Q4 FY2017 Earnings Call Transcript – May 12, 2017

Corporate Participants

- Amit Jatia – Vice Chairman
- Smita Jatia – Director
- Suresh Lakshminarayanan – Chief Financial Officer
- Ankit Arora – Senior Manager, Investor Relations

Moderator Good day ladies and gentlemen, good day and welcome to the Westlife Development Limited Q4 FY17 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 now hand the conference over to Mr. Ankit Arora – Senior Manager, Investor Relations. Thank you and over to you, sir.

Ankit Arora Thanks, Margret. Welcome everyone, and thank you for joining us on Westlife Development Limited earnings conference call for the fourth quarter and fiscal year ended March 31st, 2017. We are joined here today by Amit Jatia – Vice Chairman, Smita Jatia – Director and Suresh Lakshminarayanan – Chief Financial Officer of Westlife Development Limited.

Please note that results, press release and investor presentation had been mailed across to you earlier, and these are also 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 the 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 Q&A session.

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 risks and uncertainties we face. A detailed statement and explanation of these risks is available in this quarter's press release and 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.

Amit Jatia Thank you, Ankit and good morning everybody. Thank you so much for joining us on the call today. FY 2017 has been another foundational year for the company, re-setting the base for growth for brand McDonald's in India. We have made excellent progress on key strategic levers even as the economy remains challenging through the year and consumer sentiment volatile.

FY 2017 saw a significant impact of demonetization leading to disruption in consumer spending and sentiment. Our strategic pillars that primarily included broadening our accessibility through new stores and growing sales through our new menu and brand extensions have helped us mitigate this quite well.

Throughout the year, we focused on driving menu innovation and creating value for the consumer rather than relying on myopic initiatives led by promotions and discounts. This has helped us clocked positive comparable sales of 4% for FY 2017.

We are happy to see the footprint of brand McDonald's McCafé grow to 111 with 36 new McCafé's added by the end of March. It is also heartening to see that the average McCafé sales per restaurant has risen considerably without any above the line advertising indicating a strong consumer connect.

McDelivery has been another spring board platform for us. It has delivered around 25% growth through the year. The new McDelivery app was launched in December 2016 and is gaining traction month-on-month leading to strong double-digit growth in delivery sales for the year.

FY 2017 saw an expansion of the Breakfast Menu that included choices like the Dosa Masala Brioche, the Masala Scrambled Eggs, etc., making our menu more relevant to Indian palate. These products have been well received by our patrons and have clearly established McDonald's leadership in the approximately $2 billion outside of home breakfast market.

New stores have performed remarkably well under the Restaurant Operating Platform 2.0 that was launched in the last quarter of FY 2016. The bunch of new stores that were opened under ROP 2.0 yielded substantial cost efficiencies and contributed positively to cash flows for the fiscal year. We believe this will continue as we build more stores under this platform. We are now taking our learning's from this platform and implementing them in older stores to help us improve our overall restaurant operating margin.

We have been able to rationalize food and paper cost considerably and this has contributed towards a continuous improvement in gross margin. Other levers like menu and the marginal price hikes have aided improvement in gross margin on a year-on-year basis.

The key challenge in FY 2017 quarter four was the sudden and retrospective increase in minimum wages by 25% plus in Karnataka which hurt payroll and employee costs for the quarter. As demonstrated in the past, we will fundamentally keep improving employee productivity to overcome this rise over the next few quarters.

Despite these external non-negotiable challenges, the cash flows increased by about 28% in FY 2017. Brand McDonald's is in accelerated growth phase and I am confident that the foundation we have built will spur the company to achieve greater targets and create new benchmarks.

Clearly, the progress made year-on-year stands out within the industry which is facing many challenges at the moment. Our long-term vision and a very dogged consumer focus will help us in retaining our Burger leadership position.

Let me now hand over to Smita to take you through the year and the quarter highlights.

Smita Jatia Thank you, Amit and good morning, everybody. Please could we move to slide 5 which states the highlights for the financial year.

Total sales for FY 2017 stands at INR 9.3 billion which is 11.6% growth Y-o-Y. Same stores sales for the year at 4% and for the quarter at 1%. This is over the base of a very strong 8.4% comparable sales in the same quarter previous year.

In addition to this, we had a negative impact of extra trading day on 29th February last year. So, like-to-like we would be 2% comparable sales for the quarter. Gross margins improved by 60 basis points and cash profit by 28%.

As seen in the trend year-on-year on total sales growth, we are increasing total sales growth year-on-year. As per the Euromonitor, IEO was expected to grow at 5.3% for FY 2017 and hence, in the year we have grown at a double rate grabbing market share.

Our total restaurant count stands at 258 with gross additions of 25 stores. Our focus is to open profitable restaurants in the right trading area while we continue dominance in the six key cities of Mumbai, Pune, Ahmedabad, Bengaluru, Chennai, Telangana.

Moving on to some factors contributing to this growth, on the McCafé side we stand at 111 McCafé at a 45% penetration, making us the number 2 player in the coffee market. Average McCafé sales per store grew by 30% and total McCafé sales by 2.25 times in the last 12 months.

Moving on to McDelivery, we upgraded the mobile app with more functionalities and a better user interface. Today, we stand at 148 delivery hubs with a total sales growth of 25% in FY17.

To give our customers news and variety, we had few product introductions like the Mini Mac, Loaded Fries as well as limited time offers.

Now, going into operational profitability, gross margins grew by 60 basis points due to product mix play through menu interventions and increases McCafé sales. The ROP 2.0 platform as designed also contributed to profitability. The baskets of new stores contributed positively to the cash flows of the quarter as well as for the year.

I now hand over to Suresh who will take us through the financial performance discussion.

Suresh L Thank you, Smita. I will now take you through the business performance for the fourth quarter and the full year ended 31st March, 2017.

If you will move on to slide 16, you will notice that overall the performance financial has been in line with our expectations. We grew the sales by almost 12% this year through all the four quarters delivering positive comparable sales. We delivered same store sales growth of 4% in FY 2017 and 1% in Q4 FY 2017 compared to 1.8% in FY 2016 and 8.4% in Q4 FY 2016 respectively.

Increase in sales has also been led by addition of new restaurants and on account of our significant work around our brand extensions namely

McCafé and MDS which has seen a very healthy growth rate as mentioned in the previous slides.

The sales growth in this quarter has been lower at 5.8% largely on account of shift in promotion and season sales done by malls as well as an impact of additional day last year which was mentioned Smita earlier.

Overall, the sales performance shows that the efforts, we have been trying to drive over the last 18 months to 24 months around delivering superior customer experience to our consumers is yielding results and we hope to keep this momentum going as we move forward in FY 2018 and beyond.

Talking about gross margins, our continuous work around driving better product mix management aided by McCafé, product line extensions and menu innovation round the year along with other usual levers of menu price hike and supply chain efficiencies has helped expand our gross margins by approximately 70 basis points in FY 2017 and 40 basis points for Q4 FY 2017.

On the restaurant operating margin, while we expanded our gross margins year-on-year in FY 2017, our RoM saw a dip of approximately 90 basis points largely on account of higher payroll and employee expenses impacted by hike in minimum wages by around 25% to 30% in Karnataka. Also, this year we have consciously invested higher in brand marketing compared to last year. This has been slightly offset by ROP 2.0 restaurants led efficiencies on our operating cost structure.

On the operating EBITDA, we have been able to drive leverage across our G&A expenses in FY 2017. Therefore, largely on account of lower restaurant operating margins, we have seen a dip of ~50 basis points in our operating EBITDA margin this year. The operating EBITDA margin for the quarter stood at 5%.

Coming over to slide 19, it is quite encouraging to demonstrate the progress on driving better cash profits as we move towards our journey and strategy of having profitable growth every year. Our hard work around driving efficient capex and opex largely led by ROP 2.0 restaurants, we have been able to more than double the cash profit over the last 24 months and we registered a healthy increase of approximately 28% in cash profits during FY 2017.

Lastly, we shall continue to build on our strategic initiatives and progress which we have made in FY 2017 to help us deliver better profitable growth in future.

With that said, I would now hand over back to Amit who would take you through the strategy and outlook for FY 2018 and beyond and give the closing remarks.

Amit Jatia Thank you, Suresh. Our new stores that offer a brand-new service experience catapulted McDonald's into another league. The newly launched experience of the future restaurant, empower the customers to choose and define the dining experience according to their unique preferences. Our customers had greatly appreciated the convenience of table service, self-order kiosk, and the customizations that the new stores offer. These experience of the future restaurants, expansion of the menu and increase penetration of brand extension including breakfast will be the building blocks for McDonald's over the next few years.

We will continue to offer contemporary experiences to create brand differentiation and maintain our lead in the industry. We will continue our growth trajectory in FY 2018, the plan is to add 25 to 30 new restaurants through the year. The company will sharpen its focus on driving profitability, it will keep a close eye on its restaurant portfolio and keep evaluating opportunities to maximize shareholder return.

With this, I now open it up for Q&A. We will be happy to answer any questions you might have.

Moderator Thank you very much. We will now begin the question and answer session. The first question is from the line of Latika Chopra from J. P. Morgan. Please go ahead.

Latika Chopra Just wanted to check on, if you could give us a split of this 4% SSSG over the year in terms of what was the contribution coming from pricing, volume, and probably mix?

Amit Jatia Thanks for the question, Latika. Obviously, we do not break-up the details so much. But I think it is primarily driven by three things which is pretty much what worked for us in the past as well. First and foremost, McDonald's delivery continues to grow quite substantially as we have shared with you. The McCafé continues to grow quite substantially. And the third thing is menu and value. So, these are the three things that have sort of contributed to grow the same store sales. As far as prices hikes are concerned, we have kept it extremely marginal last year, anywhere between 2% to 3%. So, I think that is really the way we were able to grow our same store sales.

Latika Chopra And how would you view the SSSG to pan out over the course of FY 2018? Are you seeing demand to be back to normal levels now and given your efforts to accelerate various initiatives, should we be more confident about high single-digit sort of an SSSG over the course of FY 2018?

Amit Jatia Yes, absolutely. See, one cannot discount a major disruption that came in last year. If you look at our trends, our comps were continuing to grow quarter-on-quarter, last quarter was challenging. Now, if you think about the demonetization was announced on November 8th, you cannot expect that around 31st December the impact is gone. It has taken as a quarter to sort of get back. I do believe that we are surely back to the predemonetization days and especially our new value platform that we have launched on April 1, has yielded good connection with the consumer. So, we are quite hopeful that we would be in the mid-single-digits number as you asked. We are quite confident about that.

Latika Chopra Still wait out for high single-digit numbers to come through in couple of quarters is that so?

Amit Jatia Yes, it will. I think quarter-on-quarter you will see us in pretty good shape. I am already seeing the consumer sentiment improve a little bit but I think it is not overnight it is going to take a few more months and quarters. I think GST should help consumer sentiment as well. Let us see how it all pans out with pricing and what companies respond but I am generally quite positive about where we are going and you will see that in our results quarter-on-quarter.

Moderator Thank you. The next question is from the line of Vivek Maheshwari from CLSA. Please go ahead.

Vivek My first question is on the input cost, how is the trend on the input cost side right now for you?

Amit Jatia It is all right. Some things go up, some things go down but we have been able to manage that well. So, how we are able to do that Vivek is we basically know that input cost basically things rise. So, you need to have enough pipeline of projects that essentially ensures that while something's going up to work on some efficiency to keep it at least at the same level. So, overall inflation has been quite supportive to us and it has helped us basically gain the work we have done through menu. Otherwise in few years before whatever gains we would get out of menu would go away in just keeping inflation at bay. So, if you see the chart in the Investor Presentation of the Earnings Call, I am very pleased with the very steady progress. So, no knee jerk reactions for the consumer, very slow and steady product mix plays have helped us improve it. So, I hope that answers the question.

Vivek Right. And over the last few quarters we have been consistently seeing you focusing on cost aspect. Do you think the low hanging fruits are in the bag or you still think there will be more opportunities to do so?

Amit Jatia I think there are more opportunities to do that. All I keep saying is do not focus on one quarter because our business is in the growth mode and there are tonnes of external impacts that come in. Plus, there are new restaurant that suddenly open for example last quarter we opened nine restaurants. But year-on-year you will generally see us make progress. To give you a little more flavor, our utility initiative has yielded good results. Utilities is an extremely difficult area because we cannot do much about the rates at which we get utilities. So, for us having made serious impact in that area clearly tells us that yes, when we zoom out and we think about it strategically we are able to find solutions.

Vivek Okay. And this quarter gross margin almost 61.5% or just shy of that. do you think those are like sustainable, is there anything although of course, over the years you have been seeing an expansion but 61.5% is something that can be modeled into FY 2018 as well?

Amit Jatia I think so, we do not expect it go down for sure but 20 basis points here and there is possible on a quarter-on-quarter basis. But on a year-on-year basis you will see progress. It is got to be steady in today's business environment.

Vivek Sure. And on the staff cost side you mentioned about Karnataka, can we just know that total staff cost is Rs. 29 crores in this quarter, how much will be the element of one-off if you can quantify because I believe you mentioned it is from retrospective effect, right?

Suresh L 40 bps is basically the impact that we have taken in this quarter including the retrospective effect.

Vivek So, if I am modeling it ahead, can you just tell me how much of this Rs. 29 crores will not be recurring?

Suresh L So, exactly the half of it is basically pertaining to the previous quarter. So, on a quarter basis you can take about 20 bps is the impact.

Amit Jatia Also Vivek, I would like to provide you with some flavor on that. So, the quarter for January to March, if you see our trends by 10-12 quarters, you will find that this is the weakest quarter generally for sales and you will see that the labor cost are going to be much better quarter-on-quarter moving forward. But that is more to do with seasonal trends as well. So, just factor that into your thinking as well.

Vivek Sure. And this corporate expense on a Y-o-Y basis is essentially just because of the base, right otherwise you are pretty much continuing with the trend that we had through the course of this year except third quarter where there was as slight increase.

Suresh L Yeah. So, you see, Vivek basically on the corporate expenses there are various corporate initiatives events activities and trainings etc. that have skews within the year. So, it is appropriate to review it on an annual basis and you will see therefore that we have had leverage on the corporate expenses as well and it is also important to note that the full impact of various investments that we have made at corporate level are yet to play out. And therefore, we believe that there will be more leverage as we grow from here onwards.

Amit Jatia But the important thing is that I think last year was a good year on corporate costs and our endeavor is to sort of maintain that and as Suresh said, as sales grow we expect corporate cost as a percentage of sales to keep coming down.

Moderator Thank you. The next question is from the line of Vijay Chugh from Nirmal Bang. Please go ahead.

Vijay Chugh I think most consumer companies have alluded in the past saying that northern India was where they had seen significant impact of demand on demonetization whereas that is not the case in your portfolio. It will be helpful to know if any dispersion in terms of demand that you can help us with western India versus southern India or urban markets like Hyderabad or Mumbai versus sort of small tier towns. Any color that you can share because obviously demonetization was a very significant event for consumers.

Amit Jatia So, we of course do not have north India into our portfolio, so I would not be able to add anything around that. Outside of which we do not share break-ups but we are more skewed towards the 6 key cities which is Mumbai, Pune, Ahmedabad, Chennai, Bengaluru and Hyderabad. So, I think it has been even. But to be honest we cannot share too much details around that as we do not break-up by region.

Vijay Chugh Okay. Anything in terms of recovery because obviously, the event was fairly significant, so it helps to sort of understand what will be the path of recovery for you ahead?

Amit Jatia No, actually as I mentioned to you we launched our new value platform on April 1 and that has yielded pretty good results for us. So, we are seeing decent results from a value point of view. But you know future quarters I think best to be discussed in the next call. But the recovery is even is the key message.

Moderator Thank you. The next question is from the line of Abneesh Roy from Edelweiss. Please go ahead.

Abneesh Roy Sir, my first question, in breakfast you are the only branded QSR player. What I am surprised if you have revamped the entire menu. So, is it really attractive enough that no other QSR player is entering there and you need to revamp. So, is the revamp because it has not worked or you think it was needed the time period has lapsed so it was needed?

Amit Jatia See, leaders follow their own path and we do not look at other QSRs to decide what we want to do. We have a pretty clear strategic path and like I said, all we have to do take event to deal with tactics not strategy. Globally breakfast is an absolutely fantastic brand platform for McDonald's. We are global leaders by far in breakfast and globally it is the same program we have seen country after country where it starts in a certain manner but you keep investing, keep investing and soon you become a leader. We have seen that happen in the past as well and every brand platform needs to get renewed and evolved. So, you know our previous focus from 2013 to 2016 was to build McCafé and obviously as McCafé continuous to play out breakfast is a future potential that we worked on and as I mentioned in many of my calls that you got to keep the pipeline of tomorrow's businesses quite full and we think that breakfast is tomorrow's business and we think that there is a $2 billion market in our estimate of outside of home consumption of breakfast. And breakfast along with delivery for us is a pretty powerful tool. So, we are quite focused on it.

Abneesh Roy And sir, globally, you said it is quite big, so any numbers you can share as a percentage how much it is total and in India culturally is that a challenge because in India breakfast options are local in terms of offering, so that is really you have started in a way in terms of Dosa flavor, etc., but clearly that is very different from the actual product. So, in India the standard number will be much lower in a mature phase.

Amit Jatia See, basically, if you tell me that China had the habit of eating breakfast or even for that matter 20 years ago U.S. was in a different platform when it came to breakfast. So, when we started breakfast we started getting the history of how we have built in other markets. I think to be honest the trend is the same. Breakfast on the go, convenience and people coming to work and ordering out all that is typically how the breakfast business has grown everywhere else. So, we are quite confident about that. Also I will tell you that every country in its own way is unique. India is only unique for India. But China is as unique in China as it would be for anyone else. I hope you know what I am trying to say. So, we are quite hopeful. We have seen growth in the business, we have seen how other emerging markets like Philippines, China, Indonesia and how they have behaved on breakfast and that tells us that it is an area we want to invest in.

Abneesh Roy But can it be double-digit contribution

Amit Jatia Absolutely, it can be but not in a short span, it is going to take three years to five years build. It is just like you talked about the Dosa Masala similarly when we introduced Aloo Tikki we got the same comments in 1997. But today is the Aloo Tikki is a platform and a product that pretty much every QSR has followed us on. Everybody has an offering similar to an Aloo Tikki. So, we think that as consumers use us for convenience of the breakfast offering, soon the product starts getting ingrained into the DNA and that is how the business gets build. So, we are quite hopeful, we have seen double-digit contributions in other markets and we do expect over a three years to five years period. It is not a quarter-on-quarter game is the crux.

Abneesh Roy Sir, coming to McCafé, you said you are number 2 currently. So, is this in terms of number of stores and second is you have grown extremely strongly at 30% in terms of average sales per day in McCafé. Now, does it become very difficult because 30% is a good number now base also will be there, so now we should look at a much more reasonable number in FY 2018?

Amit Jatia No, I do not think so. I mean, this is what I feel that when you are looking at delivery we have been doing 30% to 40% growth over for the last five years to six years and I feel it is going to continue to grow pretty strongly as Smita shared in the comment as well. Similarly, I feel McCafé is only the beginning, in fact it has grown almost 70% average stores sales per day of McCafé since the beginning. So, firstly, we feel that the 111 needs to go to 250. Secondly, we believe that average volume, there are many categories of beverage that we have still not played in McCafé and the reason we have been able to grow the average unit by 70% is of course first a great product secondly, a great experience because of the Barista's. But thirdly, because of the product library we built. So, every summer we have introduced a new line of products, whether it is the Coolers, whether it is the Smoothies, whether it is share shakes, whether it is line extensions around some of our current products. So, you will continue to see a play there. So, if you zoom out of McDonald's and look at the broader beverage market, we see that all the fun that is happening in the beverage market, with other non-carbonated game is playing out within McCafé as well. Therefore, we are quite hope that this growth trajectory will continue.

Abneesh Roy Sir, my next question is on the FY 2018 comment which you made that it is looking good. So, two questions there, one is you said because of GST you said I think sentiments will improve. So, I wanted to understand that part. Second is sir, you are present in six key cities and in most of these cities IT and BPO segment is quite big and what we are seeing as a new development is job additions which was happening earlier big time in these, now it's the other way around it is job losses. So, big job losses being announced by the bit IT and BPO companies. So, does this really impact I know you cater to the entire population but clearly, a lot of the consumption has also happened in IT, BPO sector.

Amit Jatia See, we have been through ups and downs. We do not go into IT Parks for example specifically. So, people have asked me, why are you not in office buildings, office complexes. So, McDonald works on multiple generators, okay. So, when we look at real estate and that is a whole different understanding of why therefore we want multiple generators to support a restaurant. So, I am quite confident that just one sector getting impacted is not necessarily going to show up in our results. But yes, if the overall economy slows down and footfalls to retail locations take a beating then definitely that will be visible in pretty much every brand that you can see. And when I said FY 2018 all I am saying is key just to make sure that it is well understood is that I definitely feel the impact of demonetization is behind us. I am sensing a decent consumer sentiment coming back and I feel that reforms basically psychologically and sentimentally help the consumer. But again, it depends on how everybody that is all corporate deal with GST. So, if GST is going to help with rationalization of prices, if the efficiencies of supply chain start coming in, I think that it might help consumption over all to the consumer. Also, to some extent I think from our point of view as we get efficiencies because of GST, that will help us from our supply chain costs, etc. So, I am quite positive about where we are heading month-on-month, it is not a shift that is going to happen just tomorrow.

Abneesh Roy Sir, one small on the Burger was when I see the large footfall spaces for example, stadium for example, sea beaches, some of the Pizza players are doing interesting thing that they readymade product and limited SKU but readymade and that is selling a lot. In your case are you doing something on these lines?

Amit Jatia No, these things we feel, takes energy away from our core and we do not do that Abneesh, we do not work on such projects. Sometimes there are one-offs that we take advantage of but it is rare.

Abneesh Roy What is the issue?

Amit Jatia The important thing is that we do not tend to focus on that because the game that we get versus the effort and cost, we do not find that justified. We like to keep our energy on the big-ticket items and for me I would rather build another three McCafé than to take my energy to get that volume from one stadium and then we have the risk of food safety, cold product, terrible service which takes the band down. So, we stay away from such things.

Moderator Thank you. The next question is from the line of Neha Bothra from Axis Capital. Please go ahead.

Neha Bothra Sir, you just mentioned that in FY 2018 you plan to add around 25 to 30 restaurants. So does this include McCafé or it is the overall number that you have shared?

Amit Jatia No, McCafé is always on top. These are just new store additions. McCafé as we have maintained at over the next two years to three years again we will sort of double. But 30 to 40 new McCafé's you can expect for sure in FY18.

Neha Bothra Okay. So, total would be like 30 new restaurants as well as another 30 to 40 McCafé's.

Amit Jatia Yeah, exactly.

Neha Bothra Okay. So, what would be the total investment for this?

Amit Jatia Typically, as always about Rs. 100 crores to Rs. 110 crores is roughly what we are investing every year, so it will remain within that level.

Neha Bothra Okay. And sir, any store consolidation or rationalization or like right sizing of stores that you are looking at?

Amit Jatia I mean right sizing we do not do because of course we keep looking at our portfolio. In every year, two to three restaurants, you can see them sort of close because either the lease expires given that we have been in the business now for 20 years, some leases are coming up for renewal. So, about three stores to four stores a year is what you will see us close or relocate.

Neha Bothra Okay. And sir, what is your current debt and any debt reduction that you are looking at?

Amit Jatia I think, we are still quite all right when it comes to debt and equity, Suresh can help with exact numbers?

Suresh L So, when you look at debt the net debt we are just about 20 odd crores. We do not look at debt in isolation, as there is also sufficient cash on the balance sheet. So, net-net we are about 20 Crores.

Moderator Thank you. The next question is from the line of Kuldeep Gangwar from HSBC. Please go ahead.

Kuldeep What is the current indirect tax rate for us and post GST what would be the area of benefits and if possible, the quantum of the same?

Amit Jatia See, it is hard because it is state by state and every state has a different way of taxing it. But typically, 12.5% is normally VAT and about 6% is roughly the Service Tax but it varies state-by-state. So, if it comes to about 18% we should be pretty all right.

Kuldeep Okay. And second thing, regarding the competition from the technology platform like what is your take about this Food panda, Swiggy, etc., how it is playing out for you?

Amit Jatia It is playing out beautifully for us because not only do we have our own platform but we are also are on their platforms. My best example to you is think about going to a mall and in a food court there are 40 players and yet we take a very large share of the foot court sales. Similarly, just imagine on internet there are many-many people available and as long as we are available on all platforms, our brand and our product and everything else, pulls them to us. So, we are partners with them rather than competing with them.

Kuldeep Okay. Last thing, do you share the contribution from the delivery for you?

Amit Jatia We do not share as a percentage of sale, but I think we have been getting better like annually at least we are sharing the growth rate which I think Smita did in her Presentation.

Kuldeep So, is it still single-digit?

Amit Jatia 25% growth and we cannot share the break-up as a percentage of sales.

Moderator Thank you. The next question is from the line of Yash Jhaveri from Alder Capital. Please go ahead.

Yash Jhaveri Just one question, how many stores did we refurbish in fiscal 2017 and what was the money spent for that?

Amit Jatia So, again, we do not break-up our capex by that. But roughly, I would say between 30 stores to 40 stores we would have reimaged.

Yash Jhaveri Okay. And any guidance on this refurbishment?

Amit Jatia It is going to continue at a similar pace because what we like to do when we are adding a McCafé we like to refurbish the store with it. So, if we are adding 30 to 40 McCafé's, yes some could be new restaurants as well but we like to refurbish at that pace.

Yash Jhaveri Sure. And usually I mean after how many years do you refurbish is it five years or seven years?

Amit Jatia No, it is normally 8 to 10-years that is typically the cycle for refurb meanwhile we of course maintain the store through a refresh of wallpaper and cleaning-up, anything else painting job that is pretty much sort of M&R.

Moderator Thank you. The next question is from the line of Latika Chopra from J. P. Morgan. Please go ahead.

Latika Chopra Just any thoughts on the Fat Tax being talked about the regulators off late.

Amit Jatia See, it is all speculation and if you read the details, firstly, I believe that when you look at say even a McDonald's offering, there are different kinds of products with different calorie content. But in any case the core thing is that it is primarily speculation as yet. We do not know what they are talking about. I would say 80% to 90% of the food that we eat will come in that, if they come out with the regulation the way I read it. It is not about McDonald's.

Latika Chopra All right. And any experience in Kerala so far?

Amit Jatia I keep telling that they call it Fat Tax to get media attention, in really it was VAT. So, the way we read the tax is it is just a rate of VAT for all restaurants basically, it is not that it is just for Burgers or Pizzas or anything, it is in line with all other states as well. So, if you go to Tamil Nadu, if you go to Telangana, Karnataka, all of them have the same VAT that Kerala has. They just made it interesting for readers by calling it Fat Tax. Basically, it is a tax for restaurants not for fat.

Moderator Thank you. The next question is from the line of Kunal Vora from BNP Paribas. Please go ahead.

Kunal Vora On the food aggregators wanted to get a sense on like what proportion of your sales would be coming from them? And also are they getting bigger, are their sales increasing and are they increasing decreasing discounts, some trends there?

Amit Jatia No, I am proud to say that our platform is really-really robust. What you got to also understand that just because they add, just because they offer say 1,000 restaurants, you got to understand there are a lot of restaurants do not have the ability to package and deliver on time which impact customer experience as well. So, for us it is a small platform it is not yet substantial platform. I think bulk of the business still continues to be from our own platform. But we are partners with them and we do quite well for them. So, I think it is a very good co-existence I would say.

Kunal Vora But would not the sales on their platform to be extremely fragmented considering that they offer a large variety

Amit Jatia No. See, like I mention to you, if you go to a mall, to a food court, there are 30 players in a food court and if you look at the sales that McDonald's does in that food court it would be significant, we do not share the details. But we are very-very important anchors when it comes to a food court. Similarly, what we have learned is that you will always generally order from a place that you are familiar with. When you are hungry, you are not going to take a chance or taking a new restaurant and ordering because you do not know the quantities, you do not know the taste of the food and if by chance you do not like it you are two hours away and you are hungry. So, we have seen that primary users are McDonald's users and as we have over 180 million to 200 million users that is a lot of users. So, I think on the FoodPanda or other platforms that we are there McDonald's offer the same advantage that a food court offers to customers with a McDonald's being there. That is the way I see it.

Kunal Vora Sure. So, in that case branded QSR should be a large proportion of sales which these food aggregators are doing, is that the case? Is it reflecting?

Amit Jatia I have no idea, what their sales break-up is obviously I have no clue but the point is that one, we have been growing the delivery platform very substantially and our business has been extremely good. Like I said, do not under estimate what the restaurant readiness has to be, to deliver. It is not just about having a platform and you think that all restaurants will get that platform to deliver. Everybody is learning, aggregators are learning. So similarly, we have had the learning from 2005, so I think we are at a different platform and scale when it comes to our ability to manage the whole online delivery business. Delivery is a very operational business, you got to recognize that. And, companies who are operationally excellent which I believe McDonald's falls in to that have a much better chance to do good delivery sales than somebody who is not geared up with operational excellence.

Kunal Vora Understood. My second question sir, on GST, there is general expectation that there will be shift from unorganized to organized. Do you see this happening in restaurant industry as well and how is the tax compliance level obviously like prima facie the tax compliance level in restaurant industry would be very-very low.

Amit Jatia Exactly, so it is to that extent and advantage of us because if you go to the street you are not paying any taxes and as more people start complying with taxes it becomes a more level playing field for the organized sector. So, we are looking forward to GST to be honest.

Kunal Vora But do you see this actually happening like local restaurant and would they actually start becoming compliant

Amit Jatia We are not counting on it but we are saying that okay, if it benefits us, it benefits us.

Moderator Thank you. The next question is from the line of Manjeet Buaria from Solidarity Advisors. Please go ahead.

Manjeet Buaria I had one question sir, is it possible for us to kind of break the SSSG by the vintage of stores may be say stores which we are more than seven years old then ones which are between 13 months and 7 years' kind of metric?

Amit Jatia No, we do not share that data in any case. But the important thing is in the portfolio we believe that we are a small portfolio as yet, 258 stores of which may be 200 stores are comparable sales. So, pretty much every store needs to perform if you want to at least in this difficult environment to deliver positive comps but we do not share the break-up.

Manjeet Buaria Actually, where my question is coming from I was wondering in the cities where we started over the last 20 years, initially the acceptance in metros would have gone up and what I really struggle to understand in last few years when other discretionary spends have been so high and us being in the value chain of the product and food. We still have not seen consistent SSSG and I am not talking about 10% but even 6% to 8% which I believe is a reasonable SSSG to have to sustainably improve operating margins over time. So, were the low-hanging revenue fruit plucked out and now these older areas do not grow as much. So, how does one think about?

Amit Jatia No, I will tell you how to think about it. I think, I do not agree with that thinking. See, what happens is at the end of the day we cannot run in isolation of the economy. So, if your value does not mean that the economic impact is not going to come to anything that is value. The critical thing is when do you eat outside of home, when you go outside of home, right? So, basically where are we present? We are present in retail locations of footfall areas. So, if footfalls to malls, footfall to retail locations, if shopping is impacted, if people are not trying to conserve they will say let us eat at home instead of eating out, all of that impacts us because yet, eating out is still in India discretionary spend and in a lot of other countries in my view it is kind of wise people because you have to eat out to survive. So, I feel, therefore, it is about retail footfalls it is about footfalls in high streets that impact our business as well. So, I feel that, we feel we have given differentiated results over the last seven quarters where particularly even if you look at the last quarter where our SSG is actually about 2% if you take out that February. We have retained the base line that is very important. When we have taken the base line up to 8.4% in last quarter same period on top of that we have been able to give a 2% comparable sales effectively I feel that shows their sustainability in the way we are executing. It is not built around promotion or discounting that I have got the business for the quarter and the minute I pull the discount out is gone. So, when I am coming back against a strong same store sales period I am going weak under that. I hope this explains the thinking to you.

Manjeet Buaria So, I had one question on this. In the earlier periods when say there were a bit longer back 2010, 2011, 2012, 2013 kind of periods but when we saw those extremely high SSSG were the Shopping Malls and the high streets and all doing so much better than they were doing in the last two years - three years?

Amit Jatia It is simple because we track data quite substantially, the frequency of eating out was rising. There are lot of dynamic changes that are happening in the retail environment. So, for example, were multiplexes available 15 years ago, no. Even if there were, there were 10 multiplexes, today there are maybe 2,000 multiplexes. Today when a movie comes in a one week people go out and see it and the game is over. Earlier it would run for golden jubilee, silver jubilee, platinum jubilee and so on. So, the dynamics are changing and as malls came, as retail came, people started eating out more often because they got more opportunity to eat out. The minute the economy and the GDP went down to 4%-5%, people stopped spending because of whatever economic condition we were in, obviously the footfalls took a beating and everybody's results were down. It is not that one brand alone took a beating. So, my point of view is that those were the days when the frequency of eating out was rising because of all the things I have just talked about. In the last few years you tell me how many new malls have come up, it is primarily consolidation. People are buying and selling malls and yes, there are 5-10 malls that are opening in the whole country maybe. But I feel that as investment climate changes, as consumer sentiment changes, consumer start buying houses they need to refurbish that house. There is a good feel about it, they go to malls, they spend, that is what is needed for consumption to go up. I hope this gives you a bit of flavor.

Moderator Thank you. The next question is from the line of Kenneth Serrao from Alpha Capital. Please go ahead.

Kenneth Serrao Just two questions, one is a minor one which is this other income is now becoming significant if you could shed some light on that and what comes out of that simple. And the second one is large part of the McDonald's play is really about investing for the future and the brand and often the best way to measure it is just customer satisfaction, customer reviews, are you guys doing something around that and if so, not necessarily right now but over time could you kind of just share that as part of your standard pack because that would just be finally if you look at Amazon versus Flipkart or if you look at Uber versus Ola it is just customer satisfaction that finally wins the game I like McDonald's as brand and is there some way that you guys could capture that statement.

Amit Jatia Sure, I will just cover the second one first, that is easy. See, the good news is that is not in our control to start with and you could just Google and you get the McDonald's reviews. The important thing I can tell upfront is that if you see reviews for Crossroads-2, for our Bandra Hill Road restaurant and some of the newer restaurants, you will see that the reviews are at 4.5 to 5 on an average and the comments are absolutely outstanding. This tells us that the experience of the future is resonating with the consumers and as we built more and more of the stores are hoping that our average reviews go up. So, what I am saying is while we of course track that and there is a global program that looks at consumer feedback to measure how we do business but that is an internal data that we do not like to share but the point I am trying to make there is a lot of external data that you can look at to tell how McDonald's is resonating with the consumer. On the second question yes, we have investments and we have interest cost, so you will see that we keep balancing that and that is really what the other income is all about.

Moderator Thank you. The next question is from the line of Nishit Rathi from CVC Advisors. Please go ahead.

Nishit Rathi Just one question, did I hear it right you have 180 million to 200 million users is that correct?

Amit Jatia Yes, you heard it absolutely right, we are happy to reconfirm that.

Nishit Rathi Across over the years these many people have come and eat at McDonald's?

Amit Jatia No, every year we get 180 to 200 million people visit us across the 258 restaurants that we have in West and South. These are not unique customers of course, these are the total number of customers we get.

Nishit Rathi Okay. So, it is basically these are the number of orders that you serve.

Amit Jatia No, these are the number of people who visit at McDonald's.

Nishit Rathi Is there any chance you get the number of unique customers, do you track that or you can share that?

Amit Jatia Even if we do, I am sorry, we would not be able to share that.

Moderator Thank you. The next question is from the line of Aditya Joshi from Antique Limited. Please go ahead.

Aditya Joshi Sir, my question is regarding breakfast delivery. Has it started picking up with the newly offered menu that we have worked upon. So, are we seeing more and more delivery in breakfast?

Amit Jatia We do not share that data unfortunately.

Aditya Joshi Okay. And sir, will we be taking a similar price hikes in FY18, that we have taken in FY 2017?

Amit Jatia Yeah, price hike as I mentioned from a guidance point of view is anywhere between 2.5% to 5% a year depending on inflation and other things. So, that is roughly where we intent to stay.

Aditya Joshi Okay. And sir, going ahead our store expansion will it be in the newly opened format store or it will be in the regular format that we have been opening?

Amit Jatia It will be primarily closer to the new format.

Aditya Joshi Okay, sir. And do we have s store expansion focus geography wise in South or West or will we be expanding the way we have been across different states?

Amit Jatia No, we are pretty focused about 70% of our new stores will open in the six key cities and about 20% to 30% will be either in other cities in than the six or new cities.

Aditya Joshi Okay, sir. And sir, we have been hearing that Patanjali would be entering the QSR space, so any thoughts on that?

Amit Jatia There are a lot of thoughts, we are looking forward to having them come in. We will enjoy having some additional competition. My view is I mean there are millions of restaurants around we compete with everybody the Sukh Sagars of the world, etc., if you call ever restaurant a competitor. But if you really think about it we are Burger company and we compete with people who do Burgers. So, anybody who opens a new restaurant does not impact us. It is primarily if it is in the western fast food area.

Moderator Thank you. The next question is from the line of Umang Shah from JM Financial. Please go ahead.

Umang Shah I have just one single question. So, going forward we are looking at the government policies they are increasing the roadways & highways. How are we looking at that opportunity? Are we investing towards it or have we any thought about it while going for new stores?

Amit Jatia We look at it is the highway traffic and as highway traffic is growing, we will of course, you will see restaurants there. If you drive from Mumbai to Ahmedabad today you will see a McDonald's pretty much every 150 kilometers or so, 100 kilometers rather. So, we are pretty, we have a way in which we evaluate how to open on highway and that will continue.

Umang Shah No, not regarding toll. Are we in this year when we are seeing 25 new stores and around 40 new McCafé's, so that is on basis of this new roads, new highways?

Amit Jatia No, that may be a part of it, I mean I do not think this just determines our number of stores, the store basis is a mix of wherever we get the best real estate.

Moderator Thank you. The next question is from the line of Neha Bothra from Axis Capital. Please go ahead.

Neha Bothra Sir, just wanted to understand, many QSR companies are focusing on reducing the employee cost and in your case the employee cost is pretty high in this quarter. So, any thought on automation and reducing employee cost going forward?

Amit Jatia No, basically it is a continuous process. See, cost in India rise all the time and productivity growth is important, so two years ago we had the same impact in Mumbai and then we brought labor cost down quite well. So, it is a continuous process and we will deal with it. But it is not that we can deal with it tomorrow but you can deal with it over a period of time. So, it is a continuous process, that is the key here.

Neha Bothra And sir, a little more focus on your new format store as you said there would be self-kiosk and also table service. So, these are the only two different things within the store or anything else that is additional?

Amit Jatia No, it is everything, the décor is completely different, it kind of gives you a different feel, there is of course McCafé with it, there is food elements in there, like you know many of these have soups & salads, you can customize your products when you are ordering from the self-ordering kiosk, you can add more sauce, take something out, there are games, there is a family area, so there are tonnes of things that are different. I mean, I think, the best would be to go see it which will give you a better sense of that.

Neha Bothra The stores sizes have increased because of like as you say there is games and family areas and all?

Amit Jatia Store sizes still around 3,000 square foot on an average.

Neha Bothra Okay. And sir, all the new stores will have McCafé along with it?

Amit Jatia By and large, so it depends on the city, depends on timing. So, by in large, most new stores open with a McCafé.

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

Amit Jatia Well, thank you for attending the conference call today, I really appreciate your time listening to us and for your questions. If there are any more questions, please do reach out to Ankit Arora, all his details are available on our website. Thank you. Good afternoon and have a great weekend.

Moderator Thank you. On behalf of Westlife Development Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.