

Incremental capital deployment to be RoE dilutive...

About the stock: V-Mart, having over the years built its fortress in non-tier I cities, is well poised to capture market share in the growing ~₹ 2.5 trillion value fashion industry. The company enjoys strong moats that would provide an edge over increasing competition in tier III-IV regions.

- V-Mart follows a cluster based approach of adding stores within a radius of 50-100 km. This gives it better economies of scales, supply chain efficiencies and better understanding of fashion needs of the specific region

Q3FY23 Results: V-Mart reported a subdued operational performance with significantly higher operating expenses impacting profitability.

- Revenue for the quarter grew 12% YoY to ₹ 776.9 crore, with Unlimited format (17% of sales) registering 12% sales growth. Revenue per store for V-Mart business continues to lag pre-Covid levels (down 15%) at ₹ 1.9 crore
- Bloated operating expenses came in as a negative surprise, which led to significant miss on the EBITDA front. Employee and other expenses increased significantly by ~₹ 41 crore QoQ (up 31%) mainly owing to integration of LimeRoad division (~₹ 36 crore of which ₹ 12 crore is one-off)
- Subsequently, EBITDA margins contracted 620 bps YoY to 13.3% (excluding the LimeRoad integrations, the margins would have been ~17%)

What should investors do? V-Mart has been a consistent compounder with stock price appreciating at 18% CAGR in the last five years. However, the stock has been under pressure on YTD basis (down 25%) as higher inflation is pinching consumer spending especially for people salaried < ₹ 25000 (its main target consumers). Also heightened competition from large retailers in Tier III/IV cities is exerting pressure. **We expect RoIC for the company to be below historical levels as incremental cashflows generated by the legacy business would be deployed towards new initiatives (such as LimeRoad that would need 20% of V-Mart's EBITDA), which would be margin dilutive.**

- Hence, we downgrade from BUY to **HOLD** and await material recovery in same stores sales growth

Target Price and Valuation: We value V-Mart at ₹ 2560 i.e. 13x FY24E EV/EBITDA.

Key triggers for future price performance

- Recent acquisition of 'Unlimited' store brand (77 stores) will enable V-Mart to cater to the fashion needs in western and southern markets of India (where V-Mart has minimal presence)
- We expect total retail space to increase at ~14% CAGR in FY22-24E with total area of 4.3 million square feet by FY24E

Alternate Stock Idea: Apart from V-Mart, in our retail coverage we like Trent.

- Inherent strength of brands (Westside, Zudio, Zara) and proven business model position Trent as a key beneficiary of economy unlock theme
- BUY with target price of ₹ 1730/share



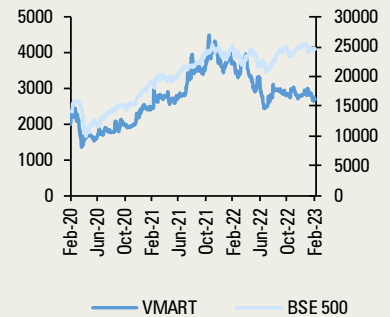
Particulars

Particulars	Amount
Market Capitalisation (₹ crore)	5,194.3
Total Debt (FY22) (₹ crore)	-
Cash & Investment (FY22) (₹ crore)	161.8
EV (₹ crore)	5,032.5
52 Week H / L	4026 / 2406
Equity Capital (₹ crore)	19.7
Face Value (₹)	10.0

Shareholding pattern

	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
Promoter	46.4	46.2	46.1	46.1	45.8
FII	21.1	20.2	18.2	11.5	11.2
DII	22.0	23.2	25.6	31.5	32.7
Others	10.5	10.3	10.1	10.8	10.4

Price Chart



Key risks

Key Risk: (i) Slow ramp up of store network (ii) decline in RM prices could improve margins

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Key Financial Summary

Financials	FY19	FY20	FY21	FY22	5 year CAGR (FY17-FY22)	FY23E	FY24E	2 year CAGR (FY22-FY24E)
Net Sales	1,433.7	1,662.0	1,075.5	1,666.2	11.0%	2,438.3	2,926.4	32.5%
EBITDA	132.9	213.7	131.2	204.3		308.9	377.6	35.9%
PAT	61.6	49.3	-6.2	11.6		28.1	68.0	
P/E (x)	77.5	96.8	NA	446.6		184.6	76.4	
EV/Sales (x)	3.3	2.9	4.4	3.0		2.1	1.8	
EV/EBITDA (x)	35.3	22.3	36.3	24.6		16.9	13.9	
RoCE (%)	27.2	27.0	6.0	10.3		14.9	19.2	
RoE (%)	15.0	10.7	-0.8	1.4		3.2	7.2	

Key takeaways of recent quarter & conference call highlights

- Revenue for the quarter grew 12% YoY to ₹ 776.9 crore (I-direct estimate: ₹ 823 crore). Revenue from Unlimited format (17% of revenues) grew 12% YoY to ₹ 132.0 crore. Store addition was healthy during the quarter as the company added nine new stores taking the total store count to 414. The average ASP for apparels declined 1% YoY to ₹ 500 but was up 15% compared to pre-Covid levels. V-Marts operating metrics over the past couple of quarters has been turbulent owing to higher inflationary stress on lower price point discretionary categories. Despite 15% higher realisations than pre-Covid levels, revenue per store for V-Mart was at 85% of pre-Covid levels. Footfalls have increased 13% YoY but conversion ratio declined ~600 bps YoY to 55%
- Employee and other expenses increased significantly by ~₹ 41 crore QoQ (up 31%) mainly owing to integration of *LimeRoad* division (~₹ 36 crore of which ₹ 12 crore is one-off). The company has completed integration of "LimeRoad" (D2C website) in November 2022 which is expected to strengthen its e-commerce channel. The aforesaid investment would pressurise margins as the segment would entail investments in the initial phase. The company highlighted it would spend ~15-20% EBITDA of V-Mart to scale up the business
- Higher operating expenses resulted in EBITDA margins declining 620 bps YoY to 13.3% (I-direct estimate: 18.3%). Absolute EBITDA declined 23% YoY to ₹ 103.7 crore
- V-Mart is gradually changing the product portfolio of 'Unlimited' stores and is introducing V-mart products in these stores. The new stores added in southern region (about six new Unlimited stores) have yielded healthy revenue/square feet of ₹ 700/month that is 20-30% higher than legacy stores. However, the acquired 74 stores are continuing to underperform
- Factoring in Q3FY23 performance, we trim our EBITDA estimates for FY23, FY24E by 12%, 8%, respectively. Expect RoE to gradually improve to 8% by FY24E but significantly below FY19 levels (~15%)

Q3FY23 conference call highlights

- The management indicated the consumer and inflation perspective was not positive for the value retail industry in Q3FY23. However, Inflation has been trending down and consumer confidence is gradually inching up with mass consumers returning back. Footfalls have increased YoY but conversion rate is down. The management highlighted that the decline in conversion rate was owing to a high conversion rate during the pandemic when customers used to visit stores for focused product purchases. Also the management said the value retail was showing signs a gradual recovery and reduction in price in certain categories was gradually showing positive results
- The like to like growth (LTL) for the company was at 1% during Q3FY23 with both V-mart and Unlimited witnessing positive LTL growth. The performance during Q3FY23 was also impacted by delayed winter, which led to lower traction in winter wear sales
- The company is currently carrying an inventory of 106 days, which is higher than the normal average (due to winter wear inventory and addition of new categories of products for Unlimited). The company expects to bring it down to 90 days in the ensuing quarters
- The management highlighted that margins in the next few quarters are expected to be under pressure as the company desires to provide more value to customers to woo them back to the stores

- On the Lime road acquisition front, the management highlighted that the business is being integrated with V-Mart. The company is facing initial teething issues with respect to the integration. Also, the management is in the process of getting the name change done in respective agreements with various vendors, etc. Further, the vendors are coming back on the market place with old vendors who had left are rejoining the market place. The revenue stream for LimeRoad is in terms of commission earned from sellers on the online platform
- The management indicated that its setting up of warehouse was progressing as per schedule. The company expects it to be operational by end of March 2023. It expects the warehouse to improve its operational efficiency and improve inventory turnaround time
- On the store opening front, the management highlighted that it had opened 40 stores in YTD FY23 and is planning to add 15-20 stores in Q4FY23 with some stores to be opened in south India

Exhibit 1: Variance Analysis

	Q3FY23	Q3FY23E	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	Comments
Revenue	776.9	823.5	692.0	12.3	506.2	53.5	Revenue from Unlimited format (17% of revenues) grew by 12% YoY to ₹ 132.0 crore. Despite 15% higher realisations than pre-covid levels, revenue per store for V-Mart stood at 85% of pre-covid levels.
Raw Material Expense	501.7	528.5	436.0	15.1	322.4	55.6	
Gross Profit	275.2	295.0	256.1	7.5	183.8	49.7	
Gross Profit Margin	35.4	35.8	37.0	-159 bps	36.3	-89 bps	Gross margins declined by 160 bps YoY to 35.4% (I-direct estimate: 35.8%) which could be possibly on account of price cuts taken by the company to perk up demand.
Employee exp	76.3	61.0	53.5	42.6	56.0	36.2	
Other Exp	95.2	83.0	67.3	41.5	74.2	28.3	The profitability during the quarter was impacted due to expenses of ₹ 36 crore on account of online business which includes one-time integration related expense of LimeRoad business to the tune of ₹ 11.8 crore.
EBITDA	103.7	151.0	135.3	-23.4	53.6	93.5	
EBITDA Margin (%)	13.3	18.3	19.6	-620 bps	10.6	276 bps	
Depreciation	47.3	44.9	40.4	17.1	44.1	7.3	
Other Income	0.7	2.7	2.6	-73.1	2.7	-73.6	
Interest	30.7	28.4	21.2	45.0	27.9	10.1	
Exceptional Income	-	-	-	-	-	-	
PBT	26.4	80.3	76.4	-65.4	-15.7	LP	
Tax Outgo	6.4	20.2	19.3	-66.6	-4.4		
PAT	20.0	60.1	57.1	-65.0	-11.3	LP	

Source: Company, ICICI Direct Research

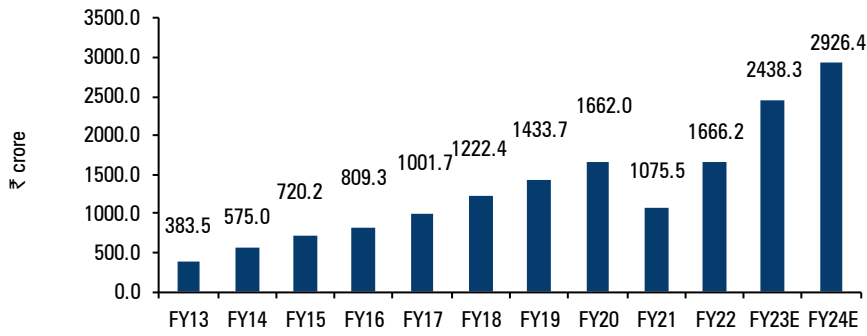
Exhibit 2: Change in estimates

(₹ Crore)	FY 23E			FY 24E		
	Old	New	% Change	Old	New	% Change
Revenue	2,529.7	2,438.3	-3.6	3,009.8	2,926.4	-2.8
EBITDA	349.5	308.9	-11.6	410.5	377.6	-8.0
EBITDA Margin (%)	13.8	12.7	-115 bps	13.6	12.9	-73 bps
PAT	72.4	28.1	-61.1	101.7	68.0	-33.1
EPS (₹)	36.7	14.2	-61.2	51.5	34.4	-33.2

Source: Company, ICICI Direct Research

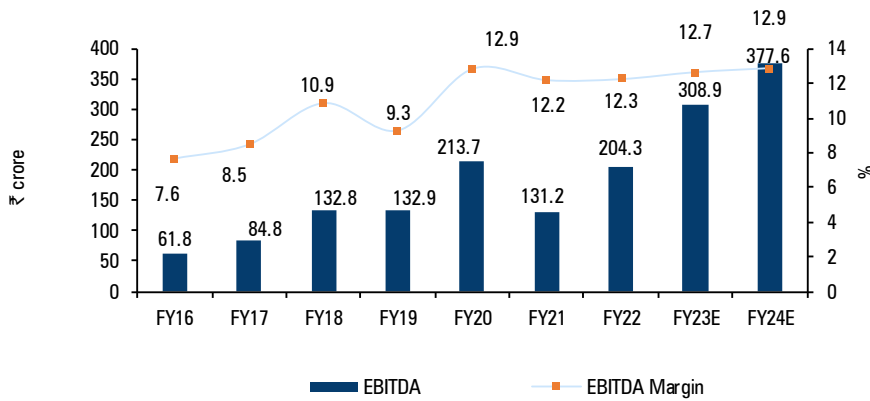
Financial story in charts

Exhibit 3: Revenue trend



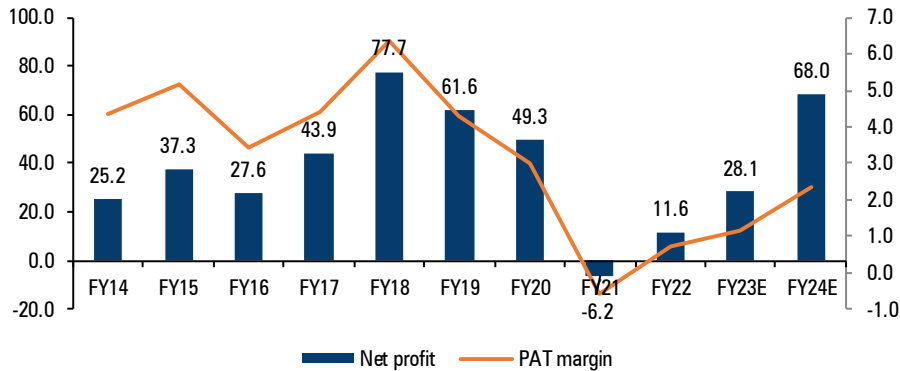
Source: Company, ICICI Direct Research

Exhibit 4: EBITDA and EBITDA margin trend (post Ind-AS 116)



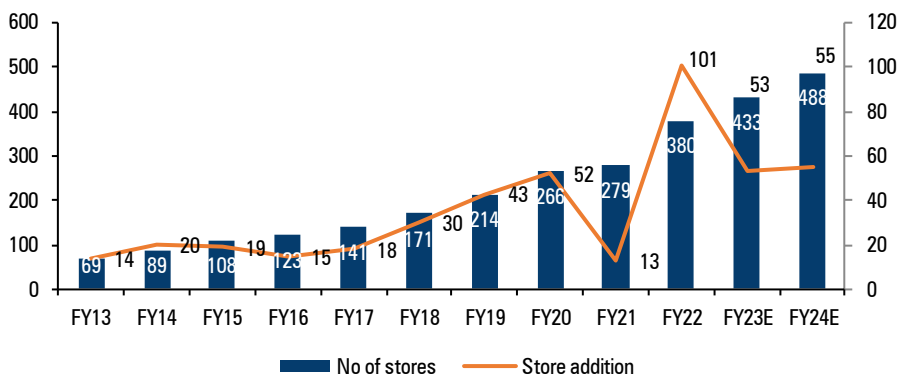
Source: Company, ICICI Direct Research

Exhibit 5: Net profit trend



Source: Company, ICICI Direct Research

Exhibit 6: Total stores and store addition pace



Source: Company, ICICI Direct Research

Financial Summary

Exhibit 7: Profit and loss statement				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Net Sales	1,075.5	1,666.2	2,438.3	2,926.4
Growth (%)	(35.3)	54.9	46.3	20.0
Total Raw Material Cost	723.6	1,091.1	1,560.5	1,902.2
Gross Margins (%)	32.7	34.5	36.0	35.0
Employee Expenses	116.9	179.6	253.6	286.8
Other Expenses	103.8	191.1	315.3	359.8
Total Operating Expenditure	944.2	1,461.9	2,129.4	2,548.8
EBITDA	131.2	204.3	308.9	377.6
EBITDA Margin	12.2	12.3	12.7	12.9
Interest	59.0	77.2	107.8	108.7
Depreciation	103.0	130.7	173.5	189.1
Other Income	21.0	14.0	10.0	11.0
Exceptional Expense	-	-	-	-
PBT	(9.7)	10.4	37.6	90.9
Total Tax	(3.5)	(1.2)	9.5	22.9
Profit After Tax	(6.2)	11.6	28.1	68.0

Source: Company, ICICI Direct Research

Exhibit 8: Cash flow statement				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Profit/(Loss) after taxation	-6.2	11.6	28.1	68.0
Add: Depreciation	103.0	130.7	173.5	189.1
Net Increase in Current Assets	29.6	-309.5	-105.9	-107.2
Net Increase in Current Liabilities	-18.2	111.1	10.1	60.3
CF from operating activities	108.2	-56.0	105.9	210.1
(Inc)/dec in Investments	-381.6	262.7	99.1	20.3
(Inc)/dec in Fixed Assets	-39.9	-152.2	-195.5	-122.1
Others	0.0	-24.9	0.0	0.0
CF from investing activities	-421.5	85.7	-96.3	-101.8
Inc / (Dec) in Equity Capital	1.5	0.1	0.0	0.0
Inc / (Dec) in Loan	-1.1	0.0	100.0	0.0
Others	334.5	-22.1	-111.3	-117.4
CF from financing activities	334.9	-22.1	-11.3	-117.4
Net Cash flow	21.7	7.6	-1.8	-9.1
Opening Cash	5.8	27.5	35.1	33.3
Closing Cash	27.5	35.0	33.3	24.2

Source: Company, ICICI Direct Research

Exhibit 9: Balance Sheet				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Equity Capital	19.7	19.8	19.8	19.8
Reserve and Surplus	805.5	829.9	856.0	919.3
Total Shareholders funds	825.2	849.6	875.8	939.0
Total Debt	-	-	100.0	100.0
Non Current Liabilities	587.3	924.7	924.7	924.7
Source of Funds	1,412.5	1,774.3	1,900.5	1,963.7
Gross block	295.3	442.8	642.1	764.2
Less: Accum depreciation	119.5	163.3	227.5	303.9
Net Fixed Assets	175.8	279.5	414.6	460.3
Capital WIP	2.2	6.4	2.5	2.5
Intangible assets	2.8	3.2	3.2	3.2
Investments	389.5	126.7	27.6	7.3
Inventory	428.3	668.2	815.0	922.0
Cash	27.5	35.1	33.3	24.2
Debtors	-	-	-	-
Loans & Advances & Other	53.1	110.8	69.8	69.9
Total Current Assets	508.9	814.1	918.1	1,016.1
Creditors	191.7	290.6	300.6	360.8
Provisions & Other CL	22.4	34.6	34.7	34.8
Total Current Liabilities	214.1	325.2	335.3	395.6
Net Current Assets	294.8	488.9	582.8	620.5
LT L& A, Other Assets	547.4	869.6	869.7	869.9
Other Assets	0.0	0.0	0.0	0.0
Application of Funds	1,412.5	1,774.3	1,900.5	1,963.7

Source: Company, ICICI Direct Research

Exhibit 10: Key ratios				
(Year-end March)	FY21	FY22	FY23E	FY24E
Per share data (₹)				
EPS	-3.2	5.9	14.2	34.4
Cash EPS	49.2	72.1	102.1	130.2
BV	419.2	430.2	443.4	475.5
DPS	0.0	0.4	1.0	2.4
Cash Per Share	14.0	17.7	16.9	12.3
Operating Ratios (%)				
EBITDA margins	12.2	12.3	12.7	12.9
PBT margins	-0.9	0.6	1.5	3.1
Net Profit margins	-0.6	0.7	1.2	2.3
Inventory days	145.4	146.4	122.0	115.0
Debtor days	0.0	0.0	0.0	0.0
Creditor days	65.1	63.7	45.0	45.0
Return Ratios (%)				
RoE	-0.8	1.4	3.2	7.2
RoCE	6.0	10.3	14.9	19.2
RoIC	12.1	12.7	15.9	19.8
Valuation Ratios (x)				
P/E	NA	446.6	184.6	76.4
EV / EBITDA	36.3	24.6	16.9	13.9
EV / Sales	4.4	3.0	2.1	1.8
Market Cap / Revenues	4.8	3.1	2.1	1.8
Price to Book Value	6.3	6.1	5.9	5.5
Solvency Ratios				
Debt / Equity	0.0	0.0	0.1	0.1
Debt/EBITDA	0.0	0.0	0.3	0.3
Current Ratio	2.2	2.4	2.6	2.5
Quick Ratio	0.2	0.3	0.2	0.2

Source: Company, ICICI Direct Research

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Reduce: -15% to -5%;

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