Rating Rationale **for Trent Ltd's proposed unsecured Non Convertible Debenture (NCD) Issue of INR 75 crore**

Issue Rating: BWR AA-	**Outlook: Stable**

Brickwork Ratings (BWR) has assigned BWR AA- (Pronounced BWR Double A minus) Rating for Trent Ltd's (Trent) proposed Rs.75 crore unsecured NCD Issue. 'BWR AA-' stands for an instrument that is considered to offer High credit quality / safety in terms of timely servicing of principal and interest obligations. The rating factors Trent's established brand and store format –Westside, strong Tata parentage, comfortable capital structure and regular equity infusions by promoters' to fund expansion plans. The rating is however constrained by the company's low profitability levels and underperformance of its Star Bazaar and Landmark store formats held in its subsidiaries.

Background

Trent Ltd. (Trent) incorporated in the year 1952, is one of India's leading retailers and is a part of the Tata Group. The company commenced its business as "LAKME Ltd" and in 1996, transferred its cosmetic business and its subsidiary to Lakme Lever Ltd, a joint venture (50:50) with Hindustan Lever Ltd (HLL). In 1998, the company acquired Littlewoods International (India) Pvt Ltd (LIIPL) and with the amalgamation of Lakme with LIIPL, the merged entity became "Trent Ltd".

Trent owns Westside (lifestyle stores), a chain of department stores across the country. Trent is also increasing its foothold in the high volume 'Hyper Market' space through its STAR BAZAAR format (value store) stocking everything from food, grocery, farm produce, clothes etc. In August, 2008, the Star Bazaar business was hived off to its subsidiary, "Trent Hypermarket Ltd" as a part of portfolio reorganization exercise to enable sharper management focus and to profitably scale up the operations. It also has presence in the books and music retailing space through its subsidiary "Landmark Ltd".

Trent has entered into a joint venture with Inditex Group which is one of the world's biggest fashion retailers from Spain to develop and promote Zara stores in India. The Company operates 8 stores under the Sisley banner, as a franchisee of Benetton in India and plans to open about 6 new stores over the next 3 years. It has also launched Fashion Yatra, a retail banner to explore the value apparel segment and which may facilitate expansion into tier 2 and tier 3 markets. Further, Trent has an agreement with The Xander Group Inc. (Xander), a global private equity firm under which Xander, through one or more of its fund vehicles, will invest in the development of an institutional retail real estate portfolio in India in partnership with high quality Indian developers.

The sourcing, warehousing, clearing and forwarding needs of Trent are met by its subsidiary Fiora Services Ltd. Trent merged with itself its wholly owned subsidiaries namely Satnam Developers Pvt Ltd (SDPL) and Satnam Realtors Pvt. Ltd. (SRPL).

Areas of Business

Westside:

Westside is an established brand the lifestyle store format. It is into retailing of readymade garments for men, ladies and children, footwear, accessories, gifts and artifacts, furnishings, toys, and a range of home accessories etc. It has its presence in all the five regions with 43 outlets across 22 cities in India. Private Labels (products under its own exclusive brand names) form a significant proportion of the products in its stores. Brands include Westside, Trent, Richmond, Westsport, Nuan, Azzuro, etc. which have been well accepted and are fast gaining popularity. Over 85% of products at Westside are manufactured or procured as per company specifications and sold exclusively at Westside stores under their labels. Extensive consumer and socio-economic research to target the right set of consumers and market has helped Westside to position itself among the leading organized apparel retailers. There are presently 43 Westside stores, 8 Sisley stores and 2 Fashion Yatra store across India and the company plans to add a significant number of stores over the next 2 – 3 years.

Star Bazaar:

The Star Bazaar is in mass retailing business. The hypermarket chain offers a wide choice of products, ranging from grocery, beverages, health and beauty products, farm and dairy produce, in-house apparels, etc. The Company's association with Tesco Plc, UKs leading retailer is expected to bring operational efficiencies to the hypermarket business. Trent will also source merchandise for Star Bazaar from Tesco's planned wholesale cash-and-carry business in India, benefiting from Tesco's sourcing capabilities and supply chain expertise. Currently the Company has 7 stores across Ahmedabad, Bangalore, Chennai and Mumbai.

Landmark:

Company forayed into the books, music, toys, gift items and stationery retail segment through its subsidiary Landmark Ltd. At present Landmark has 25 stores, varying in size from 12,000 sq. ft. to 45,000 sq. ft. across metro and tier 2 and 3 cities including at airports, malls. Landmark has over 1,00,000 book titles and has a strong presence in toys and furnishings.

Financial Profile:

Trent has a comfortable capital structure with debt equity at 0.39. Regular equity infusions by the promoters' has enabled the company undertake its expansion plans while maintaining its leverage levels. Trent is presently in the process of issuing compulsorily convertible cumulative preference shares (CCPS) aggregating to ~ Rs. 5000 mn towards expansion plans in subsidiaries and other corporate purposes.

In FY2010, the company registered a 14% growth in top line buoyed by economic growth and positive market sentiment. Revenues saw a marginal decline while profitability took a sharp dip in FY2009 due to impact of economic slowdown which resulted in lower spending by consumers. Improvement in EBITDA margins on account of effective cost control measures and favourable renegotiation of lease rentals by the company. PAT for the year is higher by Rs. 140 mn of which Rs. 114 mn pertains to profit on sale of 25% stake in its subsidiary, Landmark, to a private equity fund.

Key Financials:

	2010	2009	2008
Net Sales (INR mn)	5,875	5,140	5,157
EBITDA (INR mn)	339	62	167
PAT (INR mn)	402	252	326
Networth (INR mn)	6,335	6,068	6,058
Total Debt (INR mn)*	2,575	1,656	656
Equity Capital (INR mn)	200	195	195
Total Debt/Tangible Networth (x)	0.41	0.28	0.13
Interest Coverage (x)	5.61	4.74	12.73
Debt-Service coverage ratio (x)	1.10	N.M	27.16
Operating Margins (EBITDA/ Op Income) (%)	5.77	1.21	3.24
Profitability margins (PAT/Op Income) (%)	6.85	4.90	6.32
Return on capital employed (%)	6.26	3.82	5.60
Net cash accruals to total debt (x)	0.14	0.13	0.33
Current ratio (x)	1.99	1.33	1.26

N.M. – Not Meaningful

** Total debt includes Preference Share Capital of Rs. 70 mn.*

Trent's Star Bazaar operations (held in Trent Hypermarket Ltd) are in the incubation stage and is loss making. The company has significant expansion plans for this format which will require funding from Trent Ltd. Its Landmark operations are also incurring losses due to underperformance in Tier 2 and 3 cities (Baroda, Lucknow etc). The company is however taking steps to improve profitability by closing down unviable stores or right-sizing few of its larger stores in certain formats to achieve store level profitability. On a consolidated basis Trent made a PAT of Rs. 15 mn on revenues of Rs. 11205 mn in FY 10 as compared to a PAT of Rs. 2.1 mn on revenues of 8509 mn in FY 09.

Industry Background

The Indian retail industry is the fifth largest in the world comprising of organized and unorganized sectors. The organized retail sector is only about 8% of the total retail industry, thus allowing major scope for growth.

In 2009, the retail trade in India contributed about 10% of the country's GDP and employed about 8% of the total workforce. India has been ranked second most attractive emerging market for retail investment after Vietnam by A T Kearney's annual Global Retail Development Index (GRDI). Currently FDI policy allows 100% FDI in cash and carry wholesale formats and 51% FDI in single brand retailing. The slowdown of Indian economy in 2009 due to global economic crisis caused on one hand lack of financial support to retailers for expansion and on the other, lower consumer confidence resulting from recession and job losses. The recession also gave the retailers the power to renegotiate existing lease agreements and obtain new lease at lower rates. However, with the global economic recovery retail industry is expected to perform well in 2010. India's overall retail sector is expected to raise to US $ 833 billion by 2013 at a CAGR of 10%. According to industry experts, the next phase of growth is expected to come from rural markets with rural India accounting for almost half of the domestic retail market.

Rating Outlook

With the global economic recovery after the crisis in the year 2009, the Indian retail industry is expected to perform well in the years to come coupled with strong GDP growth, greater acceptance of organized retail in smaller cities and towns and higher disposable income. However, with the entry of more and more corporate entities into this industry and further expansion by existing players, the competition is likely to get increasingly stiff. Though currently FDI policy allows 100% FDI in cash and carry wholesale formats and 51% FDI in single brand retailing, any change in such regulation will further intensify competition. Profitability pressures are expected to continue over the near term owing to increased competition with players in an expansion mode after the lull in 2009.

Trent is one of the leading players in the organised retail sector in India and has good growth prospects backed by a comfortable capital structure, qualified management team, reasonable profitability and Tata parentage.

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