

Avenue Supermarts

Better than our muted expectations

EBITDA of Rs1.1bn was better than our estimate of zero EBITDA, led by GM beat but in-line sales/opex. But it was behind consensus estimate of ~Rs1.6bn (miss on sales and higher opex). Sales of stores having normalised operation timings recovered to ~80% of pre-Covid level. However, a significant number of stores continue to face local restrictions. Our estimate of 16% EPS CAGR (FY20-22) builds in the impact of slowdown in discretionary consumption categories (~30% of DMart sales), consequent impact on GM and slower store rollouts. Management noted increased consumer focus on convenience over value, which may aid online retailers and Kirana stores in the near term. Current valuation of 83x FY22 P/E (we are 15% behind consensus) leaves limited margin of safety. Our TP of Rs2,000 implies 13% downside. Key risks: Increase in pace of store expansion and better GM.

Revenue declined 34% YoY; in line with our estimate though lower than consensus estimate of ~30% decline YoY. EBITDA/PAT declined 82%/85% YoY led by higher employee cost (29% YoY) and other expenses (24% YoY) indicating limited operating leverage and higher salaries to store staff as indicated in 4QFY20 press release. GM (13.7%) was better than our estimate (10%) by 370bps, indicating lower discounts and/or higher share of private label products. Beat in EBITDA margin of 290bps was led by GM beat of 370bps, partially offset by higher operating cost. Management echoed our thought on customers preferring convenience over value and hence Kirana being preferred over MT during the ongoing pandemic. Our estimates continue to build in 16%/16% CAGR in revenue/PAT over FY20-22 (unchanged) with ~9% upgrade in FY21 EBITDA.

Result highlights

- 1QFY21 revenue declined 34% YoY to Rs38.3bn (broadly in line with our estimate of Rs39bn) led by lockdown-related loss of sales. DMart added 2 new stores during the quarter taking the total store count to 216.
- Gross margin of 13.7% (declined 240bps YoY) surprised positively and beat our estimate of 10% by 370bps. Beat in GM implies (a) ability to reduce discount in Foods and groceries to set off the impact of inferior mix of general merchandise and apparel; and (b) higher share of private labels given downtrading by customers and/or non-availability of branded products due to supply constraints.
- Employee cost increased by 29% YoY (16% below estimate) while other expenses increased by 22% YoY (18% above estimate). Total operating cost increased by 24% YoY (vs revenue decline of 34%) and was 6% ahead of our estimate
- EBITDA declined by 82% YoY to Rs1,089mn (vs our estimate of -Rs26mn). Beat in EBITDA margin of 290bps is completely led by GM beat of 370bps partially offset by higher operating cost.
- PBT/PAT declined by 87%/85% YoY to Rs666mn/496mn (vs our estimate of a loss of Rs798mn/Rs597mn)

Management highlights couple of challenges over Covid period

- Customers prefer convenience over value:** Management noted that unlike developed countries where organized retailers had a surge of customers walking into their stores, it has not happened with the same intensity at DMart stores. Value hasn't been top of mind for shoppers during lockdown; customers wanted products quickly over the counter or through home deliveries which Kirana stores were able to fulfil.

SELL

Result Update

Stock Information

Bloomberg Code:	DMART IN
CMP (Rs):	2,323
TP (Rs):	2,000
Mcap (Rs bn/US\$ bn):	1,505/20
3M ADV (Rs mn/US\$ mn):	882/11.7

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	(3)	(3)	71	26
Rel. to Sensex	(11)	(22)	76	38

Source: Bloomberg, Ambit Capital research

Ambit Estimates (Rs bn)

	FY20	FY21E	FY22E
Revenues	246.8	244.5	333.9
EBITDA	21.2	16.7	28.3
EPS (Rs)	20.8	16.0	27.9

Source: Bloomberg, Ambit Capital research *Last published estimates

Research Analysts

Ritesh Gupta, CFA
 ritesh.gupta@ambit.co
 Tel: +91 22 6623 3242

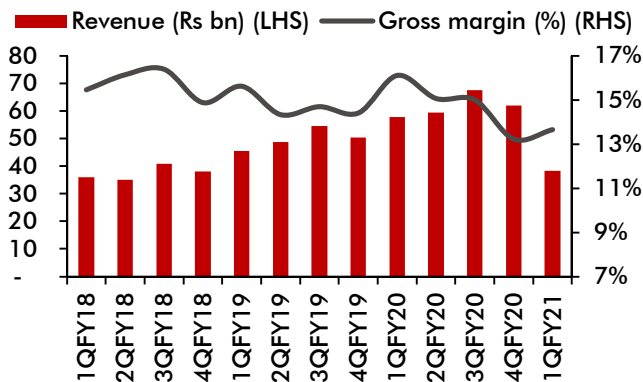
Ashish Kanodia, CFA
 ashish.kanodia@ambit.co
 Tel: +91 22 6623 3224

- **Management believes DMart’s business model** of store ownership, steady incremental store additions over time and strong focus on cost efficiency during usual times has allowed it to face the pandemic shocks with relatively less harm. Management believes they are less anxious than they were in the beginning of April 2020.
- **Online sales:** DMart Ready sales in Mumbai have grown very well and attempts are being made to scale it up in a meaningful manner. Home Deliveries (using DMart Ready App) through DMart stores across the rest of the cities has been discontinued post the stringent lockdowns were withdrawn. We believe this continues to highlight the relative less attractiveness of grocery ecommerce in a value conscious country like India. However, well-funded competition may continue to limit pace of market share gains for DMart.
- **Business operations:** Sales has recovered to 80% or more of pre-Covid sales in most stores wherever stores were allowed to operate unhindered. Discretionary consumption continues to be under pressure, especially in the Non-FMCG categories, impacting GM negatively. Store operations and duration of operation per day remains inconsistent across cities due to strict lockdowns enforced by local authorities from time to time. In addition, in certain cities authorities are once again insisting on selling only essential products. We believe FY21 operations may remain partially disrupted as cities go through iterations of lockdowns/timing restrictions and opening up.

Others

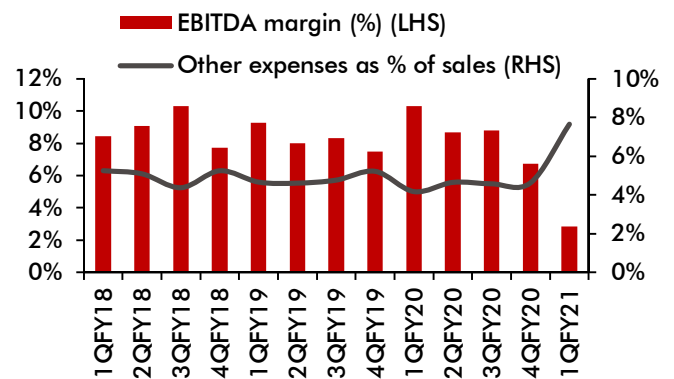
- Company MD and CEO Ignatius Navil Noronha’s term has been extended for another 5 years to 31st Jan 2026.
- Subsidiary revenues were up 46% YoY with reduction in overall losses to Rs78mn (vs Rs93mn in 1QFY20).

Exhibit 1: Revenue declined 34% while GM declined 240bps YoY...



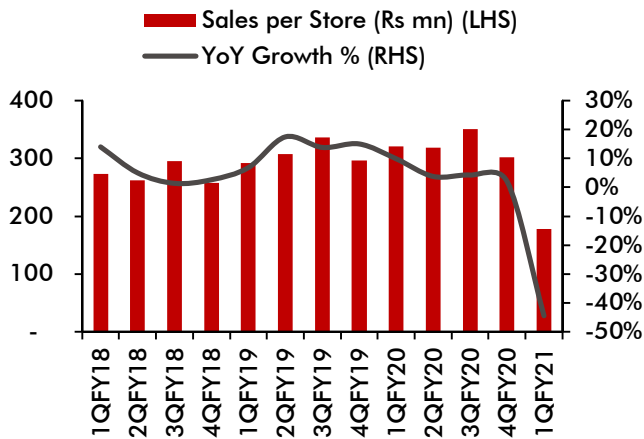
Source: Ambit Capital research, Company

Exhibit 2: ...leading to YoY decline in EBITDA margin as well



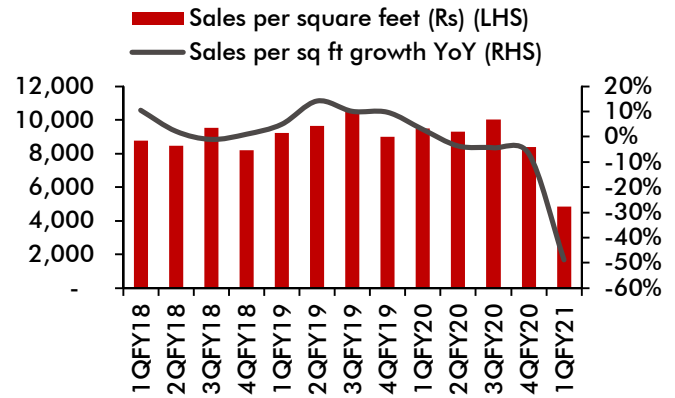
Source: Ambit Capital research, Company

Exhibit 3: Sales per store declined 44% YoY...



Source: Ambit Capital research, Company

Exhibit 4: ...while sales per square feet declined 49% YoY led by impact of lockdown



Source: Ambit Capital research, Company

Exhibit 5: Key operating metrics

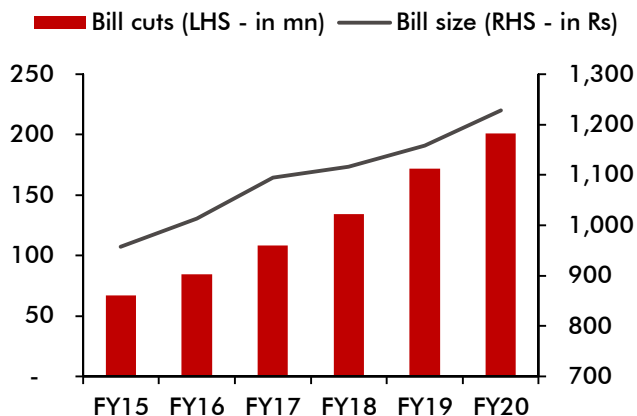
	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21
No. of stores	157	160	164	176	184	189	196	214	216
Area (mn sq ft)	5.0	5.1	5.3	5.9	6.3	6.5	7.0	7.8	8.0
Area per store (sq ft)	31,847	31,875	32,317	33,523	34,239	34,392	35,561	36,449	37,037
YoY growth	3%	3%	4%	6%	8%	8%	10%	9%	8%
Sales per store (Rs mn)	292	307	336	296	321	319	351	302	178
YoY growth	7%	17%	14%	15%	10%	4%	4%	2%	-44%
Sales per sq ft (Rs)	9,211	9,649	10,483	8,988	9,476	9,295	10,025	8,387	4,852
YoY growth	5%	14%	10%	10%	3%	-4%	-4%	-7%	-49%
Employee cost per store (Rs mn)	4.9	5.3	5.4	5.1	5.2	5.6	5.8	5.6	5.6
YoY growth	1%	2%	7%	3%	6%	5%	6%	11%	8%
Employee cost psf (Rs)	155	167	169	153	154	163	165	156	153
YoY growth	0%	-1%	3%	-1%	-1%	-2%	-3%	2%	-1%
Other expenses psf (Rs)	429	444	499	469	395	432	458	388	371
YoY growth	-7%	3%	20%	9%	-8%	-3%	-8%	-17%	-6%
Depreciation psf	81	88	100	111	123	130	129	128	109
YoY growth	-1%	4%	10%	11%	51%	48%	28%	16%	-11%

Source: Ambit Capital research, Company

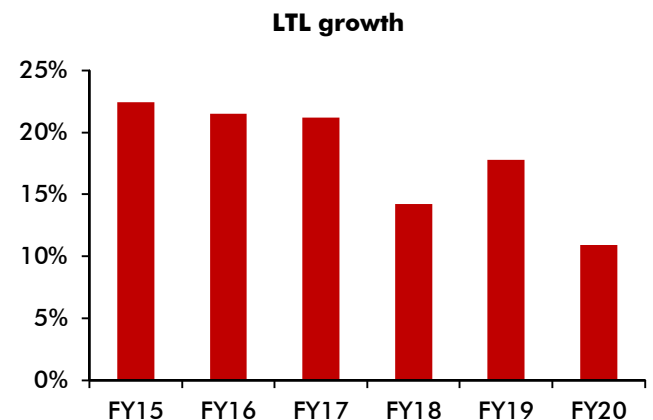
Exhibit 6: Reported quarterly performance

Rs mn, unless specified	1QFY21	1QFY20	YoY	4QFY20	QoQ (%)	1QFY21E	% Divergence
Revenue	38,332	57,805	-34%	61,935	-38%	38,971	-2%
Raw material	33,099	48,494	-32%	53,744	-38%	35,074	-6%
Gross Profit	5,234	9,311	-44%	8,191	-36%	3,897	34%
Gross margin (%)	13.7%	16.1%	-240bps	13.2%	50bps	10.0%	370bps
Employee expenses	1,212	942	29%	1,151	5%	1,439	-16%
Other expenses	2,933	2,409	22%	2,863	2%	2,484	18%
Total Expenditure	4,145	3,352	24%	4,014	3%	3,923	6%
EBITDA	1,089	5,959	-82%	4,177	-74%	(26)	NA
EBITDA margin (%)	2.8%	10.3%	-750bps	6.7%	-390bps	-0.1%	290bps
Depreciation	861	750	15%	948	-9%	948	-9%
EBIT	228	5,210	-96%	3,228	-93%	(974)	NA
Other Income	513	119	330%	356	44%	300	71%
Finance Costs	76	168	-55%	124	-39%	124	-39%
PBT	666	5,162	-87%	3,460	-81%	(798)	NA
Tax	170	1,808	-91%	591	-71%	(201)	-185%
PAT	496	3,353	-85%	2,869	-83%	(597)	NA
PAT margin (%)	1.3%	5.8%	-450bps	4.6%	-330bps	-1.5%	280bps
EPS (Rs)	0.77	5.37	-86%	4.43	-83%	(0.92)	NA
As % of sales							
Raw material	86.3%	83.9%	240bps	86.8%	-50bps	90.0%	-370bps
Employee expenses	3.2%	1.6%	160bps	1.9%	130bps	3.7%	-50bps
Other expenses	7.7%	4.2%	350bps	4.6%	310bps	6.4%	130bps
Depreciation	2.2%	1.3%	90bps	1.5%	70bps	2.4%	-20bps
Other income	1.3%	0.2%	110bps	0.6%	70bps	0.8%	50bps
Finance cost	0.2%	0.3%	-10bps	0.2%	0bps	0.3%	-10bps
Tax rate (as % of PBT)	25.5%	35.0%	-950bps	17.1%	840bps	25.2%	30bps

Source: Company, Ambit Capital research

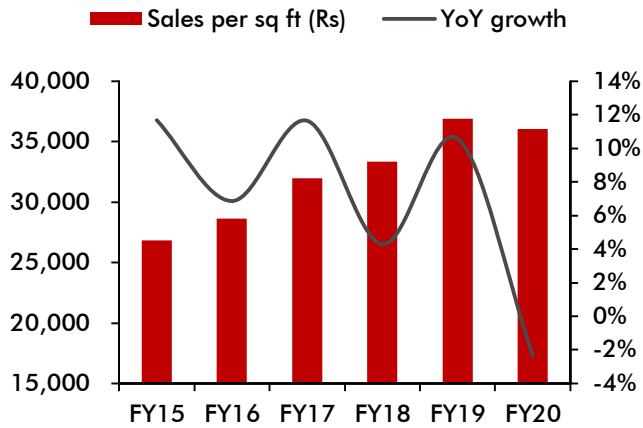
Exhibit 7: Bill cuts have witnessed 25% CAGR while bill size has grown at 5% over FY15-20


Source: Ambit Capital research, Company

Exhibit 8: LTL growth slowed in FY20 primarily due to the impact of lockdown in Mar'20


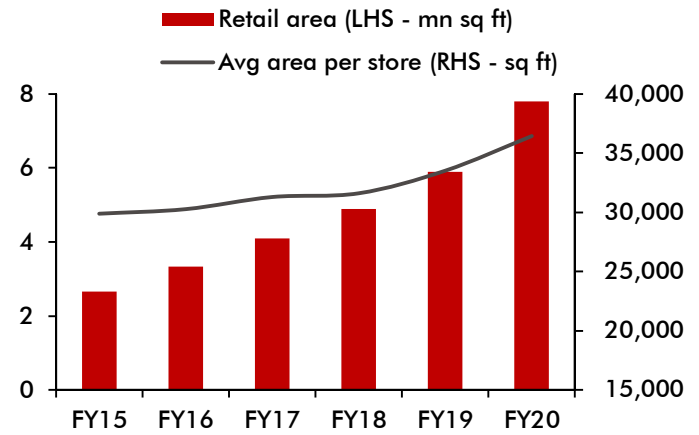
Source: Ambit Capital research, Company

Exhibit 9: Sales per square feet has witnessed 6% CAGR over FY15-20



Source: Ambit Capital research, Company

Exhibit 10: Retail area witnessed 24% CAGR over FY15-20 led by increasing area per store



Source: Ambit Capital research, Company

Exhibit 11: DMart continues to follow cluster-based approach in store expansion with no new states added during FY19 and FY20

State	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20
Maharashtra	34	40	46	50	58	60	62	70	76
Gujarat	14	14	17	22	26	29	30	34	37
Telangana	4	5	7	10	16	19	19	21	24
Karnataka	3	3	5	5	6	10	12	16	20
Andhra Pradesh						2	10	11	17
Madhya Pradesh				2	4	5	6	6	11
Tamil Nadu						1	3	4	10
Rajasthan						1	5	5	7
Punjab							3	4	5
Chhattisgarh							3	3	5
NCR						1	1	1	1
Daman						1	1	1	1
Total	55	62	75	89	110	129	155	176	214

Source: Ambit Capital research, Company

Where do we go from here?

We remain SELLERS on DMart with TP of ₹2,000 implying 13% downside. DMart is trading at a premium valuation of 83x FY22 P/E led by recent run-up in the stock price. This pretty much prices in the best the business can deliver in their business model constraints. While we continue to like the business and the large opportunity for retail/grocery players, DMart’s operating matrix is highly dependent on throughput per sq ft which we believe will be impacted due to lower footfalls due to social distancing measures and lower share of general merchandise and apparels. This was also visible with a ~34% drop in sales driving 82% YoY drop in EBITDA.

Also, over the next 12-18 months, we believe kirana stores and e-commerce players will gain market share as consumers avoid crowded places like shopping malls and large format stores and chase convenience of home delivery/nearby store over discount/pricing. While we don’t see ecommerce as a long-term viable alternative/threat to DMart from a cost economics point of view, over near term, cash burns from existing/new players may impact earnings/valuation narrative for DMart. We build in 16%/16% revenue/PAT CAGR over FY20-22. We would seek better entry point.

Exhibit 12: We increase our GM estimate for FY21 by 90bps while decrease our revenue estimate for FY21/FY22 by 1%/2%

Rs in mn, unless specified	FY21E			FY22E		
	New	Old	Change	New	Old	Change
Target price (Rs)				2,000	2,000	0%
Revenue	244,453	246,820	-1%	333,898	341,772	-2%
Gross margin (%)	14.3%	13.4%	90bps	15.0%	15.0%	0bps
EBITDA	16,710	15,289	9%	28,273	29,175	-3%
EBITDA margin (%)	6.8%	6.2%	60bps	8.5%	8.5%	0bps
PBT	13,851	11,628	19%	24,167	24,372	-1%
PAT	10,362	8,701	19%	18,084	18,238	-1%
EPS (Rs)	16.0	13.4	19%	27.9	28.2	-1%

Source: Ambit Capital research, Company

Financials

Balance sheet

Year to March (Rs mn, unless specified)	FY19	FY20	FY21E	FY22E	FY23E
Shareholders' equity	6,241	6,478	6,478	6,478	6,478
Reserves & surplus	49,704	104,878	115,240	133,324	155,756
Total net worth	55,945	111,355	121,718	139,801	162,234
Loan funds	6,952	37	2,000	2,000	2,000
Deferred tax liability	641	482	482	482	482
Total liabilities	63,545	114,303	126,628	144,712	167,145
Gross block	47,676	59,706	69,545	86,725	106,276
Net block	42,161	50,719	56,944	69,906	84,250
CWIP	3,766	3,619	3,619	3,619	3,619
Investments	2,300	3,038	3,038	3,038	3,038
Inventories	15,762	19,094	16,078	20,994	25,064
Debtors	755	485	574	778	964
Cash and cash equivalents	2,136	922	10,068	8,965	8,000
Loans & Advances	1,784	2,421	2,398	3,276	4,061
Other current assets	30	-	-	-	-
Total current assets	20,467	22,923	29,119	34,012	38,089
Creditors	4,583	4,460	5,168	6,998	8,676
Other current liabilities	1,454	1,935	1,030	1,318	1,566
Provisions	394	143	143	143	143
Total current liabilities & provisions	6,431	6,538	6,342	8,459	10,385
Net current assets	14,036	16,385	22,777	25,553	27,704
Total assets	63,545	114,303	126,628	144,712	167,145

Source: Company, Ambit Capital research

Income statement

Year to March (Rs mn, unless specified)	FY19	FY20	FY21E	FY22E	FY23E
Net Sales	199,163	246,750	244,453	333,898	413,974
Gross Profit	29,363	36,591	34,860	50,085	62,120
Employees cost	3,350	4,247	5,038	5,925	6,624
Other expenses	9,591	11,122	13,113	15,886	20,379
EBITDA	16,422	21,221	16,710	28,273	35,117
Depreciation	1,988	3,398	3,615	4,217	5,208
EBIT	14,434	17,823	13,095	24,056	29,909
Non-operating Income	514	633	1,073	480	511
Interest expenditure	472	628	317	370	442
PBT	14,476	17,829	13,851	24,167	29,978
Tax expenses	5,113	4,330	3,489	6,083	7,545
Adjusted PAT	9,363	13,499	10,362	18,084	22,432
EPS	15.0	20.8	16.0	27.9	34.6

Source: Company, Ambit Capital research

Cash flow statement

Year to March (Rs mn, unless specified)	FY19	FY20	FY21E	FY22E	FY23E
PBT	14,476	17,829	13,851	24,167	29,978
Depreciation	1,988	3,398	3,615	4,217	5,208
(Increase)/Decrease in working capital	(3,213)	(3,730)	3,045	(6,224)	(9,053)
Tax	4,935	4,815	3,489	6,083	7,545
Cash flow from operating activities	8,528	12,874	16,274	15,966	18,519
Capex	(13,800)	(16,831)	(9,840)	(17,179)	(19,552)
Cash flow from investing activities	(10,007)	(46,996)	(8,766)	(16,699)	(19,041)
Net borrowings	(206)	(5,000)	1,963	-	-
Interest paid	(509)	(679)	(317)	(370)	(442)
Cash flow from financing activities	2,040	33,835	1,646	(370)	(442)
Net change in cash	561	(287)	9,154	(1,103)	(965)
Closing cash balance	1,202	914	10,068	8,965	8,000
Free cash flow	(5,353)	(4,012)	6,435	(1,213)	(1,033)

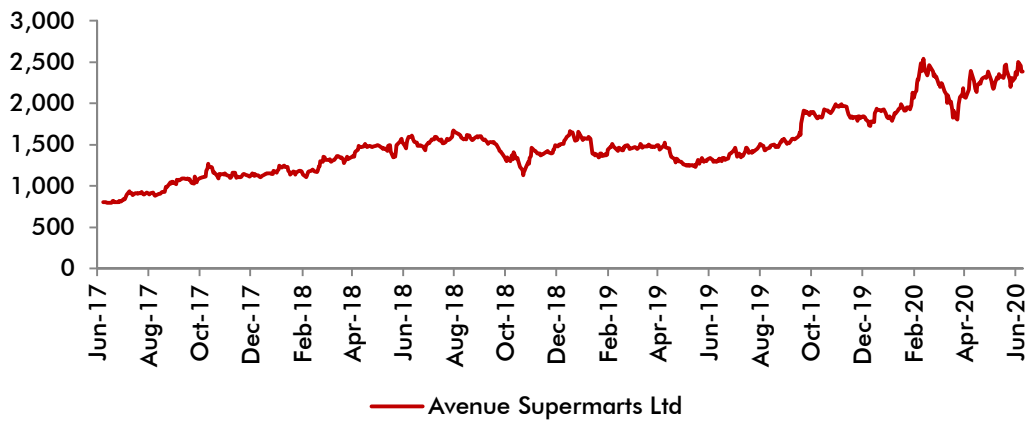
Source: Company, Ambit Capital research

Ratio analysis / Valuation parameters

Year to March	FY19	FY20	FY21E	FY22E	FY23E
Gross margin (%)	14.7%	14.8%	14.3%	15.0%	15.0%
EBITDA margin (%)	8.2%	8.6%	6.8%	8.5%	8.5%
EBIT margin (%)	7.2%	7.2%	5.4%	7.2%	7.2%
Net profit margin (%)	4.7%	5.5%	4.2%	5.4%	5.4%
Net debt/equity (x)	0.0	(0.0)	(0.1)	(0.1)	(0.1)
Asset turnover (x)	3.5	2.8	2.1	2.5	2.7
Working capital turnover (x)	16.9	7.9	5.1	6.7	7.2
Gross block turnover (x)	4.5	4.3	3.6	4.1	4.1
RoCE (%)	16.4%	15.5%	8.3%	13.6%	14.6%
ROE (%)	18.3%	16.1%	8.9%	13.8%	14.9%
P/E (x)	155	111	145	83	67
P/B (x)	26	14	12	11	9
EV/EBITDA (x)	88	70	89	52	42
EV/Sales (x)	7	6	6	4	4

Source: Company, Ambit Capital research

Avenue Supermarts Ltd (DMART IN, SELL)



Source: Bloomberg, Ambit Capital research

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Investment Rating	Expected return (over 12-month)
BUY	We expect this stock to deliver more than 10% returns over the next 12 months
SELL	We expect this stock to deliver less than or equal to 10 % returns over the next 12 months
UNDER REVIEW	We have coverage on the stock but we have suspended our estimates, TP and recommendation for the time being
NOT RATED	We do not have any forward-looking estimates, valuation, or recommendation for the stock.
POSITIVE	We have a positive view on the sector and most of stocks under our coverage in the sector are BUYS
NEGATIVE	We have a negative view on the sector and most of stocks under our coverage in the sector are SELLS
NO STANCE	We have forward looking estimates for the stock but we refrain from assigning valuation and recommendation

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