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February 16, 2023

To,

National Stock Exchange of India Ltd. Exchange Plaza, Block G, C/1, Bandra Kurla Complex, Bandra (E), Mumbai – 400 051 Email: cmlist@nse.co.in Symbol: DEVYANI	BSE Limited Phiroze Jeejeebhoy Towers, Dalal Street, Mumbai – 400 001 Email: corp.relations@bseindia.com Security Code: 543330
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Sub: Regulation 30: Transcript of Investors & Analysts Conference Call

Dear Sir/Madam,

Transcript of the Investors & Analysts Conference Call held on February 09, 2023, post declaration of Unaudited Financial Results of the Company for the Quarter and Nine Months ended December 31, 2022, is enclosed.

The same is also being uploaded on website of the Company at www.dil-rjcorp.com.

You are requested to take the above on record.

Yours faithfully,
For Devyani International Limited

Varun Kumar Prabhakar
Company Secretary & Compliance Officer

Encl: As above





Devyani International Limited

Q3 & 9M FY23 Earnings Conference Call Transcript

February 09, 2023

Moderator: Ladies and gentlemen, good day and welcome to the Devyani International Earnings Conference Call. Please note that this conference is being recorded. I now hand the conference over to Mr. Anoop Poojari from CDR India. Thank you. And over to you, sir.

Anoop Poojari: Good afternoon, everyone, and thank you for joining us on Devyani International's Q3 & 9M FY23 Earnings Conference Call.

We have with us Mr. Ravi Jaipuria – Non- Executive Chairman of the Company; Mr. Raj Gandhi – Non-Executive Director; Mr. Virag Joshi – CEO & Whole-Time Director; Mr. Manish Dawar – CFO & Whole-Time Director; and Mr. Rahul Shinde – CEO, Yum! Brands & Whole-Time Director.

We will initiate the call with opening remarks from the management, following which we will have the forum open for a question-and-answer session.

Before we begin, I would like to point out that some statements made in today's call may be forward-looking in nature, and a disclaimer to this effect has been included in the results presentation shared with you earlier.

I would now request Mr. Ravi Jaipuria to make his Opening Remarks.

Ravi Jaipuria: Good afternoon everyone. I warmly welcome you all to our earning conference call to discuss the business performance for the quarter-ended December 31, 2022.

Continuing with our store expansion strategy, DIL added 81 new stores to its portfolio during the quarter. With this, our total store count stands at 1,177 stores across all our brands. We are on target to double our store count by the end of the current fiscal year versus the number of stores we had three years ago. You would recall that we were at a store count of approximately 600 stores as at FY 2020 end. We recently celebrated the opening of our 100th Costa Coffee store, a strong testimony to our commitment to the growth of all our core brands. Our core brands footprint in India covers more than 225 cities now. We continue to target new trade areas in metros as well as upcoming cities for our store expansion.

Broad-based inflation has somewhat moderated; however, costs for some of our key raw materials like milk and cheese continue to remain elevated and are still witnessing some inflationary trends. On balance, we think we will start to see the margin stabilize over the next couple of quarters.

The inflation across the staples and food services seems to have a bearing on consumer sentiment and consumer demand. We are supporting our business with the requisite investments and continue to closely monitor the same.

Consolidated quarterly revenues were approximately Rs.791 crore, a growth of nearly 27% over the corresponding period last year. Reported EBITDA on a post Ind AS basis reached close to 174 crore, which is 22% of the revenues.

We have recently brought back “Chizza” at KFC, to strong consumer reception and uptick. As we mentioned earlier, innovation remains a strong pillar of our growth strategy across our brands portfolio, and we will continue to delight our customers with many such products in the coming quarters.

We continue to remain bullish on our brands and the Indian market. We believe that the current consumer demand slowdown is a temporary phenomenon, and once inflation stabilizes, we expect the consumer spending to improve which will help our business. In the meantime, we continue to focus on our processes, product quality and execution capabilities.

With this, I would like to conclude my address and now hand over to Manish for his comments. Thank you.

Manish Dawar:

Thank you, Mr. Jaipuria. Good evening everyone. A warm welcome and thanks to all of you for your valuable time for attending our Q3 and 9M FY23 Earnings Conference Call, our sixth such calls since the listing.

As Mr. Jaipuria said, we are a 1,177 strong restaurant company now. Just a few years back, this number was 610. We opened 81 new stores across our brand portfolio in Q3. With this, globally we have 512 stores for KFC, 487 stores for Pizza Hut and 103 stores for Costa Coffee in our portfolio as at the end of Q3 FY23. Our metro and non-metro distribution of stores in India largely remain unchanged.

The revenues for Q3 stood at Rs.791 crore versus Rs.624 crore last year, clocking a healthy 27% growth on a YoY basis. Revenue growth has been led by new store openings and some volume growth, offset by some compression on the average spending.

The gross margins stood at 69.3% for Q3. This slight impact is a result of the continued input inflation and product mix change. We are working to narrow the gap in gross margins due to product mix changes and get it closer to the rest of the portfolio. This may take a few quarters. A combination of mix change, deleverage because of lower ADS and investments made in our business suppressed the brand contribution margins. Brand contribution margins came in at 18.3% versus 19.6% in the previous quarter. Operating EBITDA, on a pre-Ind AS basis, was Rs.117 crore. Operating EBITDA margin was 14.8% and grew approximately 14% on a YoY basis.

Reported EBITDA on a post Ind AS basis was Rs.174 crore for the quarter with margins at 22% versus Rs.148 crore a year ago, an 18% growth. Profit after tax for the quarter stood at Rs. 71 crore versus Rs.59 crore in the previous quarter. There is an impact of deferred tax asset recognition in the PAT numbers for the quarter.

Coming to our core brands, KFC in India added 38 net new stores, reaching a total count of 461 stores at the end of the quarter. Average daily sales was 116,000 due to some weakness in consumer spending, and as a result of some deeper penetration where we are expecting a smaller ADS. This also had an impact of new stores and the concentrated expansion in some geographies. SSSG was 3%,

revenues at Rs.460 crore, grew 4% sequentially, and 27% on YoY basis, gross margins remained almost flat at 67.6%. We invested in the brand which has led to slightly lower brand contribution margin of 19.7% in the quarter. On-premises consumption remains steady at 64% for the quarter.

Pizza Hut in India added 17 net new stores to reach a count of 483 stores. ADS declined marginally to 43,000. Revenues came in at Rs.184 crore, growing 18% YoY. Cheese prices continue to trend higher. As a result of this and the product mix changes, gross margins came in slightly lower at 73.6% versus 74.5% in the previous quarter. Brand contribution margins dipped to 14.1% versus 17% in the previous quarter, because of the GM dilution, slightly higher delivery sales and investment in the brand. On-premises consumption was slightly lower at 43%.

Costa Coffee crossed the 100-store milestone. We added 15 new stores in the quarter to reach a total of 103. Revenues grew to Rs. 29 crore. The ADS for the brand improved to 37,000. Gross margin was slightly lower at 77.8% because of the inflation in coffee and milk prices. With better operating leverage versus the previous quarter, brand contribution improved from 19.6% to 26.4%.

On a YTD basis, we've added 239 net new stores. Consolidated revenues came in at Rs. 2,243 crore, a 50% year-on-year growth. Gross margin at 70.2% and brand contribution margin at 19.4%, has the impact of inflationary pressures. Reported EBITDA on a post Ind AS basis and on a consolidated basis for nine months has crossed Rs.500 crore for the first time with margins at 22.5%. YTD profit after tax for the year is Rs. 203 crore.

We maintain our goal of sustainable and profitable volume-led growth While the near-term outlook for consumer sentiment in the three categories remains a little fluid. We are steadfast in our growth aspiration and are confident that our portfolio of time-tested brands, and our execution strength will enable us in achieving our aspirations.

On that note, I would like to request the moderator to open the forum for any questions or suggestions that you may have. Many, many thanks.

Moderator: We will now begin the question-and-answer session.

The first question is from the line of Percy Panthaki from IIFL Securities.

Percy Panthaki: Just wanted to understand the reasons behind the significantly different SSSG for KFC and Pizza Hut. Where KFC has grown by about 3%, Pizza Hut has declined by about 6%. Is it just that the pizza category has now become too cluttered with overall about 2,500 outlets of the top two players put together, there is not much more room for penetration, and that is why you're seeing the SSSG being significantly lower versus KFC?

Manish Dawar: Percy, as you know, the chicken category remains a very strong category. And right from the last six to eight quarters, we've been emphasizing that chicken is highly under-penetrated in the country given the consumption habits of the consumers. Therefore it remains a very attractive category, and that's the reason we are focusing on a rapid expansion in KFC. Also, we started penetrating deeper into the country. And obviously as you go deeper, your non-metro consumption, although it has a strong potential, the consumption levels are still not equal into metro level, and therefore that kind of impacts a little bit on the ADS numbers. Having said that, we've also seen a general sentiment issue because of the broad inflation in the current quarter, which has impacted the SSSG numbers, although for KFC, we believe it is still healthy at 3%. So, therefore, we think we are absolutely on the right track as far

as KFC is concerned. On Pizza Hut, I agree with you that obviously the market is kind of getting cluttered and there is some competition from the other QSR segments as well. We also focused on the new launch in the form of Fun Flavor Pizzas. And Fun Flavor has led to our long-term expectation of transactions. But, at the same time, it has led to some bit of dilution on the average realization which has led to a little reduction on the SSSG numbers. Having said that, we are working on the gross margin piece, because Fun Flavor as of now, because it's a new launch, is a little bit of margin dilutive as well. So, in the next few quarters, we will be able to resolve that. And it will also help us to kind of grow the brand by attracting new set of consumers over a period of time, which will take Pizza Hut to a stronger level.

Percy Panthaki: Just a sub-question. You're on Fun Flavor. Is it resulting in any downtrading or is it that whatever sales are coming from Fun Flavor, they are all incremental sales only, which would not have come had this product not been there?

Manish Dawar: Percy, whenever one launches a new category, it takes time to kind of attract the new set of consumers. And in an inflationary environment, when we've launched this category, obviously, there is some downtrading happening because consumers are seeing a cheaper option available. Now, therefore the hypothesis could well be, let's say, if we would not have launched a Fun Flavor Pizza, these consumers could have been left out of the brand, which is not the case. So, therefore, we've managed to retain those consumers. But at the same time, it's important over a period of time, we will be able to attract the new set of consumers, and that was the fundamental objective behind Fun Flavor and I think we'll be able to achieve that.

Percy Panthaki: Second question from my side is about the store opening plan for FY24 across your different brands and are you sort of tapering down the store expansion given the kind of demand environment we are in?

Manish Dawar: In the past we talked about 250 stores-odd. Recently, we have talked about 250 to 300 stores, we remain steadfast on that guidance. So, we are talking about 250 to 300 stores for next year as well. There could well be some mix change between the brands depending on how the market is and depending on how things are, and therefore, obviously, we will be accelerating KFC more, because that market is kind of responding very well...but the overall numbers remain the same, which is 250 to 300 stores for the next year as well.

Moderator: The next question is from the line of Devanshu Bansal from Emkay Global Financial Services.

Devanshu Bansal: So, I was asking that on-premises mix for KFC has remained similar to what it was in the base quarter. However, in my opinion, the mobility was much better this quarter versus the base. So, what is the reason for that?

Manish Dawar: Devanshu, as I said, we are kind of taking the brand deeper into the country. And obviously in non-metro cities, it is more of a novelty value to order at home. So, let's say your food aggregators are expanding, people are experimenting with home delivery. So, it has a novelty value and that is how it is. And I don't know whether you've noticed in our presentation, we've started opening flagship stores for the KFC as a brand. So, our objective is that over a period of time, we will open at least 10% of the KFC flagship stores. And the fundamental premise and logic is that these stores are going to be bigger as far as the real estate is concerned. They will be more digital, they will have expanded menu, they will have some localization in terms of look and feel, which will kind of help us expand the KFC portfolio from a dine-in perspective. So, therefore, we've already started taking that initiative, and during the quarter, we opened about five flagship stores.

Devanshu Bansal: And for Pizza Hut, you have been guiding for high single digit sort of SSSG over the medium term, but over the last two quarters, the performance here has not been up to our expectations. So, are we sort of revising our SSSG numbers for the medium-term, as you also indicated that this category is being impacted because of it being largely penetrated as well as because of other QSR category?

Manish Dawar: Devanshu, as I said, one is obviously the market issue, when I say market issue means pizza as a market, which is what Percy also alluded to. Second, it has been an inflationary environment. And obviously, the consumers have kind of economized given that their wallet size has remained the same. And it's a broad-based inflation. They are also tightening their spends in terms of various other discretionary categories. And at the same time, I also mentioned that because we launched a Fun Flavor Pizza during the during the quarter or let's say we kind of pushed it, it has had some impact on that. But, otherwise, the transactions are higher. And therefore on a medium-term basis, we remain confident that we will be more or less at the numbers that we've spoken earlier.

Devanshu Bansal: Last question, Manish, if you could indicate the kind of inflation that we are expecting on the raw material basket for Q4. Also, if you could provide any guidance for FY24 on this account will be really helpful?

Manish Dawar: Devanshu, KFC portfolio seems to be stabilizing now as far as the raw material and the input prices are concerned. But, having said that, in today's environment given the geopolitical situation, given what could happen in the world, obviously, we will not be able to kind of guide accurately what will happen. But, as we see today, the next quarter, KFC portfolio seems to be stabilizing. On Pizza Hut, there still remains a challenge as far as the milk and the cheese prices are concerned. But we believe that overall as a cycle, I think inflation is stabilizing now. It's no longer the same trends that we used to see a couple of quarters back and therefore we are moving towards stabilization. And as Mr. Jaipuria also mentioned in his address, that we see margins stabilizing over the next few quarters.

Devanshu Bansal: Just a follow up on this, the prices are stable on a sequential basis you're indicating, right?

Manish Dawar: Yes, because as of now, we are not seeing any indicators, which kind of gives us that the prices are rolling back. I'm talking about the input prices. So, they're just stabilizing, whereas earlier they were going up on a month-to-month basis, quarter-to-quarter basis.

Moderator: The next question is from the line of Shirish Pardeshi from Centrum Broking.

Shirish Pardeshi: Just two questions. So, when I look at the Slide #17, which says that the gross profit, which is at 67.6%... obviously, on a YoY basis, it's not comparable, it's coming down. But is it fair to assume in taking your comment that the input material is now stabilizing, will inch up towards 69%, 70% or maybe historically what we have delivered, or it will remain stable at this number?

Manish Dawar: I assume you're talking about KFC margins, right, because Slide #17 is the KFC, is that right?

Shirish Pardeshi: Yes. I'm talking about KFC.

Manish Dawar: So, as I said, KFC as a portfolio is stabilizing. But we've still not seen the prices getting rolled back. And 69% is only possible when the prices start to roll back, we've still not seen that. So, therefore, when we talk about stabilization, which means that

we will be stabilizing around this level. And as we go along, and there is a broader acceptance, maybe we can expect something, but we are not alluding to that.

Shirish Pardeshi: But have you taken any price increase in Q3 or maybe early January or February?

Manish Dawar: We've not taken any price increase on KFC.

Shirish Pardeshi: The question here is you think the inflation if doesn't subside, you will have to take at least 2%, 3% price increase?

Manish Dawar: Let's see how it goes, because for example, if you remember, KFC pricing, we took way back in April, May of last year, and after that, we've kind of managed to hold on to KFC prices for nine months now. So, therefore, let's see how it goes. Our preference will be not to increase the pricing, because, although it's a discretionary category, but it's closer to staples, because that is how the consumption is happening. So, let's see how the situation pans out and then basis that, we will take appropriate calls whatever is good for the business.

Shirish Pardeshi: The reason why I'm asking, Manish, is normally the inflation if it is subsiding, most of the companies would up the ante on the ad spends, and you're now quite visible on the traditional media. So, that's why this assumption is that more to do with the customer acquisition or is it more to do with the benefits what we are getting because of the falling raw material?

Manish Dawar: Look, it's a little different hypothesis, because if you look at the voices which are coming from staples is basically they are talking about rollback of prices, because they are seeing very clear trends, whereby the input materials for staples category, or are actually getting rolled back. And typically, the discretionary segment follows the staples whenever the prices are going up or whenever the prices come down. So, therefore, that's the reason we are seeing that. We've still not seen a rollback, but let's see how the situation pans out.

Moderator: The next question is from the line of Srinath V from Bellwether Capital.

Srinath V: I would like to understand what is working for Costa Coffee given SSSG numbers have come strong, ADS is also very strong, so could you help us understand what is working in Costa Coffee? And from a new store opening perspective, are the similar formats to what it was before we had this scale down a few years back, are these a larger format stores or more kiosk, what would be size of a store, anything you could probably share? And the last one on Costa would be, is this largely a beverage only offering or are there food offerings also and how are the soft drinks doing, any broader perspective on product side also?

Manish Dawar: So, let me answer your second question first, Srinath. If you go to a Costa store in Bombay; we've already opened a store at Phoenix Mall Kurla and therefore you will be able to see the complete offering there. So, we have food present in our menu. You have sandwiches, you have wraps, you have rolls, you have cakes. So, there are snacking items and food items there. We have Pita Bread and Hummus. So, you can actually go and have lunch there. Having said that, the dominant contribution still comes from beverages. Our focus is to continue to push food as well, and that's how we are coming up with the innovations as far as Costa is concerned. So, it's kind of well balanced and well mixed as far as the overall menu contribution is concerned. Coming to your first question, in terms of what is happening in Costa. As we said, we are bullish on this category. Coffee is an aspirational category in the country. We consistently get consumer feedback that Costa Coffee is probably one of the best coffees in the market from a taste perspective, from a flavor perspective, and the genuine coffee lovers prefer Costa over other brands. So, that is what our

consumers tell us. Having attained that position, it is a matter of making sure that we reach the consumers through our distribution network and the stores network, and that is what we are trying to do. So, Costa, I don't know whether you're aware about the history, was acquired by Coke. So, there was a little bit of uncertainty as far as Devyani was concerned, and that's the reason we in between kind of started downsizing the brand, we did not expand. But we signed the fresh agreement around the IPO time last year and since then we've been kind of expanding the brand and it is gaining salience now. So, that is what is happening.

Srinath V: Yes, sir, I'm reasonably aware of the history. So, we've seen Pizza Hut store format evolved over the past eight years, and to some extent may not be to the same extent as in KFC. So, could you help us understand how the Costa format from a store size or a service area, have we changed from what it was three, four years back before the Coke acquisition, how are you looking at the store rollouts? And the last one there, is 20% SSSG price-driven or our own stores are also seeing volume growth?

Manish Dawar: if you were to go back, let's say four, five years, we used to focus on a little larger format as far as Costa was concerned. In the new avatar, it's a good mix of whatever is working in a particular environment. So, we do have a focus on a smaller store; we are not heavily focusing on large format lounge type stores. These are very, very functional, very accessible to consumers, very easy for consumers. But at the same time, because we need to establish Costa as a brand, we also look at some of the flagship locations. So, it's a mix of both, but our focus will be on smaller format Costa Coffee stores.

Srinath V: Last one would be the SSSG. Is it price-driven, volume-driven, any broad qualitative feedback you can give?

Manish Dawar: It's largely volume-driven, very, very small impact of pricing.

Moderator: The next question is from the line of Kaustubh Pawaskar from Sharekhan By BNP Paribas.

Kaustubh Pawaskar: Sir, my question is on the gross margins again. In your initial comments, you alluded to the point that product mix change has some bit of impact on the gross margin. So, can you just explain that point, is it specifically towards Pizza Hut or for the overall portfolio, sir?

Manish Dawar: Yes, Kaustubh, it is specifically for Pizza Hut, and the product mix that we talked about, was basically the Fun Flavor portion that I talked about in the earlier answers.

Kaustubh Pawaskar: Also, in that case, for Pizza Hut, we used to be around 74% to 75% gross margins. So, is now the product mix kind of margin-dilutive? So, should we expect our gross margin of Pizza Hut to stabilize at around 72% to 73% going ahead once your raw material prices stabilize, or there is a scope of margin improvement once inflationary environment is stable?

Manish Dawar: So, as far as Pizza Hut category is concerned, a few days back, there is a Rs.3 increase in the milk prices, which will lead to almost Rs.30 to Rs.40 for cheese prices. So, therefore, the inflationary environment still remains. And at the same time Fun Flavor is also diluting the margins a little bit, whereby I said that we are working on correcting that and it will take us a few quarters to kind of get the Fun Flavor margins in line with the rest of the portfolio. And post that, let's say, once the milk prices and cheese prices are stabilizing or they're getting rolled back, we could see the gross margins inching up.

Kaustubh Pawaskar: My second question is on KFC. You mentioned that you're also looking for some large format stores in some of the markets. So, whether it will initially have impact from the cost front, because normally, if the store size is higher as the cost is on a higher side, so, considering that, just wanted to understand that what exactly would be the size of the stores and how the store fundamentals would be for this KFC?

Manish Dawar: So, at a store level profitability, what you're saying is right, that, there could be small impact because of the rentals and all. But the reason why we are doing it, because we expect that because of the larger format and expanded menu, we will have the increase in ADS for the stores, which will more than make up for the increase in costs. So, therefore, there could be some timing mismatch, because obviously, we have to first put up the stores and then the consumers will start to walk in. But otherwise, in general, we do expect that this will result into high ADS, this will result into higher brand acceptance and gaining prominence, and therefore it will be good for the P&L as well.

Moderator: The next question is from the line of Jaykumar Doshi from Kotak.

Jaykumar Doshi: Sorry, I joined the call late. If I am repeating the question that was already answered, I'll go back in the queue and read the transcript. There's some weakness generally in ADS across the space. So, how do you think about store opening targets that you have set for FY24 or calendar year 2023 target? Second is, in case of KFC, or maybe even Pizza Hut, what percentage of your stores will open in new cities, essentially, current demand environment may not matter as much you're opening the store in a single city store? And how many stores would you open in the existing markets where you already have stores, there could be some cannibalization?

Manish Dawar: Jay, I did answer the earlier question on the number of stores, but let me just kind of repeat it. So, we've talked about opening 250 to 300 stores even in the current environment. If you see our guidance in the past has been 250 stores of late we've been talking about 250 to 300 stores. As a result of the current environment that you've rightly pointed out, we are not changing the store opening guidance, we will remain with 250 to 300 stores. However, depending on the immediate market situation, there could be some mix change. So, for example, we are definitely looking at opening higher number of KFC stores and a little lower Pizza Hut stores, but overall, the store count will remain the same, and we are not changing that. We remain bullish as far as the overall market is concerned. We do understand that currently, because of the inflation, consumer sentiment and the consumer demand is impacted, but we remain bullish in the medium-to long-term and we don't see any concern.

Jaykumar Doshi: How many new cities would you be entering for KFC?

Manish Dawar: So, we continue to open at least four to five new cities every quarter and that is what we'll be doing. So, therefore, the entire strategy is all around densification in the existing cities, plus the new cities, plus as you know there are some cities where we have single stores, and we continue to evaluate them for opening more stores.

Moderator: The next question is a follow up from the line of Percy Panthaki from IIFL Securities.

Percy Panthaki: So, I'm just looking at your corporate overheads. In Q3, last year, it was Rs.34 crore which was 5.4% of sales, this time it is Rs.28 crore which is 3.5% of sales, so there is 190 basis points saving on this as a percentage of sales, which has really sort of helped your overall company level margins. So, can you just help us understand why this is the case even in rupee million terms, the number is down by about 18%?

- Manish Dawar:** So, Percy, given the current environment, obviously, we've tightened our belts, and there have been some initiatives on the cost control and cost reduction. But, at the same time, there is a small element of some old provisions which are no longer required, and that also was written back, but that's a small one. But, overall, we are tightening the belt because of the current environment, and therefore, that is not a big concern area for us.
- Percy Panthaki:** So, going ahead, shall we take this Rs.33 crore to Rs.34 crore as sort of a quarterly number in future?
- Manish Dawar:** Yes, you can take around that number.
- Percy Panthaki:** Secondly, just wanted to understand, in terms of your margins at a restaurant level, I mean, I'm not looking at individual format, I'm just looking at the overall restaurant level as a company assuming that there will not be much mix change in restaurants going ahead. The kind of margins that we've done this quarter, are they here to stay temporarily given where the input costs, given where the demand environment is, etc., or do we see some revival, because at an individual restaurant level, margins have fallen by about 250, 300 basis points in your two major formats?
- Manish Dawar:** Percy, if you see the restaurant level margins are typically driven by the ADS numbers, and the ADS is a little lower in the season, even though it's a good season. So, which I said is a combination of basically some of the new store openings, and at the base, we are kind of opening the new stores, because if you look at the pace, we are probably the leaders in the industry as far as the new store openings are concerned. But as things start to stabilize, as the new stores start to mature, and they start coming into the base, we will see the margins coming back.
- Percy Panthaki:** Lastly, on Costa Coffee, while your margin profile is very healthy, the sales per store is sort of pretty low at about 2.5-3 million per quarter. So, do you think that given the kind of format you're operating, this is the kind of sales per store that you will generate, and let's say someone like a Starbucks is a completely different format, and they make like 7.5 million sales per store per quarter, which is like maybe 2.5, 3x times of yours, so that's not a number that we would aspire for, given that it's a completely different model or you think there is significant headroom for improvement in this number?
- Manish Dawar:** So, we are not looking at that number, and to be honest, we are not aspiring for that number also, because, as you said, it's a completely different format, and it's a completely different positioning. As far as we are concerned, we want to have a healthy mix of both top line and bottom line, and that is how we are approaching all of our brands. As I said earlier, we are focused on the food category, and this whole focus and stabilization of the entire supply chain will give us some additional ADS numbers. But, for sure, we are not aspiring at 7.5 million kind of a number.
- Moderator:** The next question is from the line of Akshen Thakkar from Fidelity.
- Akshen Thakkar:** Most of my questions have been answered. I just wanted to push a little bit and understand the flagship store strategy. You said 10% of stores will be flagship stores in KFC. Is that 10% incremental or total? And if I were to think about sort of economics there, what's the kind of delta Capex or delta ADS, are we thinking about in the stores? I know it's more to do with just sort of keeping the product more relevant, more fresh, etc., but just in terms of how it plays out into numbers, one, two, three years out, just wanted to also understand, how much more Capex is spending on that, and what's the kind of incremental ADS gets out of that?

- Manish Dawar:** So, as far as KFC flagship is concerned, our immediate target is that whatever new store openings we are having, 10% of new store openings will be flagship stores. But, as we go along, and we get confidence from the format, our eventual objective is to have 10% of the total store count. Because we don't want to kind of push it and rush it in one-go. So, that's the reason as internal management team, we've taken a target of 10% of the store openings to begin with, stabilize the format, see, what the results are coming, is the increment ADS coming or not coming, but our eventual objective is to go to a 10% store count for the entire portfolio. So, very marginal Capex increase, about 8% to 9%, not much. And we are yet to see the firm numbers on top line coming up. But whatever store we've seen in the few weeks; the response is encouraging. So, we'll keep you posted as to how the strategy is going.
- Akshen Thakkar:** So, just going back to Percy's point on corporate overheads, on the run rate basis, given that where you are, what's the kind of growth we should expect generally going ahead?
- Manish Dawar:** We should expect the growth on corporate overheads to be in line with the normal inflation. And therefore, as we continue to expand our store portfolio and we continue to grow on top line, you will see a leverage coming in on corporate overhead and a percentage to the total sales will continue to drop.
- Akshen Thakkar:** If we think about in terms of trade that he have with some of the food tech platforms, given that some of those platforms are focusing more on profitability, are you seeing any changes in terms of take rates for them, etc., going up or your terms remain broadly same?
- Manish Dawar:** We've not seen the take rates going up as of now. Obviously, the pressure is always there; it's a two-way negotiation. So, so far, the take rates have remained stable for us, because we also are continuing to grow our store count, we are continuing to grow in volume. So, therefore, they are also getting additional business from us. So, therefore, to that extent, the relationship is very mutual and very healthy, and it's going well.
- Akshen Thakkar:** You mentioned that you're thinking about adding more KFC next year versus Pizza Hut, whatever your store opening this year was, maybe will be different. That mix will also have a bearing on your eventual store level EBITDA, right, because KFC has much better margins?
- Manish Dawar:** You're right.
- Moderator:** The next question is a follow up from the line of Devanshu Bansal from Emkay Global Financial Services.
- Devanshu Bansal:** Sir, the Total System Sales reported quite a bit of growth divergence within Q3, specifically, November was quite bad. So, if you could sort of throw some light on the trends during the quarter it could be helpful?
- Manish Dawar:** So, Devanshu, we also saw a little bit of weakness in November, because obviously, the two months, which is October and December, did well. So, let's see, I mean, we believe it is temporary, but yet to be tested, yet to be seen. Because our belief is that is predominantly because of the all-round inflation, which is happening, whereas the consumer wallets have remained the same. And at the same time, if you see the entire scenario on tech layoffs, that also is kind of gaining prominence, although let's say the tech layoffs are in the US, most of these companies have their back room operations in India, and they are also getting impacted. We've seen a lot of announcements from the Indian tech companies also where the layoffs are happening. And obviously, all of this has some bearing on the consumer sentiment.

Devanshu Bansal: So, December pick up from November, that growth trajectory continues in January or January is more or less similar to November?

Manish Dawar: Let's see, because obviously it's too early to comment on the overall quarter results, because we are not giving any month-on-month results, but let's see how it kind of shapes up but it's not so bad as probably if you're thinking.

Devanshu Bansal: Sir, Mr. Jaipuria also mentioned that there are quite a bit of new launches going ahead. So, if you could throw some light on that front, because they definitely are a big growth driver in the QSR industry?

Manish Dawar: We are not looking at any new brands as of now. Obviously, if we kind of finalize something, we will come back to you guys to make that announcement.

Devanshu Bansal: I was asking for new product launches, not brands.

Manish Dawar: So, that's a continuous cycle, Devanshu. As Mr. Jaipuria talked about KFC Innovation, in Pizza Hut, as you know we launched a complete range of Fun Flavor Pizza, we launched a new version of Momo Mia Pizza, we've launched new sides. So, therefore, that's a continuous process, and every quarter, we keep on doing something or other in our portfolio.

Moderator: The next question is from the line of Prashant Kutty from Sundaram Mutual Fund.

Prashant Kutty: Just one question on the demand front. We seem to be seeing a very different kind of a direction in terms of how pizza is behaving or probably how burger is behaving. Any thoughts on this front, especially because you also spoke about opening flagship stores, is anything to do with the fact that maybe the last two years is more about delivery and this year seems to be more about dine-in or things kind of coming back, can one probably pick out some trends in that?

Manish Dawar: Prashant, look, obviously, as we spoken earlier also, I mean, last two, three years, there are no trends emerging, because we got impacted by COVID first, which kind of changed the entire consumer thinking, that lasted for almost two years. As we were coming out of COVID, obviously, there has been a significant inflation pressure that all the commodities and most of the categories are witnessing. So, obviously, these are not the normal times that you're able to kind of see the trends and extrapolate those trends. But, again, fundamentally, how we look at the business, if you look at India as a country, the way the demographics are, the way the income levels are growing, the way the consumption habits are changing, we are absolutely and we remain bullish on the QSR segment, it is highly under-penetrated in the country, and there is a strong potential. Now, within that, obviously, these are some short-term impacts, which are there, and that's the reason we're not changing our strategy, and we continue to remain bullish, and we continue to kind of execute on our strategy.

Prashant Kutty: That's why I just want to know when you talked about, there's a focus more towards KFC, Pizza Hut obviously was more about our turnaround story, and it kind of kind of achieved that. But, here after probably, incrementally, is there a case that the opportunity is more on KFC rather than on Pizza, because we are the challenger over here, is that a thought or there's an equal amount of focus towards both?

Manish Dawar: There is an equal amount, because if you see, these are all temporary adjustments, for example, it is easily possible that in a year, we could focus more on KFC, in the maybe next few quarters, we could focus more on Pizza Hut, because obviously we want to optimize the return on capital, and that is how we approach the business.

But otherwise, fundamentally, pizza category also remains a large category, it is a growth category, it remains an attractive category, there's nothing wrong with the category as such.

Prashant Kutty: Last question is on the margins. Obviously, last year were more driven by the fact that there were a lot of tail winds as well. This time you do have headwinds, because especially on the back of gross margins and all. At a steady state level, when you look at a restaurant EBITDA margin for KFC or for Pizza Hut, are these the norm which we should take up as the restaurant EBITDA margin numbers, or what should be the right benchmark?

Manish Dawar: So, as we see the ADS improve, as we see the SSSG improve, as let's say, we have the new stores maturing on the maturity curve, we will see some improvement in the brand contribution margins.

Prashant Kutty: So, suffice to say that maybe something like for a KFC, '21-22 is more like a normalized level and maybe for a pizza at '16-17 is like a more normalized level, is that a fair assumption to make, in a normal scenario, I'm not saying for guidance?

Manish Dawar: Yes, that's a fair assumption, I mean, give or take some points here and there, but otherwise, in the normal scenario, you are right.

Prashant Kutty: As demand has been extremely weakened, are things only deteriorating, is there a worry for us?

Manish Dawar: I think probably the worst is behind us.

Moderator: The next question is from the line of Deesha Jain, an individual investor.

Deesha Jain: I'd like to understand a little bit more on your store opening strategy, like how do you choose a new location and what is the split between metros and non-metros for Costa?

Manish Dawar: Costa predominantly is a metro phenomenon as of now. So, there are very few stores which are outside the metros, maybe a handful, but otherwise it remains a metro phenomenon as of now, because that is whereas you know bulk of the consumption is. As far as the store opening rigor is concerned or the discipline is concerned, Costa is no different compared to our other brands. So, we have multiple databases available, we have the consumption habits available for various trade areas. So, whatever rigor we follow for opening a KFC store or a Pizza Hut store, is followed for Costa as well. Costa, as of now, we are focused more on metro areas, because the store count is really small compared to where we are on KFC and Pizza Hut. And once we've kind of done that, we will start to go into the smaller geographies as well.

Deesha Jain: How long does a Costa store take to stabilize looking at your aggressive expansion trying to breakeven basically?

Manish Dawar: So, we normally try and achieve the breakeven in the first six to 12 months for our entire portfolio of stores and the maturity curve will be close to 24 months.

Deesha Jain: Just trying to understand the ADS of Costa enjoy versus KFC and Pizza Hut, these kinds of brands, because coffee as such is a margin-accretive product?

Manish Dawar: It is not very different; so, Costa also is about close to Rs.400 to Rs.500.

Deesha Jain: For the value?

Manish Dawar: Yes, within that you have coffee, which is a strong margin contributor, food is little kind of lower compared to coffee. Our focus is to kind of push the food category because that will eventually help to build Costa ADS also. So, therefore, that is how we are approaching the brand. So, our objective is that for Costa, the margins should be in line with our rest of the brands and rest of the portfolio, so that it is not dilutive on the overall business.

Moderator: Ladies and gentlemen, this was the last question for today. I would now like to hand the conference over to the management for closing comments.

Manish Dawar: Thank you, chairman and all the investors, analysts who have been on the call. I do hope that we have been able to respond to your questions satisfactorily. Should you need any further clarifications or would you like to know more about our Company, please feel free to contact our Investor Relations team. Thank you once again for your time to join us on this call today and to participate in our growth journey.

Disclaimer: This is a transcription and may contain transcription errors. The transcript has been edited for clarity. The Company takes no responsibility for such errors, although an effort has been made to ensure a high level of accuracy.