March 26, 2020

Covid-19 to subdue near term revenue growth…

The Indian retail sector faces unprecedented circumstances owing to the Coronavirus (Covid-19) outbreak leading to a nationwide lockdown announced by the Central government along with other stringent restrictions imposed by several state governments on movement of men and material. The impact is likely to vary depending on whether the consumption pattern is discretionary or essential utility.

- Companies with high share of discretionary products such as apparel, jewellery, footwear and other accessories are expected to witness a sharper decline in revenue growth in the short-term as consumers may restrict their discretionary purchase
- Post normalisation, discretionary categories like jewellery, apparel and footwear could see some revival of revenue growth due to pent up consumer demand. However, given the discretionary nature, the entire revenue loss may not be entirely recouped in FY21
- On the other hand, companies in the grocery and essential product business are expected to witness a limited impact and a spurt in revenue growth in Q4FY20 owing to pantry-filling
- Q4, on an average, contributes ~24% of annual revenues for Titan, Trent and Bata. Most companies had end of season sales in Q4 (January-February), which did not see a significant disruption due to Covid-19 as store closures started in mid-March
- Among retail companies, Q1 revenue contribution to total revenues for Titan, Trent is ~24% while for Bata it is ~ 28% as in Q1 Bata has higher revenues owing to sales of school shoes (unlikely to be impacted much as major sales happen in June)
- Overall, for our retail universe, we have assumed store closure of nearly two months and have pruned our revenue growth estimates by 11-12% in FY21@ factoring in lower SSSG
- Furthermore, the management may revisit the store expansion plans for FY21 impacting topline growth
- On the cost front, given the high fixed cost nature of the retail business (rental & employee expense: 10-15% each), a fall in footfalls would result in a more than proportionate decline in profitability for players
- Major retail chains are in negotiations with mall owners for exemption or rebate in rentals to overcome the decline in revenues
- With a continuous change in fashion season cycles, apparel retailers may indulge in higher discounting strategies (impacting gross margins) in a bid to reduce old season inventory
- We revise downwards our EBITDA growth estimates for discretionary retail players in FY21E in the range of 20-30%

Valuation & Outlook

Covid-19 is still at an early stage in India and the quantum of the impact can only be assessed in coming quarters. **We anticipate next two quarters will be difficult for all retail sector companies whose product portfolio is skewed towards discretionary products. Though the near term performance of the retail sector is expected to be negatively impacted, we prefer fundamentally sound companies, with strong brands and good promoter pedigree.** Large retail companies and category leaders (Titan, Bata) will be able to tide over the current scenario by adapting to the new situation better than smaller companies by tweaking their business model as was evident in earlier disruptions like demonetisation and GST implementation. **Hence, in our coverage, we recommend BUY on Bata, Titan, Trent, ABFRL and Avenue Supermarts**.

Recommend BUY** on companies with strong balance sheet, established brands with good promoter pedigree viz. **Titan Company, Trent, Bata, Aditya Birla Fashion, and Avenue Supermarts

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Exhibit 1: Recommendation change

	Old			New		Upside (%)
Company	Target Price	Rating	CMP	Target Price	Rating	
Bata	1955	Hold	1200	1480	Buy	23%
Titan	1470	Buy	910	1100	Buy	21%
Trent	725	Buy	495	610	Buy	23%
Avenue Supermarts	1700	Reduce	1995	2330	Buy	17%
Aditya Birla Fashion	300	Buy	165	225	Buy	36%

Source: Company, ICICI Direct Research

Stock specific comments

Bata: Bata may witness near term supply disruption as the company procures certain finished goods from China. As on FY19, the company sold ~4.7 crore pairs of which 2.7 crore pairs were manufactured in-house (rest being procured from India, while others imported). On the demand front, we believe the revenue growth may get derailed in Q4FY20 and Q1FY21 owing to a decline in footfall in retail stores, especially high ticket size items. Over the longer term, Bata continues to remain a preferred pick owing to its strong balance sheet (healthy cash and bank balance of ₹ 839 crore and negative working capital cycle). The share of premium products for Bata is now at ~50%. Also, its continuous pursuit of premiumisation of the product portfolio would maintain the positive margin growth trajectory, going ahead. The stock price has corrected by ~36% over the last month and offers an attractive entry point. We believe that with its strong brand patronage and pan-India retail reach, Bata India should be able to revive its revenue growth trajectory as and when the impact of Covid-19 is phased out. **Owing to the significant decline in stock price, we upgrade the stock from HOLD to BUY with a revised target price of ₹ 1480 (40x FY22 EPS).**

Exhibit 2: Change in estimates

	FY20E			FY21E			FY22E		
(₹Crore)	Old	New	% Change	Old	New	% Change	Old	New	% Change
Revenue	3,206.1	3,074.9	-4.1	3,602.4	3,198.8	-11.2	4,017.1	3,695.9	-8.0
EBITDA	564.3	507.4	-10.1	659.2	521.4	-20.9	747.2	657.9	-12.0
EBITDA Margin (%)	17.6	16.5	-110 bps	18.3	16.3	-200 bps	18.6	17.8	-80 bps
PAT	428.8	383.9	-10.5	503.4	387.9	-22.9	570.6	492.3	-13.7
EPS (₹	33.4	29.9	-10.6	39.2	30.2	-23.0	44.4	38.3	-13.7

Source: Company, ICICI Direct Research

Exhibit 3: Key Financial Summary

₹crore	FY19	FY20E	FY21E	FY22E	CAGR (FY19-22E)
Net Sales	2,928.4	3,074.9	3,198.8	3,695.9	8.1%
EBITDA	477.3	507.4	521.4	657.9	11.3%
PAT	329.7	383.9	387.9	492.3	14.3%
P/E (x)	46.8	40.2	39.8	31.3	
EV/Sales (x)	5.0	4.7	4.5	3.8	
EV/EBITDA (x)	30.6	28.4	27.3	21.3	
RoCE (%)	23.7	21.6	19.8	22.6	
RoE (%)	18.9	18.9	17.2	19.4	

Source: Company, ICICI Direct Research

Avenue Supermarts: The company is expected to report a healthy Q4FY20 owing to the consumer's tendency to stock essential commodities and groceries to provide for contingences in the event of intensification of Covid-19 outbreak in India. However, the same will lead to a moderate performance Q1FY21. We expect the impact of virus to be limited owing to non-discretionary nature of the business. In a bid to reduce promoter stake to 75%, the company had successfully concluded qualified institutional placement (QIP) placement worth ₹ 4100 crore (2.0 crore shares at ₹ 2049/share). Incremental cashflow infusion in the company is expected to significantly shore up store addition pace (as per our calculations ~45 incremental stores can be opened) with foray into newer geographies. D-Mart has a capital efficient business model generating superior RoCE of 23% and fixed asset turnover ratio of 4.1x. The infusion of funds into the business would provide Avenue Supermarts the ammunition to enhance its store expansion pace resulting in higher revenue and profitability. **We upgrade the stock from REDUCE to BUY rating with a revised target price of ₹ 2330 (41.0x FY22E EV/EBITDA).**

Exhibit 4: Change in estimates

	FY 20E			FY 21E			FY 22E
(₹Crore)	Old	New	% Change	Old	New	% Change	Introduced
Revenue	25,533.9	25,789.2	1.0	32,106.7	32,120.1	0.0	41,389.7
EBITDA	2,119.3	2,166.3	2.2	2,697.0	2,730.2	1.2	3,600.9
EBITDA Margin (%)	8.3	8.4	10 bps	8.4	8.5	10 bps	8.7
PAT	1,371.1	1,406.2	2.6	1,763.4	1,921.0	8.9	2,458.3
EPS (₹	22.0	22.5	2.5	28.3	29.8	5.4	38.2

Source: Company, ICICI Direct Research

Exhibit 5: Key Financial Summary

₹crore	FY18	FY19	FY20E	FY21E	FY22E	CAGR (FY19-22E)
Net Sales	15,033.2	20,004.5	25,789.2	32,120.1	41,389.7	27.4%
EBITDA	1,352.8	1,633.3	2,166.3	2,730.2	3,600.9	30.2%
PAT	787.8	902.4	1,406.2	1,921.0	2,458.3	39.7%
P/E (x)	154.4	138.0	88.5	66.9	52.3	
EV/Sales (x)	8.3	6.2	4.8	3.9	3.0	
EV/EBITDA (x)	91.9	76.5	57.7	45.8	34.9	
RoCE (%)	24.7	23.4	25.2	19.7	21.2	
RoE (%)	17.3	16.2	20.1	14.8	15.9	

Source: Company, ICICI Direct Research

Titan Company: The Company is expected to fall short of its guided revenue target of 11-13% revenue growth for the jewellery space owing to a near washout in March. Postponement of wedding dates would negatively impact the performance in Q4FY20 (wedding jewellery: 20% of overall jewellery sales). Volatility in gold prices and reduced demand in discretionary spends are expected to impair consumer demand in the near term. However, the company is likely to recoup lost sales (wedding jewellery) owing to pent up demand from H2FY21. Titan has been the market leader in the Indian jewellery market and has grown at a robust pace compared to a decline at the industry level. **It has a consistent margin profile owing to strong pricing power in terms of higher making charges compared to peers across various gold cycles.** It has consistently exhibited its ability to gain market share amid a tough industry scenario. Robust balance sheet (30%+ RoCE and virtually debt free status) and asset light distribution model have enabled it to outpace peers in terms of store addition. Over the longer term, we expect Titan to be a key beneficiary as India's gold market continues to strive towards regulation and standardization. **We continue to have a BUY rating with a revised target price of ₹ 1100** (43.0x F22E EPS).

Exhibit 6: Change in estimates

	FY20E			FY21E			FY22E		
(₹Crore)	Old	New	% Change	Old	New	% Change	Old	New	% Change
Revenue	21,792.2	20,946.9	-3.9	25,797.4	22,668.2	-12.1	30,346.1	28,186.1	-7.1
EBITDA	2,266.4	2,136.6	-5.7	2,811.9	2,266.8	-19.4	3,443.5	3,114.6	-9.6
EBITDA Margin (%)	10.4	10.2	-20 bps	10.9	10.0	-90 bps	11.3	11.1	-30 bps
PAT	1,612.9	1,515.8	-6.0	2,034.8	1,627.0	-20.0	2,512.3	2,262.5	-9.9
EPS (₹)	18.2	17.1	-6.2	22.9	18.3	-20.0	28.3	25.5	-9.9

Source: Company, ICICI Direct Research

Exhibit 7: Key Financial Summary

(₹Crore)	FY18	FY19	FY20	FY21E	FY22E	CAGR (FY19-22E)
Net Sales	16,119.8	19,778.5	20,946.9	22,668.2	28,186.1	12.5
EBITDA	1,644.7	2,136.5	2,136.6	2,266.8	3,114.6	13.4
PAT	1,130.1	1,404.2	1,515.8	1,627.0	2,262.5	17.2
EPS (₹)	12.7	15.8	17.1	18.3	25.5	
P/E (x)	71.5	57.5	53.3	49.7	35.7	
EV/Sales (x)	5.0	4.0	3.8	3.5	2.8	
EV/EBITDA (x)	48.8	37.3	37.5	35.1	25.3	
RoCE (%)	29.3	32.4	27.4	25.1	29.9	
RoE (%)	22.2	23.2	21.5	20.1	23.6	

Source: Company, ICICI Direct Research

Trent: In the apparel space, Trent has been a consistent outperformer with industry best same store sales growth (for Westside format). Over the last three quarters, the company has recorded 30%+ revenue growth on the back of aggressive store addition pace, coupled with healthy SSSG. The revenue trajectory is expected to get derailed in Q4FY20, Q1FY21 owing to temporary store closures. We expect Trent to exit FY20 with revenue growth of 26% (vs. earlier estimate of 30%). We are also pruning SSSG for Westside stores from 10% in FY21 to 5%. The company, over the last two years, had aggressively shored up its store addition pace with capital infusion by the promoters (₹ 950 crore). We believe momentum in square feet addition would decelerate given the uncertainties in H1FY21. Westside continues to be one of the most successful, established franchises, deriving 97% of share of revenues from private label brands. Higher promoter commitment signifies a positive momentum in core business performance metrics. **We lower our revenue and profit estimates owing to the Covid-19 impact and revise our target price to ₹ 610 based on SOTP valuation.**

Exhibit 8: Change in estimates

	FY20E			FY21E			FY22E		
(₹Crore)	Old	New	% Change	Old	New	% Change	Old	New	% Change
Revenue	3,464.9	3,322.3	-4.1	4,454.0	3,902.5	-12.4	5,630.9	5,148.4	-8.6
EBITDA	307.2	281.8	-8.3	416.6	301.9	-27.5	574.8	488.2	-15.1
EBITDA Margin (%)	8.9	8.5	-38 bps	9.4	7.7	-162 bps	10.2	9.5	-73 bps
PAT	141.0	122.5	-13.2	247.5	154.1	-37.7	370.9	302.7	-18.4
EPS (₹	4.0	3.4	-13.0	7.0	4.3	-37.7	10.4	8.5	-18.4

Source: Company, ICICI Direct Research

Exhibit 9: Key Financial Summary

(₹Crore)	FY18	FY19	FY20E	FY21E	FY22E	CAGR (FY19-22E)
Net Sales	2,157.5	2,630.2	3,322.3	3,902.5	5,148.4	25.1%
EBITDA	201.2	227.7	281.8	301.9	488.2	28.9%
PAT	87.0	94.9	122.5	154.1	302.7	
EV/Sales (x)	7.7	6.4	5.2	4.5	3.4	
EV/EBITDA (x)	82.7	73.4	61.4	58.0	36.2	
RoCE (%)	10.0	10.1	9.0	9.0	13.9	
RoE (%)	5.5	5.8	4.6	5.6	10.3	

Source: Company, ICICI Direct Research

ABFRL: Aditya Birla Fashion and Retail (ABFRL) combines Madura's portfolio of leading lifestyle brands (Allen Solly, Van Heusen, Louis Philippe and Peter England) with Pantaloons' strength as the largest value fashion retailer. The company has a robust distribution network with 2656 brand stores and a reach across 24000 multi branded outlets, along with 343 Pantaloons stores. Over the years, Pantaloons has witnessed a significant upgradation of margin profile, from ~4% in FY15 to 10.1% in Q3FY20 (9.0% in YTD FY20). Owing to the discretionary nature of its product portfolio in both Lifestyle brands and Pantaloons, we expect revenue growth to take a hit in the short-term due to impact of Covid-19. We expect the earnings of ABFRL to be impacted the most owing to high leverage (DE: 1.4x) compared to peers. However, we believe that with its strong brand patronage and large distribution reach, it will be able to revive its revenue growth post normalisation of the scenario and improvement in retail footfalls. **We maintain BUY with a revised target price of ₹ 225 (1.8x FY22E EV/sales).**

Exhibit 10: Change in estimates

	FY 20E			FY 21E			FY 22E		
(₹Crore)	Old	New	% Change	Old	New	% Change	Old	New	% Change
Revenue	9,103.3	8,702.8	-4.4	10,354.0	9,140.0	-11.7	11,733.9	10,575.3	-9.9
EBITDA	666.8	545.7	-18.2	827.9	590.6	-28.7	994.1	764.0	-23.2
EBITDA Margin (%)	7.3	6.3	-105 bps	8.0	6.5	-153 bps	8.5	7.2	-125 bps
PAT	194.3	105.8	-45.5	321.3	158.6	-50.6	450.7	300.6	-33.3
EPS (₹	2.5	1.4	-45.3	4.2	2.0	-50.7	5.8	3.9	-33.0

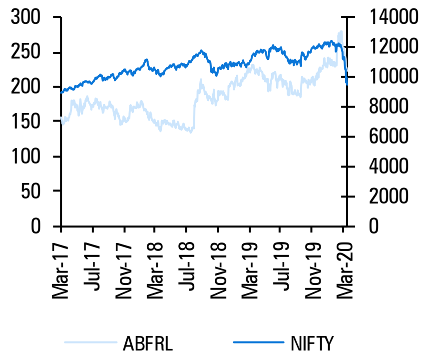
Source: Company, ICICI Direct Research

Exhibit 11: Key Financial Summary

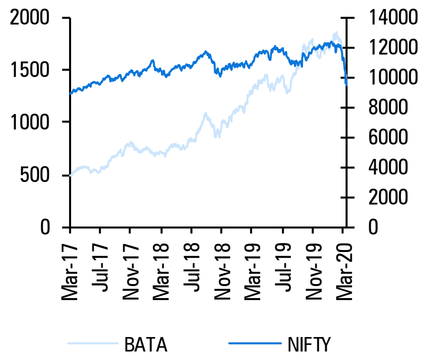
(₹Crore)	FY18	FY19	FY20E	FY21E	FY22E	CAGR (FY19-22E)
Net Sales	7,172.1	8,117.7	8,702.8	9,140.0	10,575.3	9%
EBITDA	500.3	554.1	545.7	590.6	764.0	11%
PAT*	117.8	321.2	105.8	158.6	300.6	
P/E (x)	108.1	39.7	120.6	80.5	42.5	
EV/Sales (x)	2.0	1.8	1.7	1.6	1.4	
EV/EBITDA (x)	29.0	26.0	27.1	24.7	18.8	
RoCE (%)	8.5	10.7	9.7	11.2	15.3	
RoE (%)	10.8	22.5	6.9	9.4	15.1	

Source: Company, ICICI Direct Research. FY19 PAT includes deferred tax asset worth ₹ 193 crore

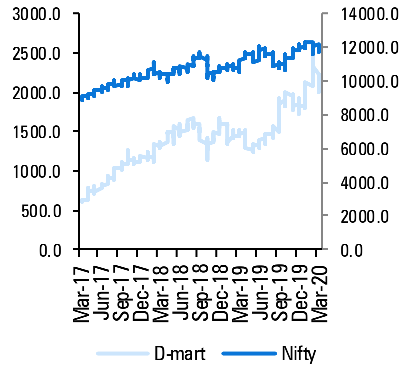
ABFRL



Bata



Avenue Supermarts



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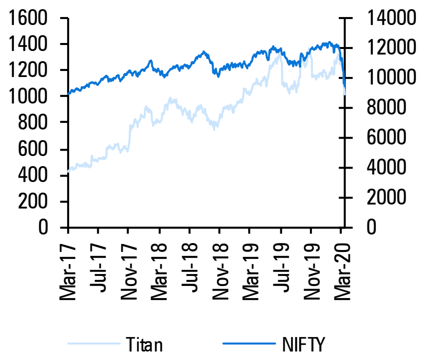

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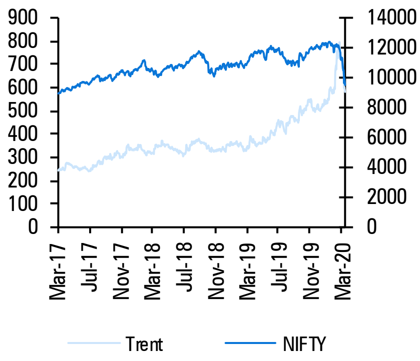

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