

## Company Results Review

30 April 2007 | 7 pages

# Pantaloon (PART.BO)

## Buy: 3QFY07; Weak Profit but Sales Growth Momentum Continues...

- Mixed 3QFY07: Strong sales, weak profit growth** – Pantaloon reported strong sales growth of 89% in 3QFY07, 5% higher than our expectations, driven by strong growth in both value and lifestyle retailing. Net profit growth at 15%, however, was lower than our expectation of c40% growth.
- Net profit growth of 15% below expectation** – Net profit at Rs187m was lower on account of a lower operating margin, higher depreciation, interest costs and tax rate. Some pressure is visible on staff costs, which rose by 150bps.
- Sales growth momentum strong** – Lifestyle and value retailing, both grew by 85%+, driving the 89% sales growth. We expect the sales growth momentum to continue with the addition of new store and opening of new formats such as Home Town etc.
- Unlocking value through subsidiaries** – Pantaloon is looking to dilute equity in some of its subsidiaries over next 2-3 months to fund growth, which will unlock value. Its subsidiaries in media, logistics, e-tailing etc are being scaled up and are not yet captured in our target price. We do, however, factor in the value of Home Solutions and Future Capital subsidiaries into our target price valuation.
- Maintain Buy/Medium Risk (1M)** – We remain positive on Pantaloon's growth story. We recently upgraded the stock to a Buy / Medium Risk (1M) with a target price of Rs500. We believe value unlocking from its subsidiaries, judicious roll-out of new store formats, lease rentals locked in at lower than average rates will give Pantaloon an edge over its peers.

### Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
30 Jun	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2005A	386	3.51	69.4	117.2	20.4	24.4	0.1
2006A	642	4.86	38.5	84.6	10.3	17.1	0.1
2007E	1,049	7.24	48.9	56.8	6.6	14.6	0.1
2008E	1,890	13.03	80.1	31.6	7.4	22.0	0.2
2009E	2,394	16.51	26.7	24.9	5.8	26.0	0.2

Source: Powered by dataCentral

See Appendix A-1 for Analyst Certification and important disclosures.

<b>Buy/Medium Risk</b>	<b>1M</b>
Price (27 Apr 07)	Rs411.25
Target price	Rs500.00
Expected share price return	21.6%
Expected dividend yield	0.2%
<b>Expected total return</b>	<b>21.7%</b>
Market Cap	Rs57,858M US\$1,422M

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



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Fiscal year end 30-Jun	2005	2006	2007E	2008E	2009E
<b>Valuation Ratios</b>					
P/E adjusted (x)	117.2	84.6	56.8	31.6	24.9
EV/EBITDA adjusted (x)	66.3	43.3	27.5	16.2	13.0
P/BV (x)	20.4	10.3	6.6	7.4	5.8
Dividend yield (%)	0.1	0.1	0.1	0.2	0.2
<b>Per Share Data (Rs)</b>					
EPS adjusted	3.51	4.86	7.24	13.03	16.51
EPS reported	3.51	4.86	7.24	13.03	16.51
BVPS	20.14	39.91	62.62	55.61	71.19
DPS	0.50	0.51	0.36	0.65	0.83
<b>Profit &amp; Loss (RsM)</b>					
Net sales	10,528	18,678	31,079	56,094	76,930
Operating expenses	-9,753	-17,465	-29,108	-52,555	-72,099
<b>EBIT</b>	<b>775</b>	<b>1,212</b>	<b>1,971</b>	<b>3,539</b>	<b>4,831</b>
Net interest expense	-275	-335	-640	-860	-1,410
Non-operating/exceptionals	31	42	800	100	100
<b>Pre-tax profit</b>	<b>531</b>	<b>919</b>	<b>2,131</b>	<b>2,779</b>	<b>3,521</b>
Tax	-145	-277	-682	-889	-1,127
Extraord./Min.Int./Pref.div.	0	0	-400	0	0
<b>Reported net income</b>	<b>386</b>	<b>642</b>	<b>1,049</b>	<b>1,890</b>	<b>2,394</b>
Adjusted earnings	386	642	1,049	1,890	2,394
Adjusted EBITDA	909	1,420	2,270	4,070	5,574
<b>Growth Rates (%)</b>					
Sales	60.1	77.4	66.4	80.5	37.1
EBIT adjusted	68.0	56.3	62.6	79.5	36.5
EBITDA adjusted	65.3	56.3	59.8	79.3	36.9
EPS adjusted	69.4	38.5	48.9	80.1	26.7
<b>Cash Flow (RsM)</b>					
<b>Operating cash flow</b>	<b>-403</b>	<b>-2,626</b>	<b>-1,085</b>	<b>381</b>	<b>-2,023</b>
Depreciation/amortization	133	208	299	531	743
Net working capital	-1,020	-3,610	-2,575	-2,089	-5,160
<b>Investing cash flow</b>	<b>-1,145</b>	<b>-1,335</b>	<b>-1,935</b>	<b>-1,166</b>	<b>0</b>
Capital expenditure	-1,145	-1,335	-1,935	-1,166	0
Acquisitions/disposals	0	0	0	0	0
<b>Financing cash flow</b>	<b>1,133</b>	<b>5,565</b>	<b>4,723</b>	<b>3,642</b>	<b>6,739</b>
Borrowings	496	3,152	1,983	2,749	6,875
Dividends paid	-63	-77	-59	-107	-135
<b>Change in cash</b>	<b>-415</b>	<b>1,604</b>	<b>1,703</b>	<b>2,858</b>	<b>4,717</b>
<b>Balance Sheet (RsM)</b>					
<b>Total assets</b>	<b>6,651</b>	<b>14,174</b>	<b>21,153</b>	<b>26,388</b>	<b>38,862</b>
Cash & cash equivalent	215	218	300	5	5
Accounts receivable	123	170	255	307	422
Net fixed assets	2,295	3,955	5,169	8,509	11,294
<b>Total liabilities</b>	<b>4,441</b>	<b>8,916</b>	<b>12,073</b>	<b>18,324</b>	<b>28,539</b>
Accounts payable	1,271	2,298	3,189	5,955	8,583
Total Debt	2,862	6,014	7,997	10,746	17,620
<b>Shareholders' funds</b>	<b>2,215</b>	<b>5,269</b>	<b>9,080</b>	<b>8,064</b>	<b>10,323</b>
<b>Profitability/Solvency Ratios (%)</b>					
EBITDA margin adjusted	8.6	7.6	7.3	7.3	7.2
ROE adjusted	24.4	17.1	14.6	22.0	26.0
ROIC adjusted	15.6	12.4	10.6	15.3	15.0
Net debt to equity	119.5	110.0	84.8	133.2	170.6
Total debt to capital	56.4	53.3	46.8	57.1	63.1

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Figure 1. Pantaloon 3QFY07: Profit and Loss Summary (Rupees in Millions)

	3QFY06	3QFY07	% Change
<b>Net Sales</b>	<b>4,554.0</b>	<b>8,610.5</b>	<b>89.1</b>
Total Expenditure	-4,169.0	(8,007.7)	92.1
<b>EBITDA</b>	<b>385.0</b>	<b>602.7</b>	<b>56.6</b>
<i>EBITDA Margin (%)</i>	<i>8.5</i>	<i>7.0</i>	<i>(17.2)</i>
Interest	-100.7	(228.9)	127.2
Depreciation	-58.6	(93.3)	59.2
Other Income	4.6	9.4	102.2
<b>PBT</b>	<b>230.3</b>	<b>289.9</b>	<b>25.9</b>
Tax	-67.9	(102.8)	51.4
<i>Tax Rate (%)</i>	<i>29.5</i>	<i>35.5</i>	<i>20.2</i>
<b>PAT</b>	<b>162.4</b>	<b>187.2</b>	<b>15.3</b>

Source: Company

Figure 2. Pantaloon 3QFY07: Cost Details (Rupees in Millions)

	3QFY06	3QFY07	% Change
<b>Net Sales</b>	<b>4,554.0</b>	<b>8,610.5</b>	<b>89.1</b>
Raw Materials and Finished Goods	3,034.6	5,808.8	91.4
<i>% of Sales</i>	<i>66.6</i>	<i>67.5</i>	<i>1.2</i>
Staff Costs	246.7	536.6	117.5
<i>% of Sales</i>	<i>5.4</i>	<i>6.2</i>	<i>15.0</i>
Other Expenditure	887.6	1,662.3	87.3
<i>% of Sales</i>	<i>19.5</i>	<i>19.3</i>	<i>(1.0)</i>

Source: Company

Figure 3. Pantaloon: Segmental Details (Rupees in Millions)

	3QFY06	3QFY07	% Change
Value Retailing	2,978.6	5,584.7	87.5
Lifestyle: Retailing	1,528.1	2,833.3	85.4
Others	119.1	302.6	154.2
Less: Inter-segment sales	71.9	110.1	53.2
<b>Net Sales</b>	<b>4,554.0</b>	<b>8,610.5</b>	<b>89.1</b>
<b>EBIT</b>			
Value Retailing	233.5	421.6	80.6
Lifestyle Retailing	214.9	363.7	69.3
<b>Total</b>	<b>448.4</b>	<b>785.3</b>	<b>75.1</b>
<b>EBIT (%)</b>			
Value Retailing	7.8	7.6	-29 bps
Lifestyle Retailing	13.0	11.6	-145 bps

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 3.5m sq. ft. with plans to expand to 30m 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 presence in retail property management services through Central Malls, managing retail space for concessionaries 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 thesis**

We rate Pantaloon shares Buy / Medium Risk (1M) with a target price of Rs500. In the near term, stock upside triggers should come from stake sales in subsidiaries. We include the Home Solutions and Future Capital subsidiaries into our valuations. We believe that the risk profile of the business has come down, and that Pantaloon is now better positioned to grow from its current base. While we are cognizant of the emerging competitive landscape, we believe that Pantaloon has sustainable competitive advantages: 1) strong brands and well-established retail formats; 2) judicious product mix; 3) below-market rentals locked in with long-term leases, and 4) longstanding experience in understanding Indian consumer behavior.

### **Valuation**

Our price target is based on sum of the parts. We value parent Pantaloon Retail at Rs390 per share based on 30x FY08E P/E, similar to early-stage valuations for Chinese retailers. Our 30x multiple is also benchmarked against our regional retail universe. We expect a two-year EPS CAGR of 64% for Pantaloon, vs. 30% for our Asian retail universe. We benchmark valuations of Home Solutions against recent stake sales (mid point of Rs7.5bn-Rs10bn). We also use Market Cap/Sales valuation of 1.2x FY08E, at par with Pantaloon's valuations. Our fair value per share for the Home Solutions subsidiary is Rs60 per share. We attribute per share value of Future Capital, Pantaloon's 74% subsidiary, at Rs50, based on the NPV of cash flows to Pantaloon from the three 7-year close-ended funds (management fee + carry). We assume a 15% increase in the fund NAV every year, and a 13% discount rate to calculate NPV of cash flows.

### **Risks**

We assign a Medium Risk rating to Pantaloon Retail shares based on our quantitative risk-rating system. The main downside risks to the shares reaching our target price include: 1) any delay in store opening plans; 2) legislative changes that allow FDI in retail; 3) increase in competitive intensity, irrational competition, and 4) continued pressure on rentals, which could result in lower-than-expected margins. The main upside risks include: 1) better-than-expected sales growth; 2) Value unlocking in subsidiaries through listing/stake sales, and 3) any significant acquisitions perceived to be creating value.

## Appendix A-1

### Analyst Certification

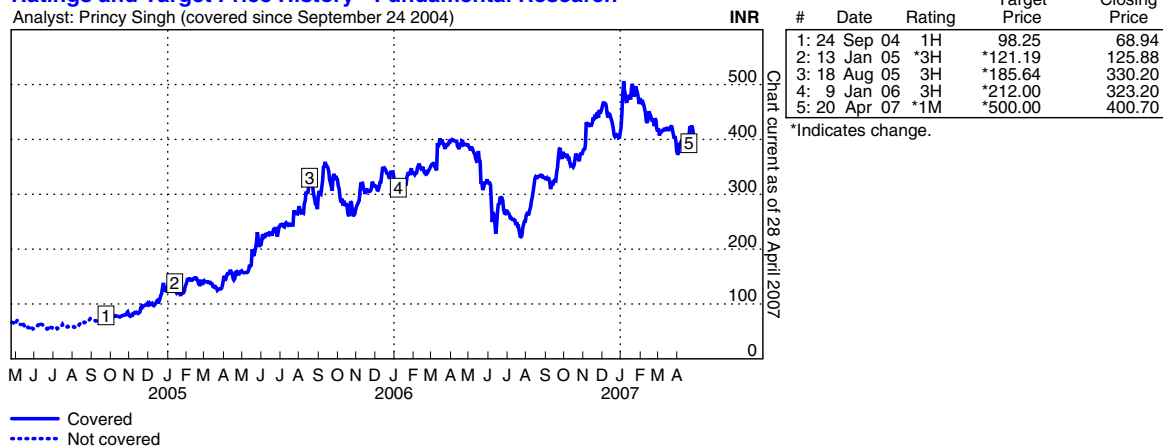
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Analyst: Princy Singh (covered since September 24 2004)



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