Q3 FY2020 Earnings Call Transcript – January 23, 2020

CORPORATE PARTICIPANTS

- Amit Jatia – Vice Chairman
- Smita Jatia – Director
- Suresh Lakshminarayanan – Chief Financial Officer
- Devanshi Dhruva – Deputy Manager, Investor Relations

Moderator: Ladies and gentlemen, good day and welcome to the Westlife Development Limited Q3 FY20 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference call, please signal for an operator by pressing "*" then "0" on your touchtone phone. I would now like to hand the conference over to Ms. Devanshi Dhruva from Investor Relations. Thank you and over to you.

Devanshi Druva: Thanks, Stanford. Welcome, everyone. And thank you for joining us on Westlife Development Limited Earnings Conference Call for the quarter ended December 31, 2019. We are joined here today by Mr. Amit Jatia, Vice Chairman; Ms. Smita Jatia, Director; and Mr. Suresh Lakshminarayanan, our Chief Financial Officer of Westlife Development Limited.

Please note that our financial results and investor presentation had been emailed across to you earlier and these are available on our website, www.westlife.co.in. I hope you had the opportunity to browse through the highlights of the performance. We shall commence today's call with key thoughts from Amit, who will provide a strategic overview, which shall be followed by Smita to take you through the key business initiatives, and Suresh will cover analysis of the financial performance and highlights during the review period. At the end of the management discussion, we will have a Q&A session.

Before we start, I would like to remind you that some of the statements made or discussed on this call today may be forward-looking in nature and must be viewed in conjunction with the risks and uncertainties we face. A detailed statement and explanation of these risks is available in this quarter's press release, investor presentation and in our annual report, which is available on our website. The company does not undertake to update these forward-looking statements publicly.

With that said, I would now turn the call over to Amit to share his views. Thank you, and over to you, Amit.

Amit Jatia: Thank you, Devanshi. Good evening, everyone. And wish you all a very Happy New Year. I am pleased to share that we have ended 2019 on a strong note. Our **consistent** focus on the customer has yielded strong results, making this quarter as the 18th consecutive quarter of positive same-store sales growth for Westlife with robust top line sales and margin growth.

Consumer preferences are changing rapidly, including their food choices and the way they are using restaurants. At Westlife, our secret sauce has been to be able to anticipate consumer needs and evolve at a very fast pace and to be able to give them what they want, even before they demand it. This has helped us build a robust foundation for the business and navigate cyclical uncertainties and volatility.

As you can see, our consistent results spanning over four years stand as a testimony to the success of our long-term business strategy. With this, we remain confident of delivering on our Vision 2022 that we had set out in 2016.

Over the last few years, we have seen a consistent and sustained spike in our same-store sales. For example, a restaurant that had a sale of Rs. 100 in Q3 2015 is, today, selling over Rs. 163, which is a phenomenal growth of 63% in the same restaurant in four years. This has been possible because we have been extremely focused on building a brand that is relevant for consumers across all locations and day parts, including coffee, breakfast, snacking, meals and delivery. Today, McCafé is being consumed with breakfast, between meals or even for a quick catch up.

With delivery, we are offering consumers the convenience to consume us at home or in office, making McDonald's a delivery favorite. Millennials absolutely love the digital-friendly EOTF restaurants, which makes us a preferred hangout destination as well. With continued growth in scale and penetration in each of these segments, we are now essentially a 'one for all and all for one' destination for our consumers - a unique proposition for any QSR in India.

Simultaneously, in the last four years we have continued to maximize efficiencies and move both our restaurant operating margin and operating EBITDA by over 400 to 500 bps, and that's almost 130 bps a year consistently. As you may know, we are the only QSR with a strong backward-integrated supply chain and long-term real estate lease structures with a high quality diverse portfolio, including drive-thrus. In the coming years too, these investments will continue to serve us as a definitive competitive advantage and will help us propel growth aggressively.

With all our bold initiatives, our Vision 2022 seems stronger than ever and we very excited to chart our next growth phase.

I now hand it over to Smita, who will share the highlights of the quarter with you.

Smita Jatia: Good evening, everyone. And thank you for joining the call. We are pleased to report that we have yet again clocked a profitable quarter with strong top-line growth of 16.8% and an SSSG of 9.2%. This is on top of a high 14.5% SSG registered same quarter last year and indicates robust performance. With this, we have achieved the 18th consecutive quarter of positive SSSG.

Moving on to Slide #4. Our consistently strong results are a testimony to the fact that our strategy is focused on a strong consumer proposition of value for money and experience is resonating strongly. In line with our plans, we have been adding new restaurants in key cities to enhance accessibility. We also continue to boost our value platform, brand extensions and customer experience.

This, coupled with strong cost controls and enhanced operational efficiencies, is aiding continued margin expansion. I am delighted to share that for two consecutive quarters, our Restaurant Operating Margins, EBITDA and operating EBITDA have jumped by more than 200 basis points.

Like Amit explained earlier, with sustained SSG, we have been able to increase average sales per restaurant by 63%. And consequently, our operational profitability has also shown significant jump. ‘Our brand’, ‘our restaurants’ and ‘our people’ continue to be the key pillars of our strategy to drive exceptional customer experience.

Moving on the details of key brand initiatives. Quarter 3 - the quarter of festivities and celebration, has traditionally been one of the most critical quarters for our business. We ensured that we made the most of it by creating occasions for our customers to visit and re-visit us through our campaigns**,** meal campaigns and festive surprises.

We kept our value platform buzzing with the launch of the all-new McSaver Combos campaign. As a part of this campaign, we offered more than 50 combos of burgers with beverages at compelling price points. This variety@value proposition hit home with our customers and improved our baseline sales.

In October, McCafé achieved the milestone of serving 10 million cups of coffee. We leveraged this occasion by asking customers to share their special coffee moments, which helped build further brand love. We celebrated November as ‘Children's month’, by launching a family meal campaign. This gave us another opportunity to reinforce McDonald's as a preferred destination for families. The campaign enhanced the meal uptake significantly.

We continue to launch campaigns with different themes to connect with our customers and further enhance brand love. This quarter, we decided to add some festive cheer with ‘Not So Secret Santa’ campaign that enabled friends and families to share Christmas cheer.

As Amit highlighted, in the last few years, we have worked to create new occasions to drive more brand usage across day parts and in between, be it coffee, breakfast, lunch, dinner, snacks, delivery. We have something for all customer segments, for those who want value or variety or convenience or wholesome food that one feels good about consuming.

McCafé, McDelivery and McBreakfast have been the key drivers of this strategy that make McDonald's a QSR for all reasons and all seasons. This has helped us to widen our customer base significantly while ensuring that our existing customers, consume us more often, making us a ‘one for all and all for one destination’.

McCafé is now an established coffee destination. With 218 McCafés, we have the scale and the penetration to tap into this huge cafe market that is pegged at $9 billion, according to Euro Monitor.

McDelivery is charting an exceptional growth path. In fact, India was among the top 5 global McDelivery market for most number of deliveries achieved in one day this October. With 255-plus hub strong delivery network, we are very well positioned to capture the booming delivery market, both through our owned platform as well as third-party delivery partners.

At the very base of all our initiatives is technology and an omni-channel strategy, to ensure consistent and seamless customer experience across all our touch points.

Our innovative technology intervention, both in terms of our restaurants and our apps, have hit home with our millennial consumers. This can be seen in consistently good ratings that our Experience of the Future restaurants have been getting, and the fact that our McDonald's app has already had 3 million downloads within a year of its launch.

We continue to expand our restaurant footprint across key markets and cities as per our growth plans. This quarter, we added 11 new restaurants, taking the total restaurant count to 315. About 90% of these 315 restaurants have modern and contemporary interiors. Our digitally enabled Experience of the Future stores have been doing very well for us and we aggressively expanding our EOTF footprint.

Moving on to the next section. It is our people who bring our strategy alive and we remain committed to investing in them. In this quarter alone, we have invested over 60,000 man hours in training, one of the highest in the entire industry.

A great testimony to our training processes is the fact that three of our restaurant managers have received the Ray Kroc Award, the highest international honor that recognizes the top 1% restaurant managers worldwide each year for superior performance and operational excellence. This quarter, we also made it to the list of World's Best Workplaces, a feat we are extremely proud of.

With this, I hand it over to Suresh, who will take you through the details of our financial performance.

Suresh Lakshminarayanan: Thank you, Smita. Good evening, ladies and gentlemen. As highlighted earlier, we have continued strong on our growth path with a robust performance in Q3 FY20 despite the challenging times. Similar to the previous quarters of this financial year, we will be discussing the comparable numbers with you, which excludes the adjustments arising out of IndAS 116.

On Slide #24, as you see, IndAS 116 has the impact of reducing actual rentals and inflating interest and depreciation. And therefore, has a noncash impact of 83.5 million on our profit after taxes.

Moving to Slide #26. In Q3 FY20, we have clocked an SSSG of 9.2%, making it the 18th consecutive quarter of positive SSSG and total revenues witnessed 16.8% growth over Q3 of last year.

Our focus on value platform, superior performance of brand extensions as they help us to cater different day parts and occasions, coupled with enhanced customer experience, resulted in higher revenues. All our initiatives have resulted in revenue growing at a CAGR of 21.4% from Q3 FY17 to Q3 FY20.

On gross margins and RoM, as mentioned earlier by Amit and Smita, our SSSG has compounded by 63% in last four years. This has played a significant role in addressing the recent spurt in food inflation. Our consistently increasing volumes and improving operating efficiencies, along with the good work done by our suppliers on productivity growth, has considerably helped in growing our gross margins. Over the years, we have also mastered the art of managing our product mix well through menu, value platform and brand extensions. All these factors have come together to boost our gross margin, which has seen a Y-o-Y jump of 248 bps to 66%.

All of the said initiatives, along with judicious price changes, have helped us improve our gross margins by a whopping 560 basis points over the last three years. Gross margin increase, along with some operating efficiencies, led to a higher RoM for Q3 FY20 at 17.5%, leading to a margin expansion of 246 basis points Y-o-Y. The RoM improvement has resulted in a higher operating profitability, operating EBITDA margins have increased by 250 basis points Y-o-Y.

As we keep expanding and building scale, we are strategically reinvesting our profits back into the business to accelerate our growth journey. These investments, along with sustained focus on menu, value platform, product mix, brand extensions and supply chain efficiencies, have enabled us to increase our operating EBITDA by 622 basis points over the last three years.

Moving to the next slide. Our profit before taxes stood at Rs. 309.6 million with PBT margins at 7.2%. Q3 FY20 profit before taxes tripled over Q3 of last year due to higher sales and improved operating performance. From FY20, Westlife falls under the bracket of full tax rate and hence to that extent, PAT with previous years may not be comparable. PBT would enable you to get a sense on the actual improvement in our profitability over Q3 FY19. Our profit before taxes has grown 4x in the last two years, and overall, we have seen a 790 basis points improvement in PBT margins in the last three years.

Slide #30 highlights our profit after taxes, which stood at Rs. 227.2 million, witnessing a growth of 228%, despite the incidence of full tax rate from FY20 onwards. Overall, our PAT margins have expanded by 590 basis points in the last three years. Our Q3 FY20 cash profits stood at Rs. 449.6 million, witnessing over 52% Y-o-Y growth and a 3x growth in the last three years.

In a nutshell, we witnessed a healthy top line growth, along with significant expansion in operating margins and bottom-line. We believe that the Company is well on track to achieve its Vision 2022. All the initiatives and investments made currently will propel us in the right direction to achieve our target of sales growth and margin expansion.

With that said, I would now hand it back to Amit, who will take you through the outlook for FY20 and give his closing remarks.

Amit Jatia: Thank you, Suresh. We believe that the uncertainty in the economy will continue for some more time and consumer spending will remain cautious. Global events too may have a ripple-down effect. The task, therefore, for us will be to remain rooted to our core strategy that will help us navigate these uncertainties effectively and keep achieving our business results. We believe there remains a lot of untapped potential in our market and a huge opportunity for the brand to grow.

We will continue to invest in expanding our restaurant base, building on our menu platforms and providing exceptional customer experience. Our brand extensions have always been giving us a competitive advantage and we will continue to leverage them. With a whole lot of interesting consumer-facing initiatives lined up for the coming months, we feel stronger and more confident than ever to chart the next five years of accelerated growth.

Thank you. And with this, I open it up for Q&A.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Avi Mehta from IIFL. Please go ahead.

Avi Mehta: Just three questions. I mean, if I look at your SSS growth that you witnessed in the third quarter, it would be useful to kind of understand how the demand environment is panning out as we go forward, and is this trend sustaining?

Amit Jatia: Okay. You want me to respond to this, or…?

Avi Mehta: No. I mean from whatever I can understand at this point is, if this trend is kind of going where it is, would you re-look at or would you see SSS growth kind of exceeding the 7% to 9% kind of expectations that we were targeting that we were kind of earlier envisaging for FY20? That was my first question.

Amit Jatia: Okay. So basically 7% to 9%, we have given this guidance quarter-on-quarter and it's more a vision statement for a three to four year period. Essentially, last year, in fact we did 16%, 17% same-store sale for the full year and the year before that was similar, 15%, 16%. But it's hard to predict quarter-on-quarter, therefore we have given a 7% to 9% final indicator. As we explained on the call that we are 63% more than four years ago, and therefore, 10% growth on 163 is Rs. 16, while four years ago, a 10% is Rs. 10. And finally, it's not about percentages, it's about rupee amount. So we are quite confident that we will continue with this trajectory over the next three to four years. But whether it will go up or down, we don't like to sort of get into that conversation.

Avi Mehta: Sir, where I am coming from is, because overall is -- sorry, go ahead.

Amit Jatia: So, I was just going to say that sequentially we have been working very hard on getting quarter-on-quarter things, right, from 5.6%, to 6.7%, to 9.2%. But I wouldn't sort of jump on to say that next quarter will be 10%. So we maintain that, between 7% to 9% is really what is more realistic.

Avi Mehta: So where I am coming from Amit is, if I look at the broader environment, FMCG, the other consumer companies, we are sort of looking at the demand weakness or signs of demand weakness. It's actually very heartening to see you stand out and see actually a demand uptick on a quarter-on-quarter basis. That's what I was trying to understand, from an underlying, is this more company-specific or is the industry itself seeing some signs of pickup as well?

Amit Jatia: Avi, it is, I feel, to some extent, company specific. I mean, if you see, last four or five years, we have invested in reimaging and modernizing the consumer experience. But mostly, we built new occasions for the consumers to use and that has now got scale and traction. As we talked about 10 million cups at McCafé sold, that's a whole lot of consumers. And the point is, as this continues to scale, we feel that this whole idea about new occasions for the consumers to use, and this one-for-all and all-for-one, is much more than a statement. And I feel this is primarily what is helping us differentiate over the rest of the marketplace at this point in time.

Avi Mehta: Okay. Perfect. The second bit was on the margins. Last quarter, I recollect, you had highlighted that there was no one-off in the gross margin side, whatever has been is on the back of initiatives. Is there any one-off mix related impacting in this quarter or this is again cost-driven and hence we can assume this kind of level should sustain as we go forward?

Amit Jatia: See, if you do something consistently over four years or five years, and we talked about our gross margins going up, I think Suresh mentioned, 600 basis points, then it cannot be a one-off. I don't think I need to say anything further at all

Avi Mehta: No, Amit, I didn't mean from an expansion point of view. I meant the absolute level this quarter.

Amit Jatia: In absolute level, there is no one-off in it. Obviously, when our suppliers are seeing volume go up and their sales go up, as Suresh explained in his conversation, and along with that, we introduced the McSaver Combos. In McSaver Combos we actually took the price of a bunch of others down to Rs. 59 and yet we were able to deliver margin. I think we have really understood the playbook on how to manage that right from a consumer point of view, and that's working for us, along with the efficiency in the supply chain.

Avi Mehta: And lastly, the food inflation that we are kind of hearing. We do enjoy a very strong supply chain a lot of energy from it. Just wanted to kind of get your thoughts on given the strength would you still envisage right now the way food inflation is, that you would need to consider price increases or it's manageable?

Amit Jatia: No. See basically, we maintain that we will stay with the 3%-ish to 4% price increase every year. If I were to take the McSavers, which actually reduced prices, then our actual price increases would be even lower. So essentially, we will stay within the 3% band and then we have to take it from there. But, Avi, if we look at four years, sometimes onion prices go up, sometimes tomatoes, sometimes milk, so it's kind of built into the platform. And as long as the company, in my view, is pushing towards productivity growth of 100 - 200 basis points every year, knowing that inflation will hurt you by that extent somewhere or the other, I think you are all right. And that's what worked for us so far.

Moderator: Thank you. The next question is from the line of Gordon Yu from Arisaig Partkers. Please go ahead.

Gordan Yu: Amit, congrats for a wonderful quarter. I have two questions. Could you give us a little bit more color on the delivery side of mix? I mean, great same-store sales process, any sense of how much delivery contributed to that? Does that change your thoughts on whether you need to sort of invest more behind delivery? That's one.

Second question is, now that you have got the format right, the cost base, the operating structure, does this mean that you can open more stores going forward? Does that change your thought process on that at all?

Amit Jatia: Thank you for your questions. As far as delivery is concerned, while we don't share the breakup, obviously, there's a lot of energy and resources going into getting the delivery business to where it is. And I don't see it stopping in the medium term for sure. So essentially, I don't know if that answers the question, but all the energy that is needed to go into delivery will continue. But our overall thought process is that delivery is just another occasion for use for a McDonald's customer and that doesn't change. The focus on in-store business is as strong and actually that's been delivering results, which is why we have got a decent balance on our same-store sales growth and margins.

As far as store openings are concerned, I feel that we are as aggressive as we should be and we continuously change as we see things. But growth in terms of store openings is all dependent on how the sequential eating out in the marketplace changes, and the ability for a city to absorb more restaurants. I think we are sort of inching towards the 27, 28 numbers right now, at least on a gross opening level. We are constantly working hard to take it to 30, but you got to understand that until frequency of eating out takes a sharp uptick, it is not about anything else other than that.

So in our view, we have still been aggressive because if you look at the quality of the stores that we are opening, the locations in which we are able to go in with the same 20-year deals. Like recently in Mumbai, we opened in Prabhadevi which is an amazing market. If you look at Chennai, the Pondy Bazaar which is a very, very hard market and we have a free-standing McDonald's in there. In Goa, in Calangute, there's a free-standing McDonald's, right in the heart of the Calangute Beach.

So for us, the quality of the real estate, the portfolio, the deep structure is material. And along with that, the absorption in the market. So we are pushing ourselves, but I would still keep it in the 25 to 30 range at this point in time.

Moderator: Thank you. The next question is from the line of Manoj Menon from ICICI Securities. Please go ahead.

Manoj Menon: Congratulations on a brilliant performance. Just three questions, again on this whole delivery piece actually. One, while I understand the competitive sensitivity about disclosing the percentage, but one comment, is it a material number? Is it, let's say, something in the 20s is what I believe. I just want to understand am I completely off or is it like somewhere in that ballpark? If you may. That's one.

Second is the delivery which goes through the own fleet and versus the aggregators. Again, it is interesting to hear about the investments or the activities which we are doing on the owned fleet side.

The third question is the relationship with the aggregators. While I understand it is highly symbiotic, both need each other, etc. The conceptual thought process which comes over a longer period of time is where the negotiations probably will eventually lie, in terms of owning the customer, which may potentially have some implications on the margins. So those are the three questions.

Amit Jatia: Okay. Sure. I mean, it's all around delivery for sure. It is becoming an important part of the business, there is no doubt. We just don't share breakups but what we will do, we have our Investor Day coming up, which we do every two years, and that is when we deep dive and give a bit more information and color on each of the brand extensions. So we definitely will take your question and see what we need to do with it.

The good news is that the in-store business is also growing because McCafé is in-store, value is in-store and then our breakfast is in-store. But yet at the same time, yes, deliveries is becoming quite important. Even in rupee terms, in absolute numbers, even if you forget the percentage.

Secondly, we are pushing our own apps and all also very hard, but we absolutely love aggregators. They bring a much wider audience to us to consume our delivery offering. It's like being in a mall in a food court where all players are around, but it's the brand that really makes it sort of work for us. I don't know if, again, that answers your question, but we feel there's a good balance. We like to push our own app as well because we want to be present in the delivery platform. While at the same time, the aggregators, we have developed a very good partnership with them. And please remember, it is a partnership and that's the way we treat and work with them.

Now, obviously, in my view, we have seen this in other global markets where McDonald's operates. And we think that there is reasonable competitiveness within the aggregators. And we feel that we bring tremendous value to the aggregators in the way we integrate with the platform and our ability to service customers faster than anybody else. And therefore, I feel that as long as we continue to bring tremendous value to them and they bring value to us, I feel it's a balanced partnership. And that's why we are also ensuring that our own assets are doing quite well also. I hope these answer your question, but more in the Investor Day which is coming up soon.

Manoj Menon: Understood. Just if you may, just two quick follow-ups on this. One, for the business which comes through the aggregator pie, actually who owns the customer data? If it is possible to deliver that. And point number two, I mean, just thinking of the McDonald's product portfolio what we have, do you have to make any tweaks to the product itself to make it a little more delivery compatible?

Let's say, something like fries, which needs to be consumed immediately, in delivery probably it takes 15, 20 minutes to reach my home. So probably the product experience is slightly different than what you experience in-store. So two questions, who owns the customer data? And point number two, do you have to make any product changes per se to ensure that the experience is closer to the store?

Smita Jatia: So, we have different arrangements with different partners for sharing of the consumer data. So we wouldn't want to say, but we do have. And even with the ones who don't give us the full customer data, we get analytics from them and this makes it easier and better for us to be able to do more targeted marketing.

Second, when you are talking about the food products, we don't do anything differently on the food products, what we do differently is in the packaging part. So if you order a French-fries, you will see that the packaging you will get is different from what you get in the store, which helps to preserve the French-fries quality. But however, our insights on the consumer is that when it comes to delivery, it's not only our brand, any brand. They are willing to go a little bit in terms of what they expect on quality in the store and what they expect on quality at home on delivery.

Amit Jatia: For convenience.

Smita Jatia: Just from a convenience point of view because, obviously, they are getting it at their home. And we have not got any feedback which is negative on quality aspect on delivery platform.

Moderator: Thank you. The next question is from the line of Latika Chopra from JPMorgan. Please go ahead.

Latika Chopra: My first question was around this whole food aggregator space. Since you track various markets closely, what is your sense on the discounting intensity? In your view, is it going up, is it coming down, any trends that you are seeing?

Amit Jatia: We think it's coming down.

Latika Chopra: Okay. And secondly, 9.2% SSG is very heavy. What would be the quantum of pricing growth in here? Did you take any price increases during the quarter?

Amit Jatia: In fact, we introduced the McSaver Combo at Rs. 59 and there were no price increases in the quarter.

Latika Chopra: This will largely be volume led and would volumes be higher than this number?

Amit Jatia: I mean yes, we don't share the breakup again, but yes, it is driven by footfalls as well.

Moderator: Thank you. The next question is from the line of Anand Shah from Axis Capital. Please go ahead.

Anand Shah: Just a few questions from my side. So firstly, I mean, we have seen very good growth in SSSG. But despite that your margin improvement expansion has completely come largely from gross margins. We haven't seen that much leverage play out. I mean, so this would be a quarter phenomenon or at 9%, 10% shouldn't you start seeing more leverage as well?

Amit Jatia: See, that’s the point, that if you do this for four years, five years consistently, 130 basis points in operating margin every year, I feel it is operating leverage. Growth margins don't come out of the blue, especially if you see recently the inflation on food is very, very high. But when a supplier sees that volumes in four years have gone from Rs. 100 to Rs. 163, right, that gives them tremendous buying advantage on their side as well, along with the productivity gains, because the same fixed cost will spread over a much wider base. That, coupled with some of the efforts we have put on product mix, is really the benefit of that. So, one, operating leverage comes from there as well.

Two, as delivery has been growing consistently, do you see that anywhere show up in our margins? Because obviously, the delivery margin as we have always maintained is slightly lower, it's obviously very cash accretive but not margin wise. So obviously, it is the other benefits that we get that is taking care of this growth in the delivery commission payout. And therefore, you will see all other line items quite flat.

Anand Shah: Okay. Perfect. And just have one thing here, the McSaver Combos and all that you have launched, would percentage margin would broadly be in line with the company average gross margins or they will be a little dilutive?

Amit Jatia: We don't share that breakup. But I think to give ourselves some good credits, is that after launching McSavers, with a 9.2% same-store sales growth, without taking any menu price increases, I think whether we grow gross margins or whether we grow anything, I feel it is very, very nice.

Anand Shah: No, it is commendable. Good job, too. Secondly just on this EOTF roll out, I mean, can you share, let's say, the percentage of stores now that would be under the EOTF?

Amit Jatia: We have, again, I mean we like to share this on an annual basis, but roughly 60 - 70.

Anand Shah: 60- 70 of the 315 stores are roughly EOTF now?

Amit Jatia: Correct.

Moderator: Thank you. The next question is from the line of Ankush Agarwal from Stallion Asset. Please go ahead.

Ankush Agarwal: I have two questions. Firstly, where do you see gross margin, EBITDA margin moving over, let's say, two, three years? And what were the factors that would contribute to such growth? And secondly, sir, can you give, like absolute number of this rent and advertisement expense for this quarter?

Amit Jatia: So, we have said in our Vision 2022 and we were bold enough to say it in 2016 when EBITDA margin was 6% or so, and essentially, our EBITDA margin target is about 13% to 15%. We don't break up targets around gross margin, but essentially from an EBITDA margin point of view, 2022, the idea is to come within the teens, low to mid-teens. The second question was...

Ankush Agarwal: Breakup of quarter.

Amit Jatia: So yes. No, we don't give breakup but advertising I can give you generic sense that by the end of the year, typically, it's between 5%, 5.5% of sales. But we don't break up rent on a quarterly basis.

Moderator: Thank you. The next question is from the line of Ikshit Naredi from Naredi Investments. Please go ahead.

Ikshit Naredi: My first question is, right now the gross margin is 66%, so how sustainable these margins are in next couple of years?

Amit Jatia: Well, as far as we are concerned, I go back to history. And essentially over the last four, five years, we have grown it by 600 basis points. And the key focus for us is really to grow operating EBITDA margin. We don't really focus on individual line items. And when we make any decision, we are looking at finally the sale, is it adding to the bottom line. Because if you look at PBT and all of that, that's over 760 basis points in just the last three years alone.

So I don't want to be very myopic, but we feel that, yes, 100 basis points here and there, definitely sustainable. But please focus on operating EBITDA, which essentially we have done about 500 basis points of improvement in the last three to four years. And as per Vision 2022 number, so we do expect that to continue to grow in that same manner.

Ikshit Naredi: Okay. And my second question is, you gave us a target of 400 to 500 restaurants in 2022, so are we on the track to achieve that target? Because like, we opened 316 restaurants until now.

Amit Jatia: Yes. So I had said that we will be at the lower end of it, so around 400-plus restaurants is where we expect to end up as per Vision 2022.

Ikshit Naredi: Okay. And my third question is, is there any price increase in Q3 or are you planning to increase in next quarters?

Amit Jatia: We can't talk about the future, but in Q3 there was no price increase. Essentially, in fact, we kind of took a price decrease if you think about it, with the launch of the McSavers Combo at Rs. 59.

Ikshit Naredi: And my last question is, like which one is more profitable at giving higher margins, McCafé or McDonald's, if we talk about it?

Amit Jatia: Both are the same.

Ikshit Naredi: No. Like, obviously, the McCafé is a total coffee thing and the McDonald's is like there is some food stuff, so like that's giving higher margins?

Amit Jatia: We don't see them separately, to be honest. And I have explained our 1+1+1 is equal to 5 theory earlier. If we were to take cafe standalone, obviously, these numbers just can't be delivered. So therefore, this is a combination of everything. At the gross margin level, normally beverages do give you a higher gross margin, but at the total business level, you have got to look at that together.

Moderator: Thank you. The next question is from the line of Sameer Dalal from Natverlal & Sons Stockbrockers. Please go ahead.

Sameer Dalal: Two quick question. The first is, any update on the royalty for next year with McDonald's International? And the second one is, on your new stores with the modernized look, what is the kind of maintenance CAPEX you are having to spend on a per store basis? If you could give some guidance on that.

Amit Jatia: Sure. Royalty has been announced for the next five years, and it's in the public domain on the website, so you can get that from there. As far as maintenance CAPEX is concerned, we don't share breakup. But typically, almost 80% - 85% of our CAPEX is going into new stores and the bulk of it, the rest of it goes into reimaging, EOTF and things like that. So CAPEX for maintenance is quite small actually.

Moderator: Thank you. The next question is from the line of Priyanka Sarkar from HSBC. Please go ahead.

Priyanka Sarkar: Congrats on a great set of numbers. Sir, I just wanted to ask, can you please take me through the unit economics? If you tie-up with Swiggy and then you deliver, so what is the amount you have to pay per Rs. 100 or anything of that sort, if you can kindly explain the unit economics, please?

Amit Jatia: Sorry, we don't share the breakup and we don't share our unit economics with each of the aggregators. As we have maintained before is that its cash accretive, because as we discussed slightly earlier in the call, the food delivery business is rising dramatically. And in the last Investor Day, we have given some sense on the average volume that our restaurant was doing as well, but yet we are generating extra rupee margins. I think, therefore, it works for us. That is the best we can share when it comes to aggregator numbers.

Priyanka Sarkar: Would it be possible to say that the discount given on some of these apps, that amount is taken on the balance sheet of the aggregators or is it taken by us partly?

Amit Jatia: So we at McDonald's, HRPL, Westlife, we don't give any discounts on delivery, on third-party apps.

Moderator: Thank you. The next question is from the line of Darsh Gada from Prabhudas Lilladher. Please go ahead.

Darsh Gada: Congrats for the good set of numbers. We have 315 restaurants, out of that only 218 have McCafé. So, is the space available for the new McCafé concept to be introduced in those stores?

Amit Jatia: Yes, they are. The idea is eventually get 100% penetration.

Darsh Gada: Okay. And all the new stores have the McCafé concept introduced in it?

Amit Jatia: Mostly, yes. I mean, the idea is to open restaurants with McCafé.

Moderator: Thank you. The next question is from the line of Rushabh Doshi from Pro Invest Wealth Managers. Please go ahead.

Rushabh Doshi: Great set of numbers. In Maharashtra, the state government has decided to keep open malls and stores, so would this add any value to us, like have you talked about it?

Amit Jatia: Yes. I mean, we have been working very proactively with the government to introduce such a thing and we think it's very progressive of the government. McDonald's does this across the world and we have been sort of really asking the government to help us doing a 24/7 opportunity. So we are definitely going to take opportunity from there. And yes, it's very interesting. It will help the brand and the business.

Rushabh Doshi: So what's the plan like, to keep all the stores open or to try it out on a pilot basis? Or the stores at the mall would be open?

Amit Jatia: So leave it to us, we will do it in the right manner. I mean, because the law does not allow us to do it across the board. So want to first completely understand what they are talking about and then take it from there. So like we have done McCafé, the EOTF rollout, we are pretty seasoned at getting a sense of how to go about it. But whatever we do, it's going to be aggressive and it's going to be quick. But it's a very good beginning from the part of the government.

Rushabh Doshi: Right. And I just wanted to understand your definition of same-store sales growth, how do you do it?

Amit Jatia: Our definition is quite simple, it's global. Of course, they are more detailed out in the press release and all that. But from the 13th month of the store having opened, it grows comp, it grows comparables.

Moderator: Thank you. The next question is from the line of Latika Chopra from JPMorgan. Please go ahead.

Latika Chopra: Just a small follow-up. If you could share, how many of your restaurants today have the breakfast option and what was that number about a year ago?

Amit Jatia: Currently, about 199 restaurants have breakfast, so say, 200. I think it was 155 earlier.

Latika Chopra: It was 155 earlier and now it is, sorry?

Amit Jatia: 199, say, 200.

Moderator: Thank you. The next question is from the line of Sabyasachi Mukerji from Centrum Portfolio. Please go ahead.

Sabyasachi Mukerji: A couple of questions. What is the major raw materials that you use? If I can kind of track the material prices, so if you can help with that.

Amit Jatia: Sure. I mean it's chicken, tomatoes, onion, vegetables, flour, oil. I mean typically whatever you would see in a food business. Chicken, potatoes, oil, packaging material, which is do with paper, for example. What else, I am thinking. A lot of vegetables, potatoes, peas, carrots, wheat, yes wheat is important. I think broadly, this would be the category. I mean, if you think about it, buns, patties, milk, cream, sugar, tea, cheese, all of that is pretty much we have.

Sabyasachi Mukerji: And what would be milk in your raw material in terms of percentage?

Amit Jatia: We don't share the breakup.

Sabyasachi Mukerji: Okay. No, because from the point where I am coming is that, milk prices have gone up in past few months.

Amit Jatia: It has gone up in the past five years many times, up and down. You see the point is, as I said before, we are dealing with commodities and something or the other is going up. And there are times that we have seen when everything has gone up. While one or two things are going up, one or two things are going down. So, over the last 10, 15 years, trust me, we have a pretty good sense.

Yes, we are taken by surprise sometimes. But I have always maintained that quarter-on-quarter, obviously, we can't deal with it. But on a yearly basis, we have been able to work on that quite nicely. Because today, there is kind of 10 years of data for HRPL in the public domain and you will notice that I think we generally handled that quite well. So we have long-term contracts, proper process, we work with farmers, we have a fully integrated supply chain backward all the way linked to the farm, the cold chain is run by our third-party suppliers. So it's a very well-oiled machine.

Sabyasachi Mukerji: Got it. Second, on the delivery commission fees that you have to pay to the food aggregators. Where exactly does it get reflected in the P&L, which line item specifically?

Amit Jatia: In the occupancy and other expenses.

Sabyasachi Mukerji: Okay. So if I look at the restaurant operating margin, that is inclusive of the delivery fees, the delivery fee commissions, right?

Amit Jatia: Absolutely. That's why it's called restaurant operating margin, so every cost except depreciation and corporate overhead, it's all in there. I think that's why we decided from day one to clearly show you restaurant operating margins.

Sabyasachi Mukerji: Right. And below that, the selling and general, the SGA expenses are basically corporate overheads?

Amit Jatia: Correct.

Moderator: Thank you. The next question is from the line of Rahul Jagwani from SKS Capital. Please go ahead.

Rahul Jagwani: Congrats on a great set of numbers. I just want to ask now, now what's the plan further? I mean, basically to grow EBITDA margins? I mean, will we just be increasing share of, say, McCafé, which will contribute to margins or are there other areas where we can cut costs or, I mean what are your thoughts about that?

Amit Jatia: See, I mean, again, the good news is, I think we have been probably the only brand that actually rolled out a Vision 2022. And if you look at our two investor presentations that are also available on the website, you will see how we are bridging the growth in the future. We have said very clearly that it is operating leverage and we feel it's playing out, whether it's playing out in one line item or another, the important thing is that it is playing out.

So primarily, it is the menu and the restaurant experience, along with different occasions for use, which is beverages, which give us certain occasions, whether it's breakfast or whether it's the delivery business, each one of these items is where we are going to grow. Five years ago, when the numbers were slightly different, it was the same question and it's the same question today. But the important thing is, it is these drivers finally. I mean, finally we are a QSR, so these are the five, ten trend drivers that we have. It's going to continue to be these drivers.

Moderator: Thank you. Ladies and gentlemen, I now hand the conference over to Mr. Amit Jatia for closing comments.

Amit Jatia: Well, thank you, everybody, for patiently listening to our call and for being on the call. If you have any additional questions, please do reach out to Devanshi. And of course, you have the website as well. Thank you, have a lovely evening. Bye.

Moderator: Thank you very much, sir. Ladies and gentlemen, on behalf of Westlife Development Limited, that concludes this conference. Thank you for joining us. And you may now disconnect your lines.