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FASTEST GROWING COMPANIES

THE HINTERLAND WINNER

A strong presence in non-metros, right products and a watchful eye on costs have helped V-Mart survive in a tough retail market

Himanshu Kakkar

PHOTOGRAPHS BY VISHAL KOUL

V-MART

SALES
5-YEAR CAGR, %
38

NET PROFIT
5-YEAR CAGR, %
74

ROCE
5-YEAR AVERAGE, %
23

“NOBODY WAS SELLING VALUE-FOR-MONEY PRODUCTS IN A GOOD SETTING. OUR STORE WAS THE FIRST OF ITS KIND IN WESTERN INDIA

—LALIT AGARWAL
Founder and CMD, V-Mart

"The problem is not in the retail segment but our approach to it," a smiling Lalit Agarwal candidly confides when talking about the unusually high mortality rate in the country's organised retail sector. In a business segment marked by wafer-thin margins, unrealistic rentals, indebtedness and high employee costs, Agarwal and his 12-year-old value retail chain V-Mart have managed to beat the odds by picking the right locations, getting the product mix and pricing right and keeping costs low. What began as a single store in Ahmedabad in 2003 with ₹1 crore as investment is now a 120-store chain — a listed company with ₹720 crore in revenue. With the number of stores tripling from 40 in FY11 to 120 in FY15, revenue more than trebled from ₹200 crore in FY12 to ₹720 crore in FY15. Clearly, Agarwal's approach helped V-Mart not only keep its head above the water but also swim along confidently.

Agarwal's tryst with retail started young: in 1975, his dad started his first suiting-shirting store in Kolkata (handed over to Agarwal's uncle when the family moved to Odisha). "I recall taking measurements of the customers at the age of 12. It was fun back then," he says. Agarwal had to wait for some years before getting back to his childhood pursuits. He pursued an MBA in Mumbai and started a printing and packaging business of his own in the mid '90s. But the charm of retail lured him out of that business very soon. In 1999, Agarwal found himself working with his elder uncle's new organised store — Vishal Mega Mart. In 2003, he decided to branch out and start on his own. His first store was then opened in Ahmedabad and was called V-Mart.

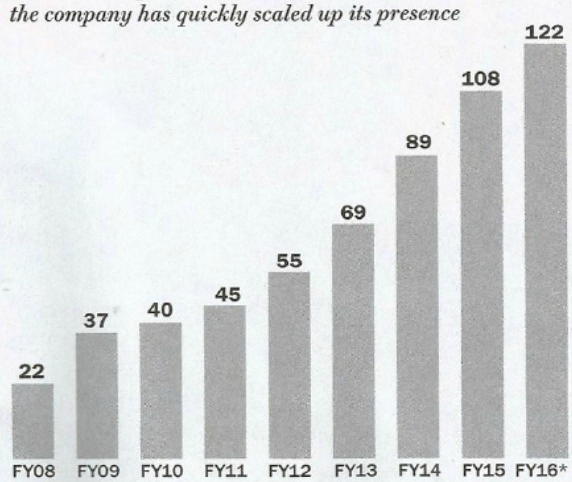
"There was only Shoppers Stop at that time; nothing in the organised affordable retail sector. Nobody was selling value-for-money products in a good setting. Our store was the first of its kind in western India," Agarwal explains. So, it didn't come as a big surprise when this store became a huge success. Agarwal recognised a gap in the time-to-market and worked towards developing a robust supply chain, tying up with manufacturers and suppliers to get just the right products on the shelves. He opened stores in big cities such as Delhi, Ahmedabad and Lucknow. Pretty soon, Naman Finance Investment, an investment entity of the Aditya Birla Group, invested in V-Mart in 2008. But when the financial crisis hit in 2008-09, the company's expansion strategy came to a grinding halt. V-Mart had over 30 stores by then but revenue and footfalls dipped. "We had to close seven stores that year," recalls Agarwal. But the shake-up did more good than bad to V-Mart. The management was forced to do a rethink on its strategy and the Aditya Birla Group (which runs More retail, among other such businesses) — being on V-Mart's board — decided to change a few things. "We decided to focus on tier 2, 3 and 4 cities for the next level of growth," says Agarwal. Once the decision was made, it all came down to execution.

SMALL TOWNS, BIG OPPORTUNITY

What that strategic shift resulted in, years later, is summed up by Agarwal in just one data point. "Almost 80% of our revenue today is contributed by tier 2, 3 and 4 town stores; tier 1 and the metros contribute barely 7-8%," he says. Of the 122 V-Mart stores, over 100 are in smaller cities and towns. In FY16, the company added 16 stores to its roster and has plans to add 15-20 stores every year over the next few years. In November 2015, V-Mart entered Odisha and West Bengal and opened stores in smaller towns such as Behrampur, Bhadrak, Keonjhar and Baripada in Odisha and Burdwan and Cooch Behar in West Bengal; V-Mart's stores are often the first organised stores in many of these district towns. Mohit Bahl, partner, transaction services, KPMG, attempts to decode the company's quick success in tier II and III cities. "The brand was the first to convert non-brand consumers to brand-buying consumers. So, there is a lot of potential in

Growing footprint

With its VFM proposition clicking in tier II and III towns, the company has quickly scaled up its presence



No. of stores; *till date

Source: RCML Research, company

In vogue

The prospect of better realisations versus groceries has resulted in higher focus on fashion

Source: Company

these towns for retailers like V-Mart and their value-for-money proposition." Having the first-mover advantage in many of these towns, V-Mart has been able to unlock this potential. "In metros, competition is very tough but none of the large retail chains (Pantaloons, Shoppers Stop, etc) are opening stores in these C and D towns," says Bahl. There are several reasons why. "They have not yet exhausted the potential of the bigger towns and it becomes harder to operate as you move down since there is the risk of dilution of brands," he adds. Arun Baid, vice-president, research, Religare Capital Markets, says, "The company's target segment has been very clear. It is meeting consumer aspirations at an affordable price point."

While meeting customer aspirations and getting the pricing right have played a critical role in the company's success, keeping a tight leash on costs has been equally important. In V-Mart's case, being in smaller towns has helped a great deal. For instance, the company leased a space at ₹30 per sq ft for its store in Raebareli in UP. If it had to lease a similar property in the metros, the cost would go up to ₹100 per sq ft. As a result, V-Mart's lease rentals are about 4.5% of its sales, as compared with 9.4% for Shoppers Stop and 9-10% for Trent. Agarwal elaborates, "We keep our store sizes under 8,000-10,000 sq ft. We never set up stores inside malls or commercial complexes — developers take loans to build properties, so these places are expensive. We target family-owned properties in the main market areas of these towns. The acquisition cost for such places is not very high and we employ the local youth." The company's investment on capex is around ₹1,500 per sq ft (₹1.25 crore). Since there isn't a big fight for the talent pool unlike in the metros, the company has been able to keep employee costs low as well. For instance, V-Mart's employee costs stand at 6.7% of its sales compared with Shoppers Stop and Trent, whose costs are higher at 7.5% and 8.4% of sales, respectively.

"THERE IS A LOT OF POTENTIAL IN SMALL TOWNS FOR RETAILERS LIKE V-MART AND THEIR VALUE-FOR-MONEY PROPOSITION

—MOHIT BAHL
Partner, transaction services, KPMG

V-Mart adopts a cluster-based approach whereby new stores are opened within a 100-km radius of existing stores, which helps the company manage inventory better as it can move stock around more quickly, besides saving on administration and marketing costs. As a result of the cluster approach, inventory days have shrunk from 112 days in FY12 to 87 days at present. Thanks to all its strategic and cost reduction initiatives, V-Mart's margins have been better than its peers. At 8.89%, its operating margins were higher in FY15 despite lower gross margins of 30% compared with Shoppers Stop's operating margin of 6.26%. V-Mart, which started off its operations offering a mix of *kirana* and fashion, soon found it more lucrative to become a fashion-only chain, with revenue per sq ft significantly higher compared with its Kirana Bazars. "The average selling price (ASP) of the company's fashion business was ₹261 per sq ft in FY15, whereas overall ASP was ₹191," says Baid. Typically, the ticket size for fashion is higher. "If you sell one shirt at a minimum of ₹299, you will probably have to sell 10 kg of branded *atta* to match that," he adds.

Agarwal feels that rationalisation of its product mix has helped V-Mart grow better in the past three years *(see: In vogue)*. "From 2012, we stopped opening Kirana Bazars. We think that we have a good grip over fashion and there is an opportunity to offer unique products as well." This means that the company offers *kirana* products in only 34 stores out of 120. No

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wonder, then, that revenue from the *kirana* segment dropped from 24% in FY12 to 9% in FY15. But Bahl feels that this strategy is not unique to V-Mart as a "lot of retailers are trying to get rid of *kirana* offerings as supply chains are difficult to manage". The overall philosophy of the company's product mix has also undergone a shift. "The retailer's original idea was that if people come to buy household items, they will check out other products as well. But the Indian consumer is very happy doing both things separately," says Baid. In V-Mart's case, turning fashion-only has worked well with its clientele, since people in tier 3-4 cities have no problems when it comes to access to *kirana* stores but have little choice when it comes to fashion. And consumers have surprised the company more often than not with their choices. For instance, when V-Mart was setting up a store in Srinagar, the staff was cautious about local cultural sentiments and proposed not to offer women's westernwear. But Agarwal shot down the proposal and went against the advice. "Today, Srinagar is one of the highest women's westernwear-selling store," he smiles.

PRIVATE EYE

In its fashion-only journey, V-Mart has also developed its own private labels in addition to working with 1,200-odd local vendors. "Private labels contribute 25% to our revenue today," claims Agarwal. "Our margins on private labels are not very high as we always try to offer value for money. Right now, our margins are around 35% compared with the industry standard of 55%-60%. While controlling costs is in the company's hands, it has little control over increasing competition.

Although e-commerce has got all the retailers in the country worried, Agarwal isn't panicking just yet. Sitting calmly in the basement of one of his company's no-frills stores in Delhi, Agarwal's eye doesn't miss any customer checking out V-Mart's range of apparels. Despite talks that the company is likely to launch its own online portal, V-Mart is yet to firm up definite timelines for the foray. Instead, Agarwal wants to spend time on understanding how he can leverage the brand's strengths. "We are trying to evolve our online model. We haven't tested it yet," he says.

While e-commerce is making its way into tier 2 and 3 cities, Agarwal believes that V-Mart might not be as impacted because e-tailing is more focused on electronic and branded goods. Also, in small towns, people still prefer to touch and feel products before buying. "While competition from both online and offline players is increasing, we are tackling that by offering the best prices, the best products, great fashion and a real shopping experience. These small towns don't have malls or multiplexes. So, customers get to experience that feeling of having a regular haunt when they come to our stores. It has been a very good pull mechanism. Price advantage is important, but with e-commerce, it is not a sustainable long-term model. There were brands that were selling three shirts free with every three shirts sold," exclaims Agarwal. He points out that out of 122 locations, in more than 60 places, V-Mart is competing with players such as Reliance, Max, Vishal Retail and other regional players. So, he is not unduly worried about competition.

However, the past couple of quarters have been challenging for the company. Baid says, "The last six quarters have not seen great same-store growth (SSG), but this quarter is critical for the company as winter sales normally come with higher ticket size and your sales go up per sq ft." During FY12-15, the company saw an average SSG of 10%. However, growth dipped to 6.5% in FY15 from 11.5% in FY14, as the slowdown in the economy led to consumers tightening their purse strings *(See: That sluggish feeling)*. In the first two quarters of FY16, SSG slipped to 8.6% and 4%, respectively. "We have been targeting and getting a same-store growth of 10% in the past, but this year the figure has been fairly low," says Agarwal.

"There are multiple reasons for the low SSG: the economy is weak, the monsoon has been weaker by 35% in the areas we operate in the most, namely, UP and Bihar. Also, income levels have not increased

That sluggish feeling

Although footfalls have been steady, conversion has fallen

	Footfall per store per day	Transaction size per store per day in ₹	Conversion rate (%)
FY09	423	485	64
FY10	405	382	66
FY11	489	400	69
FY12	501	436	70
FY13	534	489	69
FY14	524	576	66
FY15	523	625	65

Source: Nirmal Bang Institutional Equities Research

ANALYSTS EXPECT V-MART TO BOUNCE BACK WITH BETTER GROWTH IN FY17, WITH A REVENUE GROWTH OF 21% AND A PROFIT GROWTH OF ABOUT 32%

by much over the past three to four years. For our customers, who earn an average ₹25,000-30,000 per month, there is an additional bill of ₹2,000-3,000 for mobile and internet connections. Besides, educational expenses have gone up, too."

The overall retail market has also been sluggish in the first two quarters of FY16. Shoppers Stop posted a net profit of ₹12.84 crore in Q2FY16, as compared with the ₹16.9 crore it posted in the corresponding quarter of the previous financial year. Trent registered an Q2FY16 profit of ₹13.43 crore compared with ₹11 crore in Q2FY15. Overall, analysts expect a 4-6% SSG growth for V-Mart in FY16. While raw materials prices, both cotton and synthetic, have been falling, the company has had to pass on most of the benefits to customers, leading to realisations falling by 3-4%. With revenue growing by 18% and profits growing by 15% during the first two quarters of FY16 compared with 25% revenue growth and 18% growth in profit in FY15, analysts expect the year to be one of muted growth for the company. But they are not too worried about the company's ability to expand in the future. "It requires ₹1.2 crore to open an 8,000 sq ft store and a similar inventory requirement. So, to open 20 stores in a year, the outflow will be around ₹25 crore. That is not a huge number, given that most of V-Mart's 120 stores are generating cash," says Baid. Analysts expect the company to bounce back with better growth in FY17, with a revenue growth of 21% and a profit growth of about 32%.

While sustaining growth rates will be tough, the real challenge will be to remain relevant to customers. "Keeping products fresh and supply chain going will be a challenge, given rising aspirations," says Bahl. Agarwal thinks the company has that part figured out. "Fashion is a perishable industry. We are trying to reduce the number of days from design to store. From 120 days three years ago, we are at 100 today; we want to bring this to 75 days. That is what we are working on." No matter how much income levels rise, India will always have ample value-conscious customers, and that is good news for companies like V-Mart.