

January 29, 2016

Instrument	Amount (Rs. Crore)	Rating
Non- Convertible Debentures (Proposed)	100.00	SMERA provisional AA (SO)/Stable (Reaffirmed) *
Non- Convertible Debentures (Proposed)	200.00	SMERA provisional AA (SO)/Stable (Assigned) *

* Credit enhancement on account of structured payment mechanism in the form of Debt Service Reserve Account (DSRA).

* The assigned provisional rating will be converted to final rating after the required conditions are met

SMERA has reaffirmed the rating of '**SMERA provisional AA (SO)**' (read as **SMERA provisional double A Structured Obligation**) assigned to the Rs.100.00 crore proposed non-convertible, secured, redeemable taxable debenture issue and assigned a rating of '**SMERA provisional AA (SO)**' (read as **SMERA provisional double A Structured Obligation**) to the Rs.200.00 crore proposed non-convertible, secured, redeemable taxable debenture issue of Future Retail Limited (FRL). The outlook is '**Stable**'. The rating draws support from the credit enhancement in the form of DSRA, where FRL is to maintain funds equivalent to at least twelve months interest payment on the outstanding non-convertible debentures (NCD's) at all times, in the form of fixed deposit or issue a bank guarantee in favour of the trustee, equivalent to at least twelve months of interest payment on the outstanding NCD. Either the fixed deposit or the bank guarantee is to be in force for the entire tenure of the NCD.

FRL benefits from long standing operational track record and experienced promoters. The company also benefits from its leading position in the organised retail business in India and pan India presence across multiple formats. The credit profile of FRL is supported by its strong resource mobilisation ability, successful equity infusion in FY2014-15 through rights issue and preferential allotment, resulting in improvement in capital structure from 2.08 times in FY2013-14 to 0.95 times in FY2014-15 (consolidated level). Further, the company's continuous focus on improvement of the financial risk profile by divestment of non- core investments and replacement of high cost debt by low cost debt are expected to further improve the credit profile of the company.

FRL's credit profile is however constrained by moderate profitability. The company's profit after tax (PAT) margins stood at 1.38 per cent in FY2014-15. The credit profile is also constrained by FRL's presence in the fragmented and intensely competitive retail sector.

The rating is provisional and the final rating is subject to the execution of a trust deed (with a SEBI registered trustee) that will clearly lay down the legal payment mechanism and rights and obligations of various parties involved in the issuance document structure for the proposed issue. This will remain in force for the tenure of NCD's, irrespective of the demerger, merger or restructuring in the Future group involving FRL.

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The rating centrally factors in the adherence to a specific legal payment mechanism (credit enhancement in the form of DSRA) to be administered by the trustees of the NCD. The trust and retention account (TRA) is to be funded one day in advance (T-1) in case of fixed deposits and two days in advance (T-2) in case of bank guarantee for servicing the bond holders on the forthcoming due date T, and ensure that the trustee is intimated about the clear funds. If FRL fails to do so, the payment will be made good through fixed deposits by due date or bank guarantee (invocation by T-1).

Rating Sensitivity Factors

- Improvement in profitability
- Successful acquisition and demerger of Bharti Retail and its impact on financial, business and liquidity profile of FRL
- Successful divestment of non-core investments as envisaged
- Ability to withstand competition from E-commerce and other supermarket formats.

Outlook: Stable

In SMERA's opinion, FRL's credit profile will continue to benefit from its experienced management and strong resource mobilisation ability. Successful execution of the structured payment mechanism as provided, material implication of merger and realignment plan with Bharti Retail, divestment of non-core investments and thereby change in the financial, business and liquidity profile of the company may lead to a revision of its outlook to either 'Positive' or 'Negative'.

About the Company

FRL (the erstwhile Pantaloons Retail India Limited) incorporated in 1987 is the flagship company of the Future Group, promoted by Mr. Kishore Biyani. The company is a major player in the organised multi retail format business with interests in food, fashion apparels, accessories through popular brands such as Big Bazaar, Fashion at Big Bazaar (FBB) and Food Bazaar among others. As on March 31, 2015, FRL had 401 stores with 11.36 mn sq.ft. of total area.

About the Acquisition

On May 4, 2015, FRL announced the merger with Bharti Retail Limited (BRL, a step down subsidiary of Bharti Enterprises), which runs a chain of over 200 compact hypermarkets, and supermarkets (under the brand name of Easyday) for zero cash, all stock deal. The merger will combine the operations of FRL and BRL to create a national footprint of over 570 retail stores in multiple formats across 185 cities spread over 12.9 million square feet. FRL will realign its business subsequent to its tie-up with Bharti Retail. The realignment will entail division into two - i.e. Retail Business and Infrastructure and Investments. The Retail business will include leasing of store properties, product sourcing, visual merchandising, marketing, sales and store operations.

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The other entity will have Retail infrastructure and investments as its core businesses. The Retail business will have an asset light model as all the backend and store infrastructure will be a part of the other entity. The impact of acquisition, effect of structural changes on FRL and the Future Group are not considered while assigning the rating.

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