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Is the worst behind for DMart?

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For a while now, Avenue Supermarts Ltd has been finding it tough to boost sales from its high-margin general merchandise and apparel business. This is a key reason why the profit margins of the company, which runs the DMart supermarket retail chain, have suffered in the past several quarters. Take the three months ended September (Q2FY24). Stand-alone Ebitda margin stood at 8.1%, down 48 basis points from the year-ago period. This is the fifth quarter where the measure has fallen year-on-year.

Ebitda is a profitability parameter and is short for earnings before interest, tax, depreciation and amortization. A basis point is one-hundredth of a percentage point.

Overall Ebitda rose by 12% from a year ago to ₹1,001.8 crore, coming in lower than analysts' expectations as gross margin fell year-on-year and staff costs remained elevated.

According to DMart, for the half year ended September, contribution from the general merchandise and apparel segment stood at 23.2%, down from 24.8% in the same period last year. A good part of this drop was offset by an increase in contribution from the foods segment. It is this unfavourable combination that is hurting margins. Recall that the contribution from the general merchandise and apparel segment had stood at 28.3% before the pandemic (FY19). What is causing this segment to be bogged down? There seem to be two main reasons. One, rising competition in apparels from formats such as Reliance Trends and Zudio (Trent Ltd's value fashion concept). Two, inflationary pressures are curbing consumers' ability to spend on discretionary items.

Moreover, DMart's retail space grew 12% year-on-year to 13.9 million sq. ft in Q2. But the revenue throughput, which is trailing 12-month sales per average square foot, remained flat.

To be sure, there are some bright spots. In the first half of FY24, like-for-like sales growth was healthy at 8.6%. For DMart, like-for-like growth refers to revenue growth from sales of the same stores that have been operational for at least 24 months at the end of the reporting period. Moreover, revenue growth has inched up marginally in Q2 to 18.5% year-on-year from 18.1% in Q1. For perspective, before Q2, year-on-year revenue growth had decelerated for four quarters continuously.

Footfalls are also improving. Plus, while DMart's 12 new store additions in the first half of FY24 are not enough, the bulk of additions is expected in the second half. Its capital expenditure stood at roughly ₹1,270 crore in the first half of FY24. Analysts at JM Financial Institutional Securities said this is significantly higher than the spending needed for the 12 new stores opened—nearly two times. "This implies that a lot more under-construction stores are in the pipeline," said the JM report.

Hereon, store additions and improvement in sales mix are factors that investors will closely track. DMart's shares fell 2% on Monday. Its shares have stayed muted after every quarterly earnings announcement for five times in a row, including the latest one. In the past year, the shares are down by about 10%.

Investors would want to know if the pain is behind now. A few analysts think so. "Worst in terms of revenue weakness appears behind and comparables are also more favourable going forward," said JM's analysts. Prabhudas Lilladher believes the worst seems nearly over and the food and grocery segment is expected to drive a rebound in sales and profit growth in the coming quarters. The brokerage estimates 10% earnings-per-share growth in FY24, but growth is expected to be faster over FY24-26 at a 27.3% compound annual rate.

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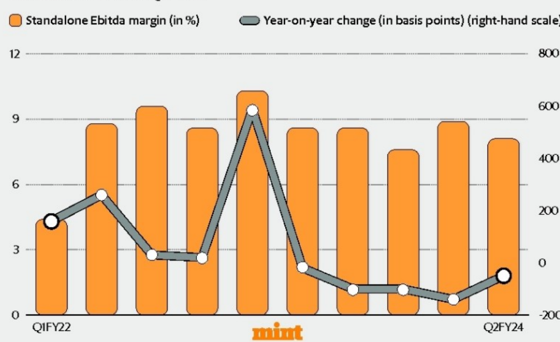
LOOKING UP

IN the first half of the financial year, DMart's like-for-like sales growth was healthy at 8.6%

REVENUE growth inched up marginally in Q2 to 18.5% year-on-year from 18.1% in Q1

Sore spot

Avenue Supermarts' Ebitda margin dropped year-on-year for the fifth consecutive time in Q2FY24.



Note: Ebitda is earnings before interest, taxes, depreciation and amortization; one basis point is 0.01%.

Source: Company, JM Financial

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