51	305.51
Reserves	3,946.45	3,946.45	4,883.07	5,973.39
Face Value	10.00	10.00	10.00	10.00
Total No. of Shares	30.55	30.55	30.55	30.55
EPS	26.03	26.95	30.66	35.69

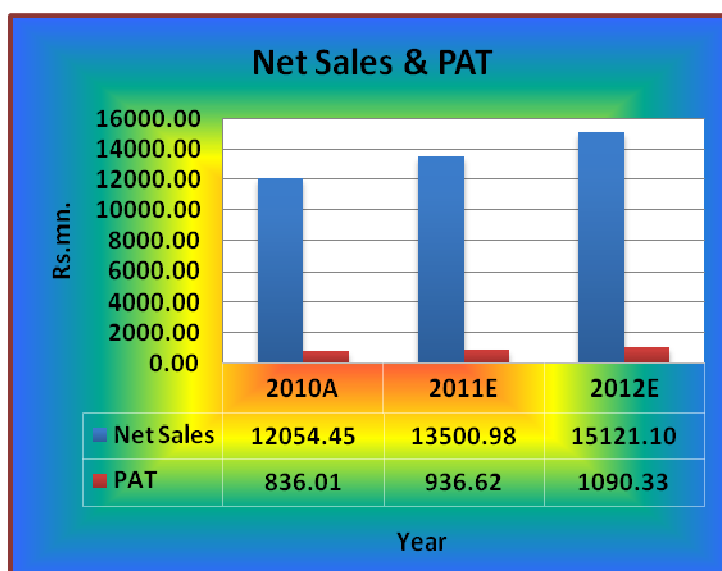
Quarterly Ended Profit & Loss Account (Standalone)

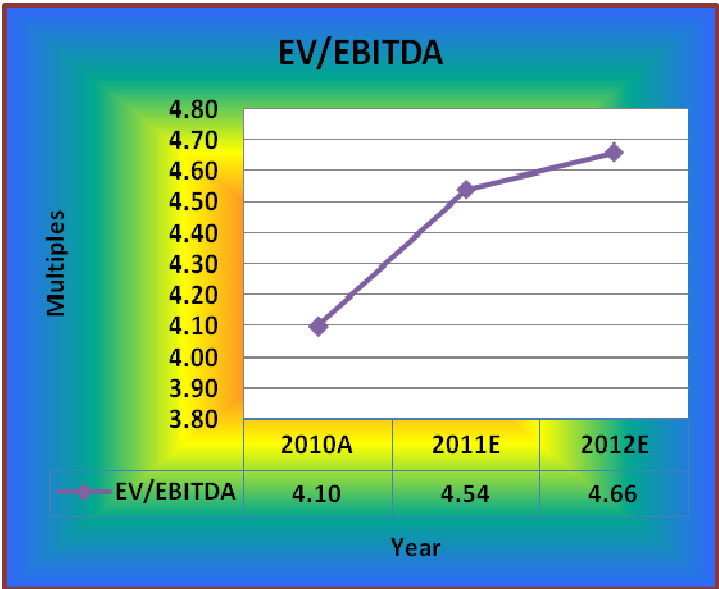
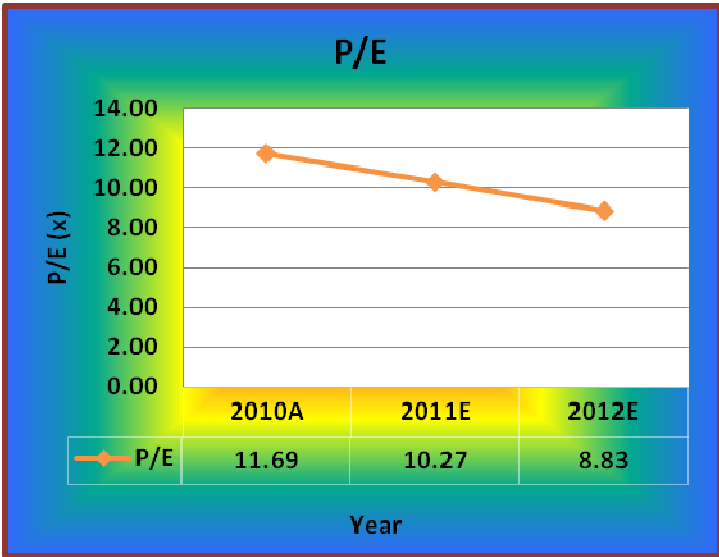
Value(Rs. in million)	30-Sep-09	31-Dec-09	31-Mar-10	30-Jun-10E
Description	3m	3m	3m	3m
Net Sales	3478.93	2697.59	3860.42	3088.34
Other Income	1.29	0.21	1.92	2.11
Total Income	3480.22	2697.80	3862.34	3090.45
Expenditure	-2861.27	-2205.20	-3112.13	-2532.44
Operating Profit	618.95	492.60	750.21	558.01
Interest	-222.01	-215.19	-203.99	-193.79
Gross Profit	396.94	277.41	546.22	364.22
Depreciation	-37.24	-38.99	-47.96	-50.36
Profit before Tax	359.70	238.42	498.26	313.86
Tax	-123.77	-80.47	-171.12	-106.71
Profit after Tax	235.93	157.95	327.14	207.15
Equity Capital	305.51	305.51	305.51	305.51
Face Value	10.00	10.00	10.00	10.00
Total No. of Shares	30.55	30.55	30.55	30.55
EPS	7.72	5.17	10.71	6.78

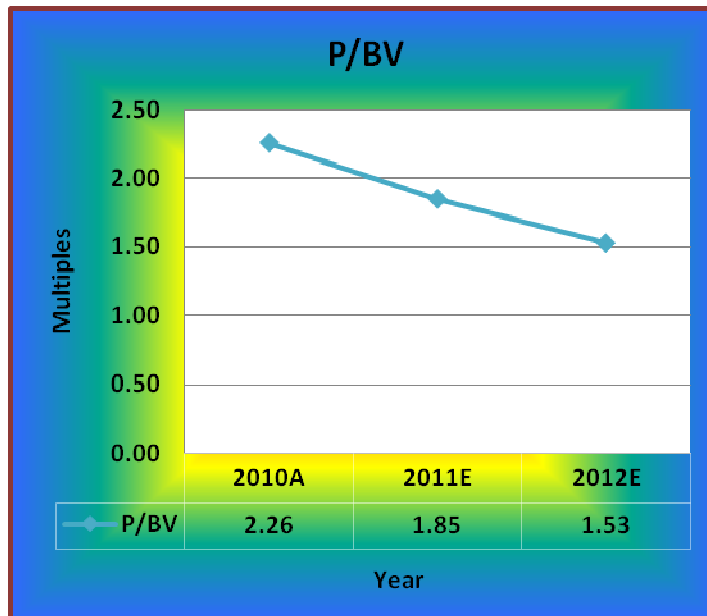
Key Ratios

Particulars	FY09A	FY10A	FY11E	FY12E
EPS (Rs.)	26.03	26.95	30.66	35.69
EBITDA Margin (%)	21%	19%	18%	18%
PAT Margin (%)	8%	7%	7%	7%
P/E Ratio (x)	12.10	11.69	10.27	8.83
ROE (%)	19%	20%	18%	17%
ROCE (%)	28%	24%	22%	22%
Debt-Equity Ratio	4.28	4.10	4.54	4.66
Book Value (Rs.)	0.99	1.47	1.26	1.09
P/BV	139.18	139.18	169.83	205.52

Charts







Outlook and Conclusion

- At the current market price of Rs.315.00 the stock is trading at a P/Ex of 10.27x for FY11E and 8.83x for FY12E.
- The EPS of the stock is expected to be at Rs.30.66 and Rs.35.69 for FY11E and FY12E respectively.
- On the basis of price to book value, the stock trades at 1.85x and 1.53x for FY11E and FY12E respectively.
- The Net sales and PAT of the company is expected to grow at a CAGR of 13% and 11% respectively over FY09 to FY12E.
- Company is planning to enter women's and kids' wear segment soon. In an attempt to strengthen its margins, Koutons Retail India has planned to take up this initiative all across India very soon.
- Koutons India Retails Ltd will expand its product line and launch its own brand of shoes by end 2010.
- The company, which had recently set a record of opening 100 stores in a single day, is aiming to break its own record by opening 200 stores across the country.

- Koutons is in full swing to enter the Saarc countries and West Asia after consolidating its position in the domestic market. Koutons currently has 600 stores across the nation and plans to take it to 1,000 by the end of the next year.
- The newly added brand of Koutons, Charlie Outlaw, is also having 300 stores across the nation and the expansion plan is aimed at having 2000 stores of Charlie Outlaw in India by next year.
- The company is planning to enhance its current store size to 5,000-6,000 sft after launching the three products.
- Koutons Retail plans to open flagship outlets in metros and Tier-1 cities. These outlets will store the entire range of the company including men, women and kids wear, depending upon the demographics of the region.
- The company has entered into fabrication agreement with various manufacturers to which it outsource stitching of apparels through the design and fabric provided by it.
- We are positive on the business model of the company. The customers benefit due to availability of quality products with affordable prices. The franchisees do not suffer due to the minimum guarantee given and the interest paid on security deposit.
- We expect that the company will keep its growth story in the coming quarters also. We recommend **'STRONG BUY'** in this particular scrip with a target price of Rs.378.00 for Medium to Long term investment.

Industry Overview

The Indian retail market, which is the fifth largest retail destination globally, has been ranked as the most attractive emerging market for investment in the retail sector by AT Kearney's eighth annual Global Retail Development Index (GRDI), in 2009. The share of retail trade in the country's gross domestic product (GDP) was between 8–10 per cent in 2007. It is currently around 12 per cent, and is likely to reach 22 per cent by 2010.

A McKinsey report 'The rise of Indian Consumer Market', estimates that the Indian consumer market is likely to grow four times by 2025. Commercial real estate services company, CB Richard Ellis' findings state that India's retail market is currently valued at US\$ 511 billion. Further, CB Richard Ellis states that India has moved up to the 39th most preferred retail destination in the world in 2009, up from 44 last year.

Banks, capital goods, engineering, fast moving consumer goods (FMCG), software services, oil marketing, power, two-wheelers and telecom companies are leading the sales and profit growth of India Inc in the fourth quarter of 2008-09. India continues to be among the most attractive countries for global retailers. At US\$ 511 billion in 2008,

its retail market is larger than ever and drawing both global and local retailers. Foreign direct investment (FDI) inflows as on July 2009, in single-brand retail trading, stood at approx. US\$ 46.60 million, according to the Department of Industrial Policy and Promotion (DIPP).

India's overall retail sector is expected to rise to US\$ 833 billion by 2013 and to US\$ 1.3 trillion by 2018, at a compound annual growth rate (CAGR) of 10 per cent. As a democratic country with high growth rates, consumer spending has risen sharply as the youth population (more than 33 percent of the country is below the age of 15) has seen a significant increase in its disposable income. Consumer spending rose an impressive 75 per cent in the past four years alone. Also, organized retail, which is pegged at around US\$ 8.14 billion, is expected to grow at a CAGR of 40 per cent to touch US\$ 107 billion by 2013.

The organized retail sector, which currently accounts for around 5 per cent of the Indian retail market, is all set to witness maximum number of large format malls and branded retail stores in South India, followed by North, West and the East in the next two years.

According to the report 'Mall Realities India 2010' by leading property consultants, Jones Lang LaSalle Meghraj and Cushman & Wakefield India in association with Shopping Centers Association of India, over 100 malls of over 30 million sq feet of new shopping centre space are projected to open in India between 2009 and end-2010.

Further, this sector is expected to invest around US\$ 503.2 million in retail technology service solutions in the current financial year. This could go further up to US\$ 1.26 billion in the next four to five years, at a CAGR of 40 per cent.

India has emerged the third most attractive market destination for apparel retailers, according to a study by global management consulting firm AT Kearney. It further says that in India, apparel is the second largest retail category and is expected to grow by 12-15 per cent per year. Apparel, along with food and grocery, will lead the organized retailing in India.

India has one of the largest numbers of retail outlets in the world. The sector is witnessing exponential growth with retail developments taking place not only in major cities and metros but even in tier-II and tier-III cities in India.

- Marks & Spencer Reliance India is planning to open 35 more stores over the next five years, according to Mark Ashman, CEO of the company. The 51:49 joint ventures between UK's Marks and Spencer and Reliance Retail Ltd already have 15 stores in India.
- Carrefour SA, Europe's largest retailer, may start wholesale operations in India by 2010 and plans to set up its first cash-and-carry outlet in the National Capital Region. Currently, Carrefour exports goods worth US\$ 170 million from India to Europe, UAE, Indonesia, Europe, Thailand, Singapore and Malaysia.

- Jewellery manufacturer and retailer, Gitanjali Group and MMTC are jointly setting up a chain of exclusive retail outlets called Shuddi-Sampurna Vishwas. The joint venture, which plans to open around 60 stores across India by end of this year, will retail hallmarked gold and diamond jewellery.
- Mahindra Retail, a part of the US\$ 6.7-billion Mahindra Group, plans to invest US\$ 19.8 million by 2010 to step up its specialty retail concept 'Mom and Me'.
- Pantaloon Retail India (PRIL) plans to invest more than US\$ 103.3 million to expand its seamless mall Central and the value fashion format Brand Factory over the next two years.
- Bharti Retail has introduced eight Wal-Mart private labels—including two of its largest, 'Great Value' and 'George'—in its supermarket chain Easyday, hoping to attract more consumers with their international design and packaging.
- Italian sportswear brand Lotto will launch two new footwear brands Sabots and Calcetto in the country in the next few weeks. The plan is to have at least 50 exclusive outlets by March 2010.
- Steel players such as JSW Steel and Essar Steel are increasing their focus on opening up more retail outlets pan India. JSW Steel currently has 50 such steel retail outlets called JSW Shoppe and is targeting to increase it to 200 by March 2010. Similarly, Essar Steel also has such retail outlets called Essar hypermarts. With a total 150 such outlets currently, this segment contributes to about 20-25 per cent to the Essar's total revenue.
- EBONY Homes, the home furniture retail arm of the US\$ 3 billion DS Constructions, has plans to invest US\$ 25.1 billion to set up a chain of 20-25 furniture stores styled Ebony Gautier across the country by March 2012.
- Gujarat Co-operative Milk Marketing Federation (GCMMF), which owns and markets Asia's largest dairy brand, Amul, plans to add 6,000 Amul retail parlours across the country in FY 2009.
- With rentals dropping sharply, large retailers such as Aditya Birla Retail, Reliance Retail and Shoppers Stop, and food chains such as McDonald's are also looking at metros and mini-metros for expansion.
- Many major international brands are also looking for a foothold in India. The brands planning an India entry include The Pizza Company and Spicchio Pizza (both pizza chains from Thailand), Coffee Club from Australia, Japanese brand Lolita Fashion, Revive Juice Bars from the UK, Mrs Fields Cookies and Jamba Juice from the US, and French fashion brand Jules.
- Retail brands such as United Colors of Benetton, Tommy Hilfiger and Puma are opening factory outlets to sell excess stock and woo the price-conscious buyers.

Policy Initiatives

- 100 per cent FDI is allowed in cash-and-carry wholesale formats. Franchisee arrangements are also permitted in retail trade.
- 51 per cent FDI is allowed in single-brand retailing.

Road Ahead

According to industry experts, the next phase of growth is expected to come from rural markets, with rural India accounting for almost half of the domestic retail market, valued over US\$ 300 billion. Rural India is set to witness an economic boom, with per capita income having grown by 50 per cent over the last 10 years, mainly on account of rising commodity prices and improved productivity.

According to retail and consumer products division, E&Y India, basic infrastructure, generation of employment guarantee schemes, better information services and access to funding are also bringing prosperity to rural households. The rural market, product design will need to go beyond ideas like smaller sizes (such as single use sachets) to create genuinely new products.

According to a new market research report by RNCOS titled, 'Booming Retail Sector in India', organized retail market in India is expected to reach US\$ 50 billion by 2011.

- Number of shopping malls is expected to increase at a CAGR of more than 18.9 per cent from 2007 to 2015.
- Rural market is projected to dominate the retail industry landscape in India by 2012 with total market share of above 50 per cent.
- Organized retailing of mobile handset and accessories is expected to reach close to US\$ 990 million by 2010.
- Driven by the expanding retail market, third party logistic market is forecasted to reach US\$ 20 billion by 2011.

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