

Aditya Birla Fashion & Retail Ltd.: Q3FY18 Result Update

CMP INR: 156
 Rating: BUY
 Target Price INR: 256
 Upside: 64%

Profitability is back

We have been wrong on ABFRL over the past few quarters with the company underperforming our estimates and therefore the broader markets. This has been on account of multiple unforeseen events (competition from e-commerce in FY16, demonetization in FY17, GST in FY18) which led to heavy volatility in quarterly performances for companies across the sector. In addition, apparel business is inventory driven which has a limited shelf life due to constant changes in trends; and hence heavy discounting occurs during such unforeseen events. As apparel and retail is a high operating leverage business, the profitability was accounted by such discounting. ABFRL in particular, has spent heavily in new businesses such as Forever 21, Pantaloons and innerwear which have further compressed profitability. We feel that the worst is over for the sector and moreover for ABFRL with the foundation led for strong profitable growth. Its sheer brand strength alongwith a prudent long term strategy render it a multi-bagger. We re-iterate BUY as we roll over to FY20E with a revised TP of INR 256 (INR 205 earlier).

Kshitij Kaji
 Research Analyst
 kshitij.kaji@edelweissfin.com

Praveen Sahay
 Research Analyst
 Praveen.sahay@edelweissfin.com

Madura and Pantaloons on track

ABFRL reported a 9% revenue growth which was slightly below expectations due to slower growth in Pantaloons and a slow October. However EBITDA margins improved from 5.1% in Q3FY17 to 7.4% in Q3FY18 which was above our estimates and led by Pantaloons. Madura has grown 8.2% in Q3FY18 with margins improving from 9.5% in Q3FY17 to 11.6% in Q3FY18. LTL was strong at 4% and the wholesale channel is also recovering. Pantaloons revenues grew 12% with flat SSG. However, Pantaloons has undergone cost rationalization in terms of resizing and rental terms which led to margins improving from 5.4% to a life-high 8.7%. While these margins are not sustainable, we feel that Pantaloons margins could surprise positively once SSG arrives. Pantaloons store expansion will continue at its current trend of 60-80 new stores with 20% on franchisee basis. Pantaloons has already turned cash positive and is now capable of funding itself for future growth.

Mixed results in new businesses

Innerwear continues to grow rapidly as it was opened in ~6000 outlets across 75 towns within 12 months of launch. Losses in the innerwear business are likely to persist due to high growth potential. Forever 21 revenues were lower due to closure/resizing of stores and slower store openings. Losses widened due to a one time inventory markdown of INR 16 Cr. Current store size and higher costs need to be rationalized to take on the increased competition in this segment. American Eagle and Ted Baker stores are likely to be launched next quarter.

Outlook and valuations: 'BUY'

We believe ABFRL is best placed among branded apparel peers to reap significant benefits of the improving macroeconomic milieu due to the sheer quality & size of Madura's 4 brands, presence in fastest growing segments such as value and fast fashion and an unparalleled distribution network. The company's pole position, ability to generate free cash flow, and RoCE expansion will yield target multiple of 3x sales for Madura and 15x EV/EBITDA for Pantaloons, leading to a revised target price of INR 256 (INR 205 earlier). We re-iterate our Buy rating.

Year to March	Q3FY18	Q3FY17	% change	Q2FY18	% change	FY17	FY18E	FY19E
Net sales	1855	1707	9%	1804	3%	6,633	7,498	8,577
% growth							13%	14%
EBITDA	138	88	57%	119	16%	438	517	729
Adj PAT	35	-12	NA	-10	NA	54	84	255
% growth							55%	205%
Dil. EPS (INR)						0.7	1.1	3.3
Diluted P/E (x)						224	144	47
EV/EBITDA (x)						32	27	19
ROCE (%)						7%	7%	14%

Bloomberg:	ABFRL:IN
52-week range (INR):	188/127
Share in issue (cr):	77.2
M cap (INR cr):	12,000
Avg. Daily Vol. BSE/NSE :('000):	1200
Promoter Holding (%)	59.2

Date: 2nd February 2018

Q3FY18 Result Highlights

Particulars	Q3FY18	Q3FY17	% change	Q2FY18	% change	FY17	FY18E	FY19E
Income from operations	1855	1707	9%	1804	3%	6,633	7,498	8,577
Cost of goods sold	865	780	11%	866	0%	3,018	3,374	3,774
Employee expenses	209	185	13%	197	6%	663	712	815
Other expenses	643	654	-2%	622	3%	2,514	2,894	3,259
Total operating expenses	1,717	1,619	6%	1,685	2%	6,195	6,981	7,848
EBITDA	138	88	57%	119	16%	438	517	729
Depreciation and amortization	67	65	3%	67	0%	242	289	309
EBIT	71	23	NA	52	37%	196	228	420
Interest expenses	43	43	0%	43	0%	180	162	144
Other income	7	8	-13%	7	0%	38	38	42
PBT	35	-12	NA	16	NA	54	104	318
Provision for tax	0	0	NA	0	NA	0	21	64
Core profit	35	-12	NA	16	NA	54	84	255
Extraordinary items	0	0	NA	-26	NA	0	0	0
Adjusted net profit	35	-12	NA	-10	NA	54	84	255
Equity capital (FV INR 10)						772	772	772
No. of shares (Cr)						77	77	77
Diluted EPS (INR)						0.7	1.1	3.3

Financials

Financial Statements						Balance sheet					
INR Cr						INR Cr					
Year to March	FY16	FY17E	FY18E	FY19E	FY20E	As on 31st March	FY16	FY17E	FY18E	FY19E	FY20E
Net revenue	6,060	6,633	7,498	8,577	9,868	Equity capital	769	772	772	772	772
Materials costs	2,755	3,018	3,374	3,774	4,342	Reserves & surplus	174	224	308	562	986
Gross profit	3,305	3,615	4,124	4,803	5,526	Borrowings	1,858	1,950	1,875	1,600	1,300
Employee costs	597	663	712	815	937	Other long-term liabilities	100	100	100	100	100
Other costs	2,311	2,514	2,894	3,259	2,664	Sources of funds	2,902	3,047	3,055	3,035	3,158
EBITDA	397	438	517	729	937	Gross Block	1,698	2,048	2,398	2,748	3,098
Depreciation & Amortization	338	242	289	309	322	Accumulated Depreciation	(1,126)	(1,369)	(1,658)	(1,967)	(2,289)
EBIT	59	196	228	420	616	CWIP	-	-	-	-	-
Other income	12	38	38	42	44	Net Fixed Assets	572	679	740	781	809
EBIT incl. other income	71	234	266	462	660	Net intangible assets	1,775	1,775	1,775	1,775	1,775
Interest expenses	175	180	162	144	131	Investments	272	272	272	272	272
Profit before tax	-104	54	104	318	529	Inventories	1,388	1,509	1,646	1,755	2,171
Provision for tax	0	0	21	64	106	Sundry debtors	391	400	411	517	595
Adjusted Profit	-104	54	84	255	424	Cash and equivalents	20	22	(44)	(176)	(183)
Basic shares outstanding (Cr)	76.9	77.2	77.2	77.2	77.2	Loans and advances	200	200	200	200	200
EPS (INR)	-1.4	0.7	1.1	3.3	5.5	Total current assets	1,999	2,131	2,213	2,297	2,783
Dividend per share (INR)	0.0	0.0	0.0	0.0	0.0	Sundry creditors and others	1,437	1,530	1,664	1,809	2,201
Dividend payout (%)	0%	0%	0%	0%	0%	Provisions	280	280	280	280	280
Common size metrics - as % of net revenues						Total current liabilities & provisions	1,717	1,810	1,944	2,089	2,481
Year to March	FY16	FY17E	FY18E	FY19E	FY20E	Net current assets	283	321	269	207	302
COGS	45.5%	45.5%	45.0%	44.0%	44.0%	Deferred tax assets	-	-	-	-	-
Employee Exp	9.9%	10.0%	9.5%	9.5%	9.5%	Other long-term assets	-	-	-	-	-
Other Exp	27.4%	27.0%	28.6%	28.0%	27.0%	Uses of funds	2,902	3,047	3,055	3,035	3,158
Depreciation	5.6%	3.6%	3.9%	3.6%	3.3%	Book value per share (INR)	12.3	12.9	14.0	17.3	22.8
EBITDA margins	6.6%	6.6%	6.9%	8.5%	9.5%	Free cash flow					
EBIT margins	1.0%	3.0%	3.0%	4.9%	6.2%	Year to March	FY16	FY17E	FY18E	FY19E	FY20E
Adj profit margins	-1.7%	0.8%	1.1%	3.0%	4.3%	Net profit	-104	54	84	255	424
Net profit margins	-1.7%	0.8%	1.1%	3.0%	4.3%	Add : Depreciation	338	242	289	309	322
Growth ratios (%)						Others	163	142	124	102	86
Year to March	FY16	FY17E	FY18E	FY19E	FY20E	Gross cash flow	397	438	497	665	832
Revenues	NA	9.5%	13.0%	14.4%	15.0%	Changes in WC	-217	-37	-14	-70	-102
EBITDA	NA	10.2%	18.2%	40.9%	28.6%	Operating cash flow	180	401	483	595	729
PBT	NA	NA	94.1%	204.9%	66.3%	Capex	-300	-350	-350	-350	-350
Adj profit	NA	NA	55.3%	204.9%	66.3%	Free cash flow	-120	51	133	245	379
Net profit	NA	NA	55.3%	204.9%	66.3%	Cash flow metrics					
Profitability & efficiency ratios						Year to March	FY16	FY17E	FY18E	FY19E	FY20E
Year to March	FY16	FY17E	FY18E	FY19E	FY20E	Cash flow from operations	179.8	401.0	482.8	595.3	729.4
ROAE (%)	NA	6%	8%	21%	27%	Cash flow from investing activities	-185.4	-312.0	-312.0	-308.0	-306.0
ROACE (%)	3%	7%	7%	14%	20%	Cash flow from financing activities	299.4	-88.7	-237.0	-419.0	-430.5
ROIC (%)	3%	7%	7%	12%	16%	Capex	-785.4	-350.0	-350.0	-350.0	-350.0
Inventory day	84	83	80	75	183	Dividends	-	-	-	-	-
Debtors days	24	22	20	22	22	Operating ratios					
Payable days	87	84	81	77	185	Year to March	FY16	FY17E	FY18E	FY19E	FY20E
Cash conversion cycle (days)	16	16	15	16	18	Total asset turnover	2.6	2.2	2.5	2.8	3.2
Current ratio	1.2	1.2	1.2	1.2	1.2	Fixed asset turnover	4.6	3.5	3.4	3.3	3.4
Debt/Equity	2.0	2.0	1.7	1.2	0.7	Equity turnover	9.4	6.8	7.2	7.1	6.4
Core ROACE (%)	7%	17%	18%	30%	41%	Du pont analysis					
Operating ratios						Year to March	FY16	FY17E	FY18E	FY19E	FY20E
Year to March	FY16	FY17E	FY18E	FY19E	FY20E	NP margin (%)	-1.7%	0.8%	1.1%	3.0%	4.3%
Total asset turnover	2.6	2.2	2.5	2.8	3.2	Total assets turnover	2.6	2.2	2.5	2.8	3.2
Fixed asset turnover	4.6	3.5	3.4	3.3	3.4	Leverage multiplier	3.6	3.1	2.9	2.5	2.0
Equity turnover	9.4	6.8	7.2	7.1	6.4	ROAE (%)	NA	5.5%	8.0%	21.1%	27.4%
Valuation parameters						Valuation parameters					
Year to March	FY16	FY17E	FY18E	FY19E	FY20E	Year to March	FY16	FY17E	FY18E	FY19E	FY20E
Diluted EPS (INR)	-1.4	0.7	1.1	3.3	5.5	Diluted EPS (INR)	-1.4	0.7	1.1	3.3	5.5
Y-o-Y growth (%)	NA	NA	55.3	204.9	66.3	Y-o-Y growth (%)	NA	NA	55.3	204.9	66.3
Diluted PE (x)	NA	223.9	144.2	47.3	28.4	Diluted PE (x)	NA	223.9	144.2	47.3	28.4
Price/BV (x)	12.7	12.1	11.2	9.0	6.9	Price/BV (x)	12.7	12.1	11.2	9.0	6.9
EV/Sales (x)	2.3	2.1	1.8	1.6	0.9	EV/Sales (x)	2.3	2.1	1.8	1.6	0.9
EV/EBITDA (x)	34.9	31.6	26.7	19.0	9.1	EV/EBITDA (x)	34.9	31.6	26.7	19.0	9.1
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0	Dividend yield (%)	0.0	0.0	0.0	0.0	0.0

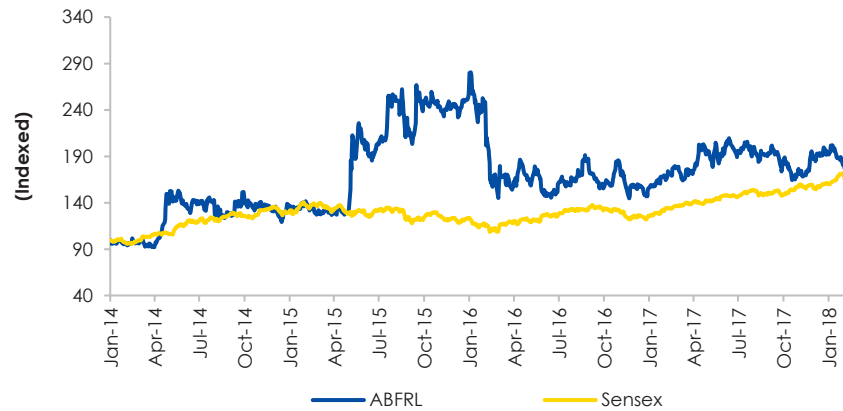
Edelweiss Broking Limited, 1st Floor, Tower 3, Wing B, Kohinoor City Mall, Kohinoor City, Kirod Road, Kurla(W)
Board: (91-22) 4272 2200

Vinay Khattar

Head Research

vinay.khattar@edelweissfin.com

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate between 5-15% over a 12-month period
Reduce	Return below 5% over a 12-month period



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