Q4 FY2020 Earnings Call Transcript – June 12, 2020

CORPORATE PARTICIPANTS

- Amit Jatia – Vice Chairman
- Smita Jatia – Director
- Pankaj Roongta – Chief Financial Officer & Vice President - Finance & Accounts
- Devanshi Dhruva – Deputy Manager, Investor Relations

Moderator: Ladies and gentlemen, good morning and welcome to the Westlife Development Limited Q4 FY20 and 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 the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Ms. Devanshi Dhruva from Investor Relations. Thank you and over to you ma'am.

Devanshi Dhruva: Thanks Lizann. Welcome everyone and thank you for joining us on Westlife Development Limited earnings conference call for the quarter and year ended 31st March, 2020. We are joined here today by Mr. Amit Jatia – Vice Chairman, Ms. Smita Jatia – Director and Mr. Pankaj Roongta – our CFO and VP Finance and Accounts for Westlife Development Limited.

Please note that our financial results and investor presentation had been mailed across to you 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, its overall operational progress, the impact and response to COVID19 ad the strategic imperatives that lie ahead. Pankaj 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.

A request to participants given the disruption due to COVID19 members of the management are joining the call remotely and is there could be some lag when responding to your queries. I urge you therefore could you kindly bear with us. Before we start, I would like to remind you that some of the statements made or discussed on this call today maybe 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. Hello and good morning to everybody, thank you for joining the call this morning. I hope all of you and your families are safe. These are our full-year results and I'm delighted to share that we have continued to build on for growth momentum and delivered a strong FY20. We believe we have built the business on the back of a strong long-term strategy grounded in consumer insights that has enabled us to remain relevant to our fast evolving customers. As a result over the last 5 years our SSG has grown by over 60%, our revenues have grown at a CAGR of 18.5% and we have improved our operating EBITDA by close to 400 bps that's more than 130 bps a year. We started FY20 on a strong note with great momentum of 18 quarters of positive same-store sales growth. Through the year we consolidated our position as a one for all and all for one destination and continued aggressive rollout of McCafé and EOTF restaurants. We have continued to invest in building a strong digital backbone through our apps. We saw a significant growth resulting from these initiatives, which continued all the way up to January and February of this year. However in March a pandemic caused a major disruption in the business. The lockdown led us to temporarily shut all our 319 restaurants overnight and presented unprecedented challenges. But as they say when the going gets tough, the tough gets going. In the wake of this massive challenge we came together as an organization and showed great agility to ensure business continuity with the safety of our employees and customers at the heart of all our efforts. We have always been committed to using our scale for good and in the wake of the ongoing pandemic we have ensured that we've reached out to communities that were most impacted by the crisis. We've partnered with several NGOs and served safe and hygienic food to more than 56,000 daily wage earners and some slum dwellers across 5 cities, something I feel immensely proud about.

Over the years I have repeatedly mentioned that we have a high quality of diverse real estate portfolio, long-term lease structures and a strong backward integrated supply-chain that together serves us as a definitive competitive advantage. It now feels almost prophetic as through these challenging times it was these spends that provided us the foundation to bounce back quickly and minimize the impact of disruption. We remain confident that our rock solid foundation, agility and conviction to lead the way for the industry with big bold moves will help us maintain a strong growth momentum in the long-term.

Before I hand it over to Smita for an overview of our FY20 and Quarter 4 results, I would like to introduce our new CFO, Pankaj Roongta, who joined us at the beginning of this financial year. Pankaj brings over 20 years of experience across sectors and will later take you through the financial details of our FY20 results but for now over to Smita.

Smita Jatia: Thank you Amit and good morning to all. I trust all of you are keeping safe. The COVID19 pandemic is a black swan event that has disrupted businesses and economies across the globe. However, at Westlife we saw this as a challenge as a defining leadership moment and embraced it to increase agility, take quick decisive actions and empower teams to come out of it bigger, better and stronger with our war cry 'serving happiness with extra care'.

I will cover slides 4 to 6 by giving context of COVID to our business. At WDL we started preparing for this crisis even before COVID19 started gaining ground in India. We proactively stepped up our already world class safety and hygiene processes and ensured that all our employees were well-trained and had complete access to all protective gear. We also went a step ahead to ensure that similar standards of hygiene were also been followed by our suppliers to give our customers food that was handled with utmost care and safety, right from the farms to their plates. Staying ahead of the customer trend we became the first QSR to launch the innovative contactless delivery service. Simultaneously, we brought alive the combined strength of our delivery, take out and digital business quickly, increasing both the scale and penetration of these formats and continue to serve our customers safely in times they needed us the most. As the government announced nationwide lockdown we enabled work from home for the entire organization including our front-line restaurant staff. This ensured that close to 10,000 young people of the country remained gainfully engaged through the lockdown while getting an opportunity to upgrade and upskill. The crisis in a sense tested the activity, resilience and versatility of our business model. We entered this crisis with a strong balance sheet and a solid business foundation. But the situation gave us yet another opportunity to revisit our cost of service across the board and sharpen our focus on our operations, something that will give us added fire power to navigate this challenge and emerge stronger.

Moving to Slide #8 and getting into details of our financial results; we are pleased to report that we have concluded a good year and registered a strong topline growth of 10.4% for FY20 with our recurring PAT surging by 71.9% year-on-year. In fact FY20 has been one of the most solid years for us with strong sales and cash flows. Even before the COVID19 pandemic hit the world FY20 was marked with challenges, the consumer sentiment was tepid and the economic environment was volatile. But we had conviction in our strategy focused on value, customer experience and financial discipline that helped us deliver robust results quarter after quarter.

Despite the macroeconomic challenges we were able to build momentum across all our performing parameters in FY20. Through the year we saw our revenues, profits and margins grow. We marked the 18th consecutive quarter of same-store sales growth followed by January and February registering a high SSSG of 12.3%. This provided us the foundation for maximizing operational efficiencies. As a result both our EBITDA and operating EBITDA jumped more than 150 basis points for year to date February, 2020.

But COVID and lockdown had a significant impact on the business in the last month of the year as you can see on Slide #10. If we were to exclude the impact of March, 2020 you will see that the sustained SSG over the last 5 years, we have been able to increase average sales per restaurant by more than 62%. Consequently, our operational profitability has also shown significant jump.

Coming to Slide #14, our performance was pivoted by three pillars of our strategy. These pillars provided us the strength and the foundation to navigate COVID19 led challenges as well.

Running safe and hygienic restaurants that our customers see as a benchmark helped us reinforce trust and permissibility for the brand.

We were also able to leverage the width and depth of our delivery network to maintain business continuity even in the toughest time. We have a diversified portfolio of restaurant location distributed across high street, standalone, drive-thrus and malls. We are also probably the only QSR to have long-term leases and sales linked rental agreements. This proved to be yet another competitive advantage and helped us conserve cash.

Moving onto key highlights of Q4, we entered Q4FY2020 on a strong note with a focus of strengthening our value platform across day parts and furthering McDonald's as one for all and all for one destination that has compelling offering for customer segments and occasions, including snacks, coffee, dinner, dessert and breakfast. McDelivery, McCafé and McBreakfast have been key levers to bring this vision alive and we continue to leverage them to create brand relevance, get more customers into the McDonald's fold and widen our customer base.

McDelivery has emerged as a delivery destination of choice with sales increasing over 6 times in the last 4 years. This quarter we further innovated to launch 'contactless delivery service' that was the need of the hour. This ensured that amidst COVID19 concerns, customers were able to get their favorite McDonald's food that was prepared without being touched by bare hands and delivered with all adequate social distancing measures. It is becoming increasingly apparent that convenience channels such as delivery take out and drive-thru will be the biggest driver of business in the foreseeable future. With over 264 delivery hubs, strong strategic relations with 3POs, along with a portfolio of over 70 drive thrus, we are extremely well-positioned to cater to this exploding demand.

Another feature in our hat is our in-house coffee chain McCafé that is growing exponentially both in terms of its footprint and revenues. This quarter we added five new McCafés taking the total number of McCafés to 223. After celebrating McCafé's landmark of serving 10 million cups of coffee this quarter we leveraged our handcrafted with love campaign to showcase our coffee mastery.

We have also been investing significantly in technology to deliver convenience and value to our customers. Our McDonald's app that was launched in last January now has over 3 million downloads. Access to this kind of customer base gives us a strong competitive advantage in the new digital phase that our industry will operate in. In the coming quarters we are leveraging our technology backbone to provide services like 'on the go' and 'take out' to offer more channels and hence more convenience to our customers.

Moving to Slide #23; this quarter we added four new restaurants taking the total number of restaurant across the system to 319 with 90% of them being modern and contemporary in design. Five more stores were ready but could not be opened due to the lockdown which we will open on priority once normalcy resumes. If we take these five unopened stores in consideration, we would have added 29 stores in the year FY20, much in line with our guidance.

Moving to Slide #26; our people have always been our biggest strength and this quarter especially we saw them come forward to keep the McDonald's flag flying high. Our army of heroes made sure that our customers got safe and hygienic food through this tough time. But that's not all. They also helped serve over 56,000 meals to front-line warriors and to sections of the community badly hit by the pandemic, including daily wage earners and slum dwellers.

I now request Pankaj to take you through the financial highlights of FY20 and Q4FY20.

Pankaj Roongta: Thank you Smita. Good morning ladies and gentlemen. First, I hope all of you and your families are keeping safe and in good health.

I'm pleased to share our financial results for FY20; the company continued its growth journey of positive SSSG of the past 18 quarters all the way up to February of this year, resulting into a strong financial performance for the year. In fact FY20 has been a very good year with robust sales growth and a strong growth in recurring PAT.

Moving to Slide #29; similar to previous quarters of this financial year, we will be discussing the comparable numbers with you, which excludes the adjustments arising out of IND AS 116. A reconciliation of the same you can find in Slide #29.

Our top line numbers registered a robust growth of 10.4% for the year. This translated into 18.5% CAGR growth over 3 years. In Jan and Feb SSSG was very strong at 12.3% as stated by Smita, with a year-on-year sales growth of 20.3%. However, due to sudden national lockdown triggered by COVID19 we ended with -6.9% SSSG growth for the quarter causing significant disruption. Despite a tough Q4, our full year top line growth was driven by a continued focus on delivering value, menu innovations, building occasions, increasing brand accessibility through digital and delivery and enhancing focus on hygiene and food safety. The growth was aided by our diversified real estate portfolio and omni channel approach.

I'm also very happy to share that we were the first company in the QSR segment to launch contactless delivery that helped us immensely to tide over these challenging times thereby also ensuring delivering growth in a very 'responsible way'.

Coming to Slide #31 on gross margins. Our consistently increasing volumes, improvement in operating efficiencies helped in improving our gross margins. Our constant menu innovations and McCafe has consistently helped us in creating more occasions for customer visits. All of these along with judicious cost optimization have helped us improve our gross margins by a significant 450 basis points over the last 3 years and for the year gross margin improved by 171 basis points to 65.2%. For the quarter, it was even higher at 208 basis points improvement to deliver 65.6% gross margin.

Coming to restaurant operating margin on Slide #32. So along with gross margin improvement and operating cost efficiency, it led to an overall expansion of 360 basis points in restaurant operating margin over the last 3 years., For the year under discussion, our restaurant operating margin landed at a robust 14.6%, an increase of 20 basis points despite a very tough Q4. For the quarter therefore, ROM landed at 10.8% of the sales driven by the adverse impact of the lockdown implemented in March. I would like to highlight that in Jan and Feb ROM was going strong at 15.4%.

Coming to operating EBITDA. Coupled with the ROM improvement and the efficiencies in management of fixed costs it resulted in operating EBITDA of 9.3% of sales, which translates to an increase of 15.8%, higher than sales growth also and representing an increase of 44 basis points year-on-year. Overall, the operating EBITDA expanded by 400 basis points over the last 3 years and our attempt is to move ahead in the same direction. Similar to ROM trend for the quarter, although Jan and Feb operating EBITDA was going strong at 10%, however, due to adverse impact of COVID the margin dropped to 5.5% during Q4.

Coming to Slide #34 on profit before tax. Our profit before tax stood strong at Rs 494 million at 3.2% of sales, representing a strong growth of over 40%. Overall PBT has witnessed 450 basis points increase over the last 3 years on the back of robust sales growth and our operating efficiencies.

All of this resulted into a very strong recurring profit after tax increasing by 71.9% YoY to Rs 366 million during FY20 at 2.4% of sales, which represents an 85 basis points increase over last year. In fact, our trajectory was so strong that in nine-month year-to-date until December'19 the company had delivered full profit of FY19. Overall, our PAT margins have expanded by 366 basis points in last 3 years. Our Q4 recurring PAT impacted by lockdown was a loss of Rs 51 million at -1.5% of sales due to significant impact on sales and P&L for the quarter.

I would also like to highlight that the company has recorded an exceptional item of Rs 166 million towards inventory provision in Q4 of FY20, which was necessary due to impact of COVID19 on sales and inventory provisions.

Coming to cash profits after tax on Slide #36. I'm also happy to announce that our recurring cash profits after tax stood at Rs 129 crores (1299 million), +19.8% growth over the last year representing an improvement of 66 basis points over last year. So our cash profits after tax also grew faster than sales growth and overall the cash profits have doubled in last 3 years.

To summarize, the company has delivered a strong financial performance despite a tough Q4 impacted by COVID19. However, resilient competitive operating advantage, operating efficiencies resulted in strong EBITDA growth and recurring profit after tax for the year. As an outlook for FY21 our focus is on survival during lockdown and revival as normalcy restores wherein cash conservation, optimizing operating cost, targeting a healthy balance sheet remains our number one priority. We also believe that with our heightened focused on providing assurance and convenience to our customers while keeping a strong control on our costs will help us emerge stronger and bounced back swiftly.

With that said I will now hand it over back to Smita, who would take you through our survival and revival strategy ahead. Thank you so much.

Smita Jatia: Thank you Pankaj. While COVID19 led uncertainties will persist for some quarters, we continue to closely watch the evolving situation and respond with the customer first approach. At the same time, we are constantly taking learnings from other global markets that are closer to the cycle of recovery and studying consumer behavior to realign strategies for the new normal. Our immediate priority for the business is focused on survival and ensuring a strong and quick revival. Maharashtra, Tamil Nadu, Andhra Pradesh, Telangana and Gujarat that have more than 75% of our total stores are amongst the worst hit states by COVID19 and yet we have been able to ensure business continuity by activating our convenience channels. What gives us a big competitive advantage is that we are one of the few players to have a significant portfolio of drive-thrus and take outs, apart from delivery, as a part of our convenience channel.

We have also launched an innovative 'on the go' service that enables enhanced convenience and assurance for our customer. Aggregating the same we will have (+) 1000 touch points with all our customers. In the last couple of months, you have seen these channels perform phenomenally well. For example, last month business from drive-thru channel alone in our store in Bharuch was the same as from its dine-in channel a year before. Another example is a store in Hyderabad, which has been breaking its own record for these convenience channels even in this tough time.

We had predicted that the pandemic will lead to a huge movement of customers from unorganized to organized food chains as safety and hygiene will take precedence over all factors. These trends validate our hypothesis and give us confidence that as we start opening our stores we will be propelled by a strong portfolio of delivery hubs, drive-thrus and take out hubs and will recover faster than many others. In the coming quarters customer assurance, convenience will be the key focus areas. We have already implemented a 42 pointer checklist across our operations to ensure our customers and employees feel safe every step of the way.

From a CAPEX perspective, we will be re-evaluating our investments but will continue to re-image restaurants and continuously expand our EOTF footprint. We are confident that our diversified real estate portfolio, globally known high standards of hygiene and safety, good food journey and high brand affinity will prove to be significant strength for us. With increased focus on hygiene and affordability, we will see IEO market move towards branded players with high trust calls. So in the new normal even as the market size may shrink we see a huge opportunity to increase our market share. I will now hand it over to Amit for his closing comments.

Amit Jatia: Thank you Smita. In terms of our belief, we believe we have the foundation to lead a quick recovery in these unprecedented times. With a strong balance sheet, focus on driving further efficiencies in our cost structure, diversified long term real estate portfolio and an omni channel approach, along with a very high customer focus, we have all the right ingredients in place to get back over previous growth trajectory as soon as the situation moves from panic to caution to the new normal.

I believe our growth will be led by our strong convenience platform of delivery, takeaway, drive-thru which contributed to about 50% of sales even pre-COVID. We have quickly redeployed resources to strengthen our digital platform along with the launch of our new updated delivery app. I feel confident that we will restart our journey to pre-COVID level growth from the second half of the year.

Finally while we are not immune to the immediate pressures of this crisis, we entered the situation better positioned than most. We will continue to make bold moves to consolidate our leadership, set new benchmarks for the industry and emerge stronger from this challenge. With this, I now open up for question and answer.

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

Avi Mehta: I want to kind of just revisit your comment that you expect pre-COVID growth rates to commence from second half, kind of just passing through this further, how is the early trend on stores where dine-out has commenced; how has the recovery been in terms of percentage of pre-COVID or how is the ROM then, some clarity on that would be useful to kind of help us understand your thoughts and if you could clarify on that part as well on why you expect such a V shape recovery?

Amit Jatia: Avi I will just clarify, I said that we will restart our journey to pre-COVID level growth rates from the second half of the year. Obviously, there is too much uncertainty for us to be able to tell you with confidence that we may get there. But we believe that the convenience channels we have and particularly as we realized through this process the 1000+ touch points that we have including the strength of drive-thru is really being tested and giving us substantial results. So we feel that the once the new normal sets in, and I'm using this from our experiences in other global markets as well what we are able to see is people move to trusted brands and particularly Western fast food and we feel with the kind of diversified real estate, the convenience channels we have, we feel that we should be able to start our journey much faster than others. So that is really the crux of what I meant.

Avi Mehta: But if you could then share what the recovery levels have been in the stores that you started or is it too early to comment on that?

Amit Jatia: No, that's all part of next quarter, so it is hard for me to give you any data without making a forward-looking. The important thing I can tell you is that we are seeing very good results out of our delivery obviously. But takeaway and drive-thrus particularly are yielding good results, I mean for the first time we really shared that we have 70 drive-thrus which is not a small number and particularly takeaway is very-very important. Along with takeaway be launched 'on the go' as well so you can order ahead and we will come and deliver it outside. So, that is what really it's all about. But I cannot tell you where we are heading but every week we are seeing growth in sales.

Avi Mehta: Amit, you said that you will continue investment in reimaging and also you highlighted that you have a very large portfolio, would you be able to share what is the kind of variable cost structure that we have or how do we look at it in this environment where a decent number of months have been lost because of the lockdown. How should we look at margins if you could help us pass through that?

Amit Jatia: The problem Avi is that of course what we have done is we've looked at every single cost and the whole thought process has been that 'okay while the business should work on 20% lower sales and make the same amount of money. So we focused very hard on our fixed cost. We are relooking at the supply chain in totality, we are looking at the portfolio of the 320 restaurants also very-very seriously and that is sort of the best I can give you at this point in time. I feel that FY21 is a tough one but FY22 we are hoping to sort of catch up and get back to the previous growth levels at least in the following year. In terms of margins, it is very hard for me to say anything because every day we hear rumors that another shutdown is coming. So I feel that the best I can tell you I repeat is that we are trying to ensure that if sales are 20% lower in the new normal, so how can we still make the same amount of money that we made earlier at the minimum and the crux is fixed cost. We've looked at every single item, we've made lot of efficiencies already plus we are working with our landlords that's the other big thing and we are relooking at supply chain.

Avi Mehta: Given the situation, on royalty rate, would there be a discussion over there or how should we look at that?

Amit Jatia: No that is 4% is a very-very good royalty rate and we prefer to work on positive sort movement forward things and there has been a bit of deferment in payments support but at this point in time that's not really the focus. Our fixed cost is really the big focus.

Moderator: The next question is from the line of Abneesh Roy from Edelweiss.

Abneesh Roy: My first question is on the CAPEX and expansion, five stores are ready you said, so when do you see that expansion coming? 10% of the stores are not in the modern format, so will that be now shelved until normalcy comes in terms of growth coming back next year?

Amit Jatia: So the stores, once the whole lockdown is completely over is when we should open because there is no point in starting the restaurant and having a rent issue then with the landlord, as sometimes there are messages that it will lockdown again, sometimes it is not. So, I feel that it will be in the second half of the year that is point number one. Point number two, 90% modern as per a McDonald's definition is a phenomenal platform already but as Smita and I was talking about in our comments that we will continue with our reimaging and our expansion of EOTF stores. What we found through this COVID and this reopening is that because in EOTF we have those self ordering kiosks that are very efficient, it allows us to make the restaurant contactless even in store and therefore we want to accelerate that and we believe we do have the capability to do that. But I will be able to give more color in the next call after our first quarter results.

Abneesh Roy: My next question is on McDelivery; you have done a commendable job of 6x in 4 years, now 2-3 questions here are, one is 260 delivery hubs, total 319 stores so do you see whenever these stores open, which are still not having McDelivery, would you start that delivery? Second is unlike pizza which is a warm product which is a hot product, the perception and the reality is burger becomes soft and burger base becomes cold by the time it gets consumed, you can definitely work on the insulation bit etc. so how do you proactively remove this perception and go the next level in terms of delivery? Contactless etc. great initiative but I think that everyone is now doing, so that is no more a differentiator, you might have done it first, but now that everyone is doing it. So how do you take McDelivery to a number which is close to somewhere in between pizza and current number what you have, you can't reach the 65% number of the pizza chain but how do you take it to the next level?

Amit Jatia: For us it's not just about delivery, you are underestimating the value of drive-thrus and take away. There are restaurants where our takeaway volume is more than the average store volume of the market and we have built a two window system, so if you have seen our restaurant in Colaba and many-many other restaurants you will see that sometimes if the store is on the first floor, then there is a takeaway window on the ground floor and we have something called a transporter that brings product directly from the kitchen down. So the amount of infrastructure we've built with technology we feel takeaway is an amazing-amazing opportunity especially with the high footfalls that McDonalds have always had. So coming to your first question, the 264 to 320 remember we have a lot of restaurants on highways; there are many restaurants that are in food courts, so sometimes it doesn't make sense to have them do the delivery because we may already be penetrated in the market through another store that covers that delivery area. So selectively as soon as possible, we keep expanding that. So will the 264 go to maybe 320? No. But will it go to maybe 280-290? Yes. So that is a continuous effort. Secondly when it comes to delivery, delivery whether it's burgers, pizzas paratha or anything delivery is a convenience driver. It's not really about hot or cold food and there is a jury still out there that even pizzas in the global markets at least when I hear there are many sort of pizza players who believe that they should or they should not do delivery while as far as burgers are concerned I can tell you from a McDonald's experience that our delivery business globally is in billions of dollars. So we feel confident that that is not a barrier and the convenience is a key driver and therefore the kind of growth that we have seen of 70%, 50% clearly confirms our view. So, I hope this gives you a perspective on the question you have.

Abneesh Roy: That was helpful. I had one question on the product portfolio; recently you had come out with the Rs. 59 McSaver that's an excellent pricing in my view. So what is the thought process here and second does it dilute your gross margins?

Amit Jatia: No, in fact we have had this Rs. 59 price point for a long time. It started April 2019 and you have seen that our gross margins are only gone up, so we have our own methodology on how we manage our product mix to ensure that when we launch value platforms, one they have to be sustainable. We look at their margin profile over 2 to 3 years horizon, we will not launch something where we don't have the confidence that we can stay the course because we want to give the consumer everyday value in their thinking and we don't want to change that because that has tremendous value from a consumer point of view. I don't see that as an issue with margins at this point in time and this has been around for a while and we intend to keep that for the consumer, even through this process through this time.

Abneesh Roy: You see commentary of many sectors; they say that work from home is something, which is not just a temporary thing. If you see IT companies' they are saying 90% workforce will eventually work from home in even longer term and across sectors this number can vary. So how does it impact your McCafe and Breakfast because I think these will be normally more from the offices and second is if you see ice cream sales for ice cream companies have collapsed. So for your cold product, cold beverages what can be the near term challenge because again same issue of ice cream can be there, people don't want to fall ill, so they will not consume cold product that much.

Amit Jatia: No, we have enough of a play between hot and cold beverages and all these things we have seen it over 25 years even during SARS. So I am sorry but that last part I feel at least doesn't worry us at this point in time. The other thing is when it comes to McCafé and Breakfast, we have diversified portfolio that services across different generators and when I say generators, its home, work, education etc. In fact we have been one brand that is not skewed towards IT park because we believe in multiple generators and not being fixed to one generator, so actually we are the most I would say widespread multi-focused brand that is not dependent on any one type of generator for our business. Last point I want to make is finally we have 230 McCafés, let's say we may have 20 stores that are link towards offices but we have a whole bunch of stores that are diversified in the generators. So I don't see there is a problem pretty much at this point in time.

Moderator: The next question is from the line of Aditya Gupta from Goldman Sachs.

Aditya Gupta: First, little clarification, can you mention delivery, drive-thru and takeaway contribute to around 50% of sales and is it for thefull year?

Amit Jatia: Yeah that is a fact.

Aditya Gupta: And is that for fourth quarter or is that for the whole of fiscal '20?

Amit Jatia: As I said its pre-COVID.

Aditya Gupta: And second is my call dropped in between so I don't know if you have answered this. How is the performance been so far in April, May on delivery wherever you have been able to start operations?

Amit Jatia: We can't share that data because that is a different quarter and that's forward-looking. But I can tell day on day, week-on-week sales have been getting better as consumers are moving from panic to caution and we feel the next phase is new normal and when the new normal comes in, we feel that Western QSRs have an advantage, especially given that the brand trust codes are high and with all our convenience channels, we feel we are in a good position to address that.

Moderator: The next question is from the line of Arnab Mitra from Credit Suisse.

Arnab Mitra: My first question was on the post-COVID situation, so in smaller towns where the fear is possibly much lower than in Mumbai or a bigger city. Are you seeing a direct correlation between what kind of recovery patterns you see in the smaller towns versus the bigger centers and is it like a substantial difference that you see in the ramp up there?

Amit Jatia: Yes, actually small towns are doing quite well and from their volume point of view they are doing far better than what they used to do.

Arnab Mitra: Because delivery now becomes a very important component and you rely a lot on the aggregators for that. Any change you are seeing there in terms of their ability, their network size, delivery times versus what it was pre-COVID times and any thoughts on that?

Amit Jatia: No, in fact it's been phenomenal because we have worked always on a partnership approach and never taken short-term views. There they find us as valuable as we find them, so this partnership is what is got us through the last 3 months and we continue to do very innovative stuff, you will see that play out quarter-on-quarter. The good news is that because of drive-thru and takeaway along with delivery; we talked about the 1000 channels that the consumers can use us at, we feel that we are quite balanced and all these three will continue to play a significant role and you will see us lead along with 'on the go' business as well.

Arnab Mitra: My last question is from my side, on takeaways, so just trying to understand what kind of consumers the requirement does takeaway serves. I mean in the Western world its basically you get down in a subway, 'on the go' you pick up something but in the Indian context is it largely to do with retail spaces or you are in a mall and you take away. Why I am asking this question is, is it possible that takeaway actually recovers as slowly as dine-in because people are not really out shopping like they used to do?

Amit Jatia: I don't agree, in fact a lot of people have been dying to get outside food and because our take away is also contactless and is as quick as you would do in-store ordering at McDonald's, it's a global strength that we have with two windows in most cases. We think that in many cases we have seen that take away is very nicely substituting the in-store business and between take away and delivery and drive-thru; in many instances we have seen sales pretty much at the old levels.

Moderator: The next question is from the line of Tejas Gutka from Tata Asset Management.

Tejas Gutka: I seek your comments on three areas largely; first is that despite the 12% strong SSSG that we had seen in the first 2 months of the quarter, the restaurants operating margin was lowered compared to the last 2 quarters and I'm talking about sequentially. If you could throw some light as to what led to this? Second was on rentals, are you in the process of re-negotiating them or moving to a revenue share model? In fact if you could help us if the current rent is fixed or a mix of minimum guarantee plus revenue share and the third is that in light of these COVID related disruptions what happens to the 2024-25 targets that we had talked about earlier?

Amit Jatia: So in terms of SSSG, if you look at our presentation and you look at Slide #33 where we share the breakup of Slide #32 actually I'm going to that slide. You will see that actually speaking our quarterly restaurant operating margin was running very strong. It was running at 15.4%, if you just take January and February, but if you add March to it then the drop is pretty significant because lot of the fixed cost—G&A is after—but a lot of the fixed cost at the restaurant level, whether it's utilities, rent etc, because March we were running pretty much the whole month, so the rental relief if at all we have got is about 10 days. So I feel this is not the right way to look at it, I feel the important thing is that our trajectory as much as up to February was very-very strong and we were quite hopeful that we would finish the year as strong as Quarter 3 and I will come back to that if you still have more questions on that. But moving to your second question; so the good news is that as we built a very strong real estate platform, most of the malls (+) 90%, we have a straight revenue fair deal and we always take an approach of partnership with our malls. So even though these 3 months have been very difficult, finally it's a 20-year relationship because we have 20-year deals and finally the end is not there yet. We believe that once we are through all this, even if it is 18 months finally we have to work with them as partners. So the good news is that they have been very-very accommodative at least to us. The second good thing is that because we had only straight revenue share obviously that became easier for us to work with our landlords particularly in malls. On high street locations we do have minimum guarantees and revenue share or only minimum guarantees. There again we work very closely with landlords and we've worked not only to try and get support for the 3 months where the restaurants have been closed but we are working with them to work with us and help us through at least this year so that things work out for both of us so it's all still work in progress. Now coming to the year '24-25, basically our vision 2022 still holds. Obviously the number of stores might become a challenge because to catch up on-store openings is always very difficult, especially if you uphold the standards we have used on long-term deal structures, rent increases every 5 years, state percentage of stale deals in most mall locations. So we will come back to you with more clarity around that in the second half of the year but the endeavor is to at least try and get margins moving to that number as quickly as we can with the cost structure, reduction that I talked about in the previous question. So I hope this answers your three questions.

Tejas Gutka: Sure, just a small clarification on the first one. What I meant was that your Jan-Feb restaurant operating margin is 15.4% was lower than what we saw in Q3, which was 17.5 and in Q2, which was 15.9 and both these quarters had a lower SSG compared to these 2 months.

Amit Jatia: So it's important to note that February has a couple of days less in the month and that impacts that, you got to March is 31 days, February is normally 28 so that has a role to play. So the Jan-Feb you cannot take as for the whole quarter. Secondly, to the way you compare in our business it is seasonal, so you have to look at Quarter 4 to Quarter 4, Quarter 3 to Quarter 3 and Quarter 2 to Quarter 2 because each quarter has a different cost structure and different sales impact. I have said that earlier as well so it's not new to that extent.

Moderator: We will move onto the next question that is from the line of Jatin Chawla from First Voyager.

Jatin Chawla: You spoke about rental cost; the other large fixed cost in the business tends to be employee cost, any effort you are taking to kind of variables?

Amit Jatia: In the employee thing the good thing about us is that we have a very large pool of part-time workers and the whole purpose of keeping part-time is so that we are able to manage our businesses where which is strong on lunch and dinner while there are certain day-parts there where logically you don't eat that much. So, that is helping us in manage our employee cost quite nicely. Obviously, we give a minimum of four hours and a maximum of eight hours and I think over 60% of our employees are part-time that gives us unbelievable flexibility. So, that is how we are managing it in a win-win both for employees and for us.

Moderator: We will move onto the next question that is from the line of Pritesh Chheda from Lucky Investment Managers.

Pritesh Chheda: One clarification, you mentioned a certain number on drive-thru, delivery and takeaway as a percentage of sales. Actually I missed that number, what is it?

Amit Jatia: That's about 50% of sales.

Pritesh Chheda: And second clarification you mentioned somewhere that you are trying to achieve a similar profitability at a 20% lower sales as well. I was just doing a basic math, at 20% lower sales you tend to actually break-even. So if you would help us connect the dot as to what efforts are you putting in to achieve the target that you have set at 20% lower sales and similar EBITDA or I am missing something in this?

Amit Jatia: That's firstly an attempt; we are working on the three things I talked about. One is we are looking at the real estate portfolio very carefully and essentially, we are looking at all the store that are slight laggards and what can we do to deal with that. The second thing we are looking at is all fixed cost including corporate G&A, which is a very-very big focus for us to see what efficiencies we can bring in there and the third thing is we are reimagining supply chain, assuming we are starting from ground zero. Also, remember commodity prices have come off quite nicely and we are looking at what advantages we can take with that as well. So that's the endeavor, I think we will be able to tell you a bit more in the coming quarters. But the whole idea is we are imagining for FY21 specifically, we are imagining that sales are going to be lower, obviously, we pretty much lost the first quarter, so how do we still try and achieve, not for this year, but progressively how do we bring the cost structure down so that at even with 20% lower sales that I talked about, we at least maintain our profitability as a percentage, that's really what I meant and those are the three initiatives that I talked about.

Pritesh Chheda: In today's cost structure at what lower sales do you actually break even?

Amit Jatia: No, we don't share all that but I feel is redundant because today's cost structure does not exist. It's a new cost structure already.

Pritesh Chheda: Lastly on the three parts which is takeaway, drive-thru and delivery sales. Have you mentioned that those three parts, which is 50% of sales is actually at the pre-COVID levels or actually it's growing?

Amit Jatia: Yeah, I mentioned it's at pre-COVID levels and it's obviously meant to grow.

Pritesh Chheda: Is it at specific stores or it's at the company level?

Amit Jatia: I told you company level, pre-COVID company level that was the number and I am expecting it to grow as things settle down.

Moderator: The next question is from the line of Sabyasachi Mukerji from Centrum PMS.

Sabyasachi Mukerji: Clarification on the part-time staffs, part-time workers; are those are on your payroll, are they on your payroll?

Amit Jatia: Yes all are on our payroll.

Sabyasachi Mukerji: Are we doing any kind of restructuring, flexi pay or hourly base incentives, our peers have done that's why I am asking.

Amit Jatia: No we don't do that, we have incentives on performance and store SOPs and all that but we don't do variable to that extent.

Sabyasachi Mukerji: Last time when we spoke on the business update you gave in the March end I think, you mentioned that you are trying to convert the mall stores to delivery hubs. Has that thing worked out or the mall stores still remain shut?

Amit Jatia: Because malls have been shut, it didn't bother us because we have a very strong real estate portfolio around retail locations. So for example in Mumbai we have 100 locations and malls might be 20-30, so we are very well penetrated and our two stores have covered the whole city, remember traffics also down because every restaurant that we opened, we wanted to maximize the throughput, so our operations team have managed it quite well.

Sabyasachi Mukerji: So basically for every store your reach has increased?

Amit Jatia: Correct.

Sabyasachi Mukerji: Last question on the aggregator side, any change in commission rates you are seeing over there, these days?

Amit Jatia: No.

Sabyasachi Mukerji: One last question on the stores, you said that you will have a hard look on your real estate portfolio and probably look at the laggards. Are we looking at any store closures this year?

Amit Jatia: That's hard to say at this point in time. We are still working through the details but in many cases we are looking at sales that we were doing earlier, the rental structure so I think by the next call I might have little more information on that.

Moderator: The next question is from the line of Latika Chopra from JP Morgan.

Latika Chopra: My first question was around clearly there is lot of talk of a long tail of restaurants, incrementally going to find it tough to survive this crisis. From a promotional or pricing perspective do you think—I understand you are of value platform—but would you anticipate that the promotion intensity in the industry will be lower and might sustain lower for a while as we emerge out of this crisis?

Amit Jatia: We are hearing there are lots of brands have moved out of value for money but we will continue with our value for money platform but let me have Smita respond to that.

Smita Jatia: We have always maintained our value platforms whether it's the McSavers at 59-69 and these are going to continue because these are our long-term value bundles to our customers. Yes, we are hearing that lot of players have taken away discounts because currently assurance and availability are bigger drivers however, we don't see any change in our value for money strategy.

Latika Chopra: My second question was Amazon entered delivery, they are trying it out at same sale stores in Bangalore, have you partnered with them yet and do you anticipate any material shift in the landscape in case Amazon decides to scale this up meaningfully?

Amit Jatia: We have been able to develop very strong positive partnerships with all the players and similarly they find value in what we have to bring to the table. So, we will continue our conversation with all such players including Amazon and I'm sure we are in conversation and it's too early to say there will be any changes. But, they will be a significant player and we feel it's good for all, it keeps a balance.

Latika Chopra: Yes that's true. I think it can help bring down the take rate for the industry.

Amit Jatia: Exactly.

Latika Chopra: My last bit was on was related to the fact that now we have a franchise in place for North and East and we understood because of various disruptions, probably the brand equity suffered in that part of the country. Just wanted to understand between both of you, how do you manage - are there common expenses, ways to leverage and improve McDonald brand equity? How do you do your dealings with the parent in this regard anything incremental?

Amit Jatia: Some things have changed; remember we have been around for 25 years and there was a franchisee in the past as well. So we have got good methodologies of working together and McDonald's also is a very big franchisor or company that understands how to work. So far it's all been very positive and it's coming along well, cannot get into specific details but yes we were already leveraging our individual supply chain volumes with our big suppliers and that effort continues on moving forward.

Moderator: Ladies and gentlemen due to time constraint we will be taking our last question that is from the line of Sankarshan Mehra from Premji Invest.

Sankarshan Mehra: Just one clarification, so this 208 bps gross margin improvement in the fourth quarter, which is actually better than the full year number, despite the disruption. Could you please pass out where this improvement is coming from?

Amit Jatia: We don't say break-ups but essentially, primarily it's been around pro-mix and sometimes if we have done well through the year on volumes we get some benefits there as well, but primarily it's got to do with sort of the three levers we have, which is raw pricing, product mix and menu prices but is primarily product mix and some benefits on raw pricing.

Sankarshan Mehra: Does the change in the mix from in dine-in versus delivery, does that have a role to play here as well?

Amit Jatia: No that does not, maybe a small role but you see I have been maintaining even in my past calls that as McCafé sales are growing, as we have been doing a lot of work around product mix, recently we had introduced a wheat bun which consumers really loved and they were paying a bit more for that. All these things help us with our gross margin, so it's a culmination, you see it's a building block; it's not one event that you can take as a quarter. It's the work, that has happened over 5 years that culminates to growth. So that's one area where I think we have been able to do a decent job while keeping the value platform.

Moderator: Thank you. Ladies and gentlemen that was the last question. I now hand the conference Mr. Amit Jatia for his closing comments.

Amit Jatia: So I really want to thank you all for joining the call today and for patiently listening to our presentation. If you have any more questions please do reach out to Devanshi. Thank you and have a lovely day.

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