Q1 FY2015 Earnings Call Transcript – Aug 1, 2014

CORPORATE PARTICIPANTS:

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

Moderator Ladies and gentlemen, good day and welcome to the first quarter ended June 30, 2014, Earnings Conference Call of Westlife Development Limited. As a reminder all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference call, please signal an operator by pressing * and then 0 on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ankit Arora, Manager Investor Relations. Thank you and over to you sir.

Ankit Arora Thanks Inba. Welcome everyone and thank you for joining us on Westlife Development Limited first quarter ended June 30th, 2014, earnings conference Call. 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 has 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, who will be followed by Smita to take you through the key business initiatives and Suresh will cover the financial analysis and the highlights during the review period. At the end of the management discussion we will have a Q&A session.

Before we start, I would like to remind you that some of the statements made or discussed on this call today may be forward-looking in nature and must be viewed in conjunction with risk and uncertainties we face. A detailed statement and explanation of these risks is available in this quarter's results 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.

Amit Jatia Thank you Ankit. Good evening everybody, and thank you very much for joining the call today. Before we discuss the current quarter results, I thought I would share my perspective on the business and the sector in general.

I request you to please turn to Page #3 of the Earnings Presentation if you have that in front of you. The economic environment continues to be challenging, leading to weak consumer sentiment resulting in lower consumer spends. And, therefore leading to lower footfalls on high street and malls. However, we are very encouraged that our new stable government is in place and are happy to see the government's seriousness to get the economy back on the growth track. We can already see business confidence coming back as well as renewed global interest in investing in India. This is very encouraging and we will accelerate the economy coming back on track in the coming months.

The informal eating out market in India is still in its nascent stages of development and therefore it is critical that WDL strategic and business imperatives remains strongly aligned with that reality. We need to continue to build on the very strong foundation that we laid down over the last 18 years in building the QSR sector and the McDonald's business in India so that we continue to remain leaders in the QSR sector.

As we navigate the current environment we need to manage the short term, but more importantly continue to ensure we build the long term which is what will determine the success of our business in India. McDonald's in India serves over 300 million consumers annually and our core value proposition is around everyday value. We have chosen to build consumer loyalty through our smile cards over deep discount which sometimes could chase empty guest counts but could result in higher same store sales numbers in the short term. However the risk is for consumers to get hooked to discounting which we believe can hurt the brand in the long term.

We do serve a very large base of customers and the current weak sentiment impact us due to lower consumer footfalls on high street and malls. However, we do believe our approach around every day value will help us grow base sales back as the economy take shape and the GDP growth gets back on track. Our everyday value is delivered through our happy price menu which starts at Rs. 25 and the extra value meals that we offer that have a discount of around 30%.

However, yet through our robust supply chain which is directly links to farms eliminating middle men in the process, we have been able to grow a gross margin quarter-on-quarter while retaining value for our customers. McDonalds is known for its quality and standardizations and we have ensured that we do not compromise on these values, but yet maintain value for the customer. With respect to broadening accessibility and becoming more a more accessible to our customers we continue to work hard on opening high quality restaurants with long leases and favorable terms while focusing on growing our drive thru portfolio which we believe gives us real estate competitive advantage.

Most of our recent openings have been free standing drive thru restaurants with at least 20 car parks and we believe that his will provide us with benefits in the long term. We continue to pursue an aggressive but sustainable growth approach while driving restaurant development cost down. In the last few years we maintained our opening cost between Rs. 25 million to Rs. 30 million and will continue to do so in the next few years in spite of high inflation.

As we have explained earlier, new stores take two to three years to establish themselves in it's trading area. Over the last two years we have added about 60 plus new restaurants which today is over 40% of our comparable store base in a very difficult environment. Even as these restaurants start with higher occupancy and other cost, we are happy to say that we have been able to maintain restaurant operating margin for the quarter. We firmly believe that as sales start looking up and these restaurants establish themselves in the trading area, we will see benefits accrue to the bottom line in the month ahead.

Lastly, our brand extensions continue to build both the brand and sales. McCafé continue to delight out customers and we have had good reviews on the coffee we have been able to serve. The interesting thing is we are able to see us building complimentary day parts, especially during breakfast and afternoons. We have also found that it attracts additional generators and customer types making it extremely complimentary to our overall business. We launched online delivery ordering through new platform in January and then the mobile application this quarter. We are happy to say that we have delivered positive comparable sales in delivery business since February 2014. We expect all our brand extensions to contribute healthily to our base sales growth in the coming years.

Moving on to Slide #4, I will quickly summarize the highlights for this particular quarter. With respect to restaurant expansion, our system wide restaurants are at about 189 stores with a gross addition of 29 new restaurants year-on-year while we added five new restaurants in quarter one. Drive thru portfolio continues to expand quite well and aggressively. We found that the economic slowdown, the high inflation and the consumer sentiment continues to remain weak and therefore comparable sales have been -9% compared to 0.5% in the same quarter in the previous year.

We will cover a bit more about McCafé in the coming slides and as I mentioned to you we are quite encouraged with the response we have got through our online and mobile app on delivery. Even while maintaining our value proposition to customers we are happy to say that we have been able to expand our gross margin by 175 basis points year-on-year. Primarily this has to do with an efficient product mix, menu pricing and managing raw cost better than before. Finally, we have cash & cash equivalents of about Rs. 1.7 billion currently on hand.

With this let me pass it on to Smita who will take you through the second part of the presentation.

Smita Jatia Thank you Amit. Continuing on our journey to accessible we open 29 restaurants in the last 12 months with 5 openings in the quarter. Out of these around one third has been free standing drive thru with at least 20 car parks. Drive thru is our real estate competitive advantage and they cater to the customers in the suburban outer cities as well as high way travelers providing them convenience and a hygienic place to stop and eat. This takes our store network to around 189 restaurants which is around 20% unit growth. Currently, our highest restaurant count is in Maharashtra and Karnataka, leaving the other states as opportunities for growth.

During this quarter, we also sharpened our strategy of customer centricity and thoughtfully tailored our marketing promotions to remain relevant and appealing to our customers. This quarter we do have school holiday and our customers are out of their houses. We launched the royal burgers in the premium platform; these burgers were created for the young adults and parents whose needs are more for taste, indulgence, and filingness. On the business front premium burgers always help giving us a healthy growth of average check.

To celebrate the spirit of FIFA World Cup with our customers, we partnered with McDonald's globally to change the look of the iconic red french-fry packaging with bold new art works, and unveiled a new augmented reality app to reward the customer with an engaging virtual trick short challenge. Additionally, we also launched the global player escort program for the first time in India, which gave them an opportunity to a child to experience the FIFA World Cup in Rio, Brazil.

As Amit also mentioned we fortify the efforts across a brand extension. We continue to expand a McCafé footprint across Mumbai taking the total count 9 McCafés as of today. McCafé has been a key factor in accelerating a beverage growth strategy and adding value to our customer experience. It has also been a key driver in optimizing the use of our restaurants at all hours of operation and thereby providing a high profit margin. Along with the McCafé we always reimage our restaurant, which also helps in lifting the brand image and hence improving comparable sales and profitability of the restaurants.

Furthermore, we have taken yet another step to connect with the millennium customer by strengthening our online capabilities with the launch of a new web ordering platform and mobile ordering app for delivery. These convenience lead initiative has contributed positively to the McDelivery business. In the coming years we will continue to invest across our brand extensions to not only be accessible, but also enhance the company's margin profile. Thank you and from here I hand over to Suresh

Suresh L Thank you Smita. I will now take you through the financial analysis of the results for the Q1 FY15. So if we move on to slide 12. The revenues have increased by modest 1.3% over the same quarter of the last year and Amit did mention in his opening remarks about the consumer sentiment still being muted. However, we are seeing some shades of improvement and as Smita mentioned during the last 12 months we have opened 29 new restaurants and this summer we also launched our new premium platform in the form of royal burgers with both the grilled chicken and the grilled paneer options.

If we move on to the restaurant operating margin, sharp focus on the operating margins at the restaurant level continues. Through the focus efforts by supply chain and menu management team, we have been able to drive significant efficiencies coupled with effective menu pricing strategy and that has helped us improve our gross margin significantly by around 175 basis points during the Q1 of FY15 over the same quarter of last year.

We have also as mentioned earlier invested in 29 new restaurants over the last 12 months ending June 2014, and this has a significant drag on our restaurant operating margins due to higher utility and rental costs. As you all know our restaurants typically take two to three years to mature and stabilize in the trading area and then start to contribute positively on the margins. Hence, in spite of the tough economic scenario and the inflationary headwinds around wages and significant new restaurants openings, we have been able to improve our restaurant operating margin by around 55 basis points during Q1.

On the operating EBITDA front, we continue to invest in people since they are the big enablers for our future growth. Hence we have consciously invested in talent acquisition management and development. Resultantly the corporate general and administrative expenses have increased by around 9% over the year in Q1. Hence while G&A would have its impact in the short term we believe this investment is critical to help us drive profitable business growth over long term and this would drive the operating leverage once the consumer confidence returns over the next few months. Largely due to this, we have seen flat operating EBITDA margin at 6% of the sales during Q1 compared to the same quarter of last year. With that said, I would now hand over back to Amit who would take you through the outlook and give the closing remarks.

Amit Jatia Thank you Suresh. We are quite excited about the opportunity in the QSR space, as per the Euromonitor the size is pretty large and WDL through the McDonald's brand is very well placed to lead the sector. The key from our point of view to navigate the short term while building for the future. We expect some short term difficulties due to delayed and short rainfall, although we believe that our risk management and strategic sourcing across the Indian geography has always been the best prepared to minimize impact in the industry.

We do believe the key is to increase accessibility of our brand McDonald's to the Indian consumer, through expanding the store network. We continue to expect to open 175 to 250 new restaurants in the next five years while adding 75 to 150 McCafés in the next three to five years. We will be more aggressive in re-imaging our stores especially in our long established markets like Mumbai, Pune, and Gujarat, to ensure that we remain relevant to the changing consumer needs. We expect menu to continue to play an important role in building our base line sales through brand extensions and limited time offers of our core products. We will continue to add more and more restaurants with free Wi-Fi for our customers, cashless services and enable our restaurants for the digital revolution that is eminent.

We will continue to look at opportunities to optimize a real estate portfolio especially in underperforming malls by relocating to better performing locations within the trading area in case the need arises. With that said, I would conclude and open it up for questions and answers.

Moderator Thank you very much sir. Ladies & gentlemen, we will now begin the question and answer session. Our first question is from Arnab Mitra of Credit Suisse. Please go ahead.

Arnab Mitra My first question is on the demand environment, last couple of quarters you have spoken about down trading into the unorganized sector, are you seeing any kind of improvement at the situation there. And secondly in terms of your own comparable sales it was around second, third quarter last year when you started seeing negative comparable sales. When do you think this negative 9% to 10% number can swing up substantially in this year?

Amit Jatia I personally feel that it is very hard to predict because it is dependent on consumer sentiment and economy, as I mentioned earlier we are very encouraged with all the moves that the new government is taking and obviously as the economy recovers and business confidence is already building the investment climate gets better. I feel as consumer it is about consumer confidence and I feel as that starts coming back, we are pretty confident that we will start seeing comparable sales get better. In terms of the down trading, we are seeing different behaviors in different quarters, for example in Q4 of last year, we saw that the eating out frequency went down and actually our share in key markets went up, because we did not lose as much as the eating out frequency went down. While in Q1 FY15, we found that the road side vendor growth was higher than the entire western fast food sector. Because one quarter is too early when you are doing research I think if you look at it from a six month to a nine month point of view clearly there is pressure for consumers to eat out and there is pressure on eating at western fast food.

Arnab Mitra Right. And the second question is on the cost side you have done a very good job of managing margins, just wondering how things like occupancy cost its almost been just about a percentage of two up year-on-year same with staff cost up only about 5%, so with the kind of 20% addition in stores how are you being able to manage these kind of cost which seem to be more fixed in nature.

Amit Jatia We feel that when we do our real estate deals we are very careful and clear about how we want to build that. So, I have mentioned before we do 20, 25 years deal so I have seen in other industries and other retailers when they do nine year deals and the deal comes up for renewal at that point in time many times they are forced to pay 50% to 100% rental increases. Whereas in our case it is during the tough times that our favorable deals really show up and help us. So because in most cases our rental increases are every five years, it helps us in the two, three years when the market is down. So, overall that has worked quite well for us and I would say that is the primary reason why we have been able to manage occupancy cost quite well.

The other thing is I have always maintained that when you are building a business like QSR in a market which is nascent. Your strategies have to reflect the realities of the market, so I have always maintained that let's say the government increases minimum wages by 40% and there is some impact on us, we believe that if you manage this right and work on it over a six or nine month horizon versus an immediate impact by raising prices to the consumer. We feel it helps both our value proposition to the customer and our ability to manage cost. So for example, we have been able to work out a bit of productivity growth on the labor side and we have used McDonald's international to help us in re-looking at our productivity, efficiencies and so on. Yet at the same time we have been able to sort of basically manage this much better through mostly productivity gains.

Arnab Mitra Just one follow-up on that so I understand on the staff side but on the rental side with 20% addition are you actually being able to see reduction in rent in some places because only then things can kind of remain almost flat.

Amit Jatia No, I do not think we see reductions but what we have definitely seen is the landlords being more realistic because of the current business environment, but also we have always maintained that when we always do deals that make business sense for us and during tough times people realize that when McDonald's opens a restaurant by an large they are there for the entire 20 years and we have found landlords coming to us because they know they can count on us to get their cheques on time and the fact is that their actual yield is better with McDonald's because they don't have vacancies then for a year, even if they have got better rents with somebody else. So actually to some extent our credibility is helping us but the real truth is that we have always been quite focused on the real estate deals that we strike.

Moderator Thank you. Our next question is from Hemant Patel of Axis Capital. Please go ahead.

Hemant Patel Couple of questions over here. In terms of breakfast and how it is actually occupying day parts, could you give us some sense in the traction on that and how many stores have you reached out with a breakfast menu, some insights on it.

Amit Jatia First and foremost breakfast we have got around 120 plus stores with breakfast now across our territory. Number two, what we are finding is that breakfast along with McCafé is becoming a pretty potent combination and we find that is building reasonably well because obviously it is a small base but we feel that the habit is slowly catching on, while we haven't yet gone with mass market on breakfast as yet in terms of television but pretty much what we are learning is that the combination with the coffee strategy is yielding decent results. Not yet at a scale that we want to, but it is encouraging us that the opportunity and the potential are quite substantial.

Hemant Patel Just to put it in another sense, I am trying to understand or gauge of how well the consumers have accepted breakfast and let's say stores which had breakfast for over a year or two something like that. Is there some comparable sales that you look at is it better than the overall general other day parts?

Amit Jatia Hemant we don't break up comparable sales by day part to be honest. However all I can tell you is from past experience if you look at our delivery business and we have seen this across the board in many parts of our business, even in-store for that matter. So since the launch of McDelivery in 2005, it has more than doubled as of today. So, what we find is that overtime our brand extensions continue to build as they get scale and as they become more visible to the customer. And what we find is we are quite confident that breakfast will find its own path in a similar manner, breakfast started only in the real sense in terms of its expansion around 2009-10. So we feel that we have to give it a few more years but the trends are in the right direction.

Hemant Patel Okay, fair enough. On the royal burgers and wraps if I would just put it as the new products that you have actually launched, are they gaining significant portion of let's say the restaurant revenues, are you seeing that actually scale up in a bigger way probably on the premium-end.

Smita Jatia So every time we do introduce a new product obviously the customer does see new news buzz and excitement and hence, you definitely do get an extra visit to the store and they do help in overall increasing the average store used units as well as also the customer spend. So as I mentioned that the premium burgers which is the Royal Burgers which we introduced they were mainly to cater to the customer need of filingness, variety, and taste and this was mainly for the young adults as well as for the parents. Thereby, by introducing it in the time when school holidays are there and parents are out with their children, definitely it helped give us the incremental visits.

Hemant Patel So if I were to just break this down into a pyramid and if I look at the royal and wraps said the premium end of your spectrum, and there is a mid-portfolio and then there is this entry level portfolio, has the premium end grown more significantly over the last two years?

Smita Jatia Yes, definitely that has been the intent to provide every customer a different portfolio of burgers by which their needs would be satisfied and hence, premium category was something which we started even with the launch of the spicy burgers and over the last three to four years there has been a very healthy growth of this entire premium category.

Amit Jatia Yes, we have been very encouraged with the way premium has grown and it has been rising as a percentage of our total products.

Hemant Patel Two more questions – one in terms of the earlier question that you answered on rentals, just wanted to understand what is the number of stores which are under revenue share rather than fix contract basis at the moment. Is it large and it is one of the reasons why we have seen the inflation not racking up as much as something like an increase in employee cost?

Amit Jatia No, Hemant we don't break it up but we always believe in a healthy mix and it is strategic because where I can do really great sales why would I also do as percentage of sales. Most people in the market thinks that is the answer to a good real estate deal, but I feel the right fix rental is also an answer to a great real estate deal. Because, a fixed rental as your sales grow remains fixed, while percentage will always remain as a percentage of sales. So we are very strategic about the portfolio, so for example we would handle a food court percentage or fixed very differently than we would for say a drive thru or a high street. And, we have learnt overtime how to manage the risk and maximize our potential so that is the best way I can answer that for now Hemant.

Hemant Patel Alright, just one final question on royalty, any guidance as to where this is going to go up as a percentage of revenue is for this year and next?

Amit Jatia So this year its 4%, it is already reported in the quarter results. Next year, it will go to 5%.

Hemant Patel Okay, I just noticed it is around 3.7%, so what it would be net including service tax and charges

Amit Jatia No, because it changed middle of the quarter, therefore it is around 3.7%

Moderator Thank you. Our next question is from Vivek Maheshwari from CLSA. Please go ahead

Vivek This is Vivek. Few questions first on the gross margins till the last month the news flow was not very positive, do you suspect some inflation on account of that or you think gross margins can still go up in the coming quarters?

Amit Jatia Like I said we want to say that our trends are moving in the right direction Vivek and we expect that to continue, however, quarter-to-quarter it is hard for me to give you a sense because we are dealing with agriculture and commodity. As I mentioned earlier sometimes even if an impact comes in we feel there is a smart way of managing that while maintaining value and building our margin back. So sometimes there may be a short term blip but long-term or even medium-term you will continue to see our margins move in the right direction. The second point I want to make is that over the last 15 years we have actually built a phenomenal supply chain and to give you an example, you can take lettuce which is a very sensitive crop, so over the last 18 years now we are growing lettuce in many geographies of India, and because we grow that in many geographies it's a hedge, so if somewhere there is a huge of rainfall the other region kicks in and these are things that are now beginning to yield results for us.

Vivek Sure. Second on the premium offering which you have launched, the Royal burgers that you have launched considering the week macro, why did you chose this time and not say perhaps next year where things would have been better on the ground?

Smita Jatia It is again what I just mentioned earlier that basically this is the quarter where we know that families are out and parents do look out for indulgent filling burger and that is the need and we see that even if they give one visit to the restaurant they want that filling indulgent burger and that is the reason why we had introduced the Royal burgers.

Amit Jatia Also Vivek it is about value for the product, so if you see the size of the product to its price point, at the end of the day it is value and I remember in 2008 when we launched our premium chicken nuggets we did extremely well with it so I feel the new news really drives the frequency and especially if it is a core product, it generally is quite well-accepted, at least for the customers who are coming in, they are okay with it.

Vivek Understood and last one would you be able to share how much would be delivery as a percentage of total revenues or that would not be possible?

Amit Jatia No we don't share the breakup but it has always been moving quite well for us but remember it is still a brand extension for us. We never expect to and what to be a delivery business, we feel that our core business is in-store and we believe that the added channel of delivery adds incremental gross margin, profits and margin contribution to the business. So it is growing well and it went through its rough phase but after we did certain changes from February we have seen some good results.

Moderator Thank you. Our next question is from Pulkit Singhal of Treeline. Please go ahead.

Pulkit Singhal I remember last quarter you mentioned about opening 70 to 100 stores every two year. Given the current run rate that I look for the last four to five quarters seems to be we are opening around 5 to 6 kind of restaurants, last year we opened more in 2Q and 3Q. So I am just trying to understand when do we see a pickup in the restaurants opening or is it traditionally that you open more in the second quarter and third quarter due to some reason or because at this rate we seem to be going at a lower than what you suggest.

Amit Jatia No, you noticed that in the last three years we have done the 30 to 32 restaurants every year. So you will find that quarter 2 and quarter 3 tend to be the highest restaurant openings and the other thing is that we have made a very big shift in our thinking around opening as I have maintained over the last two years is moving towards drive thru's. So even though drive through have a much longer lead time we have been able to make that switch without really losing on the volume of openings. So, we continue to maintain that 70 to 100 restaurants we will push for and we are quite confident we will get there.

Pulkit Singhal So just to understand for the drive thru there would be one restaurant already out there with a drive thru option so that is counted as one or two?

Amit Jatia One. So all the pictures you see in the presentation pretty much are drive thru pictures and many of these are recently opened so it is one, we do not count them as two. So even our dessert Kiosk or McCafés they are all one restaurant we do not count them as two or three.

Pulkit Singhal Okay, so this quarter how many drive thru did we add?

Amit Jatia Out of the 5, 3 were drive thru.

Pulkit Singhal Okay so we are counting them, so that is a restaurant plus a drive through option.

Amit Jatia Yes, and in fact last year almost one-third of our openings were drive thru's.

Pulkit Singhal Okay and so you are saying going ahead second quarter and third quarter could be a higher number.

Amit Jatia As always. If you see a trend you can see that in the investor presentation as well and if you actually draw this up for the previous year you will find the same trends.

Pulkit Singhal I know that you are very focused on the deals with these guys while opening the restaurants, do you think that is the reason why the opening turns to be relatively slower than what you initially expected?

Amit Jatia I do not think so, it about sustainability and the right quality of real estate. India is challenging when it comes to real estate and we are at McDonald's unlike some of our other QSR players, we want a good 3,500 to 4,000 square foot of prime real estate because remember I mentioned that we incur the complete cost when we open the restaurant but as we keep adding brand extensions like McCafé, McDelivery, dessert kiosk, play places for families, etc., as it all comes together, it size gives us tremendous advantage in the medium-to long-term. So you know the current portfolios of stores that are more than three years old are today healthily contributing to whatever cash flow that we have today. And that is what is allowing us sustain that and we need to continue to maintain that because is the fire power. Last point I want to make on this is remember McDonalds average store volume globally is the highest in the industry and we do right from breakfast all the way until even 24 hours. So that is the way we think and therefore real estate and the right size and the right quality makes a lot of difference. One very simple example, when we wanted to launch breakfast we could in 120 restaurants because we have independent operating hours as our term in every agreement. So even in a mall if we chose to we can open the restaurant for breakfast, so we think ahead is my point and therefore it is important to think ahead when you are dealing with something that is so long term like real estate.

Pulkit Singhal Right. So, in terms McCafé I think it was seven last quarter and now it is eight, just one has been added.

Amit Jatia No, it is not. I think we were at 6 and we are at 9 and you will continuously see because first you got to seeded so what we have done is we have gone to different types of restaurants and added different types of McCafes, there are two or three things we do within that. Now, the product line is stabilized and you can go to any McCafé and you will see how it is all doing. Basically you will see steady expansion plans in the coming months and you will see this number ramp up very quickly. This is how you will now be able to see the benefit of what I am talking about. So my point is that because our restaurants are enabled now that my model which opened in October and it takes us 6 to 8 months before the model gets stabilized. You got to get sourcing right, you got to get the cost structure of building a McCafé right, and we have done all that. So, now as we have said in our presentation steady expansion plans for FY15.

Pulkit Singhal Any kind of numbers to that steady plan for the next quarter?

Amit Jatia No, you will see it when we have the next call you will see where we stand on that.

Pulkit Singhal And in terms of this operational cost – rental and electricity so right now you are looking at year-on-year but when I look at Q-on-Q it was 605 in 4Q and now it is 679 so that is more than a 10% kind of a jump so what is the reason? I am assuming that is the right way of looking at it rather than Y-O-Y?

Amit Jatia No, because it is a seasonal business so you just cannot compare previous quarter. We always look at the previous year same period so to give you an example it was not raining in April and rains make a difference. We did not have Ramzan in February, holidays of children are in May so there are completely different dynamics and ball games and therefore in our business the correct way to look at it is quarter-on-quarter from the previous year.

Pulkit Singhal I am just trying to understand how much of the 679 is fixed cost?

Amit Jatia We don't break that up on a quarterly basis but yes, utility is an important part of that breakup. We have always maintained that is a challenging area and so utilities went up, so what we did is our design team got together and started working on what do we need to do from a design point of view, because there is no way I can negotiate utilities, there is no way I can change the unit structure. So we went into design and we started. So the new stores that are being rolled out have some efficiencies in there. So our philosophy is that if any impact has come, you absorb that and basically get it right and then roll it out with the new model in the future. So, utility is a big component of that obviously the other component in that is the occupancy cost itself.

Pulkit Singhal So you are saying utility went up quarter-on-quarter?

Amit Jatia We don't give that breakup on a quarterly basis, all I am saying is we have been able to maintain the total cost between quarter-and-quarter.

Pulkit Singhal What I am trying to ask is because we know and we keep hearing of power prices rising and all that so are we at a stabilized state for per unit power or are you still seeing increases?

Amit Jatia I can tell you for sure that in India there is no stabilized rate for power. There is no such thing in any area but the important point is that we have recognized that power cost and utility costs are going to rise and therefore we factor productivity growth already. So for example, as we are building our plans for FY16 we are already into the mode of thinking ahead, we are already thinking about what is the impact of utilities in the next year and what should we do from a design point of view that can allow us to manage it better. So we are conscious of the fact that utility is rising and what should we do from a design point of view rather than just increase menu prices.

Moderator Thank you. We will take our next question from Vikash Mantri of ICICI Securities. Please go ahead.

Vikash Mantri Just continuing on the McCafé. Are we looking at building independent McCafés and have we also provision for the five restaurants that we open this quarter, how does that work and also adding on to that question only. Given the logistical challenges limited in McCafé, will we have a more scared approach or this will be clusters?

Amit Jatia So first and foremost we do not do independent McCafés. McCafés work best when they work with McDonalds so that is our learning from rest of the world and we intent to follow that.

Vikash Mantri The five restaurants that open this quarter have they been provision for McCafes?

Amit Jatia Yes, all our new restaurants that are opening are being provisioned with McCafé wherever it is applicable. So for example, there may be a trading area where it is not applicable to start with so it may not be but (+90%) of our restaurants are enable to have a McCafé if there is potential to open a McCafé. And, yes we will not have a distributed strategy, for example all the nine McCafés that we have today are all in Mumbai and we found that in the last 18 years that is what works for us and we will continue to follow that approach.

Suresh L Just to clarify the new restaurants that we have opened in this quarter all of them are not in Mumbai so as Amit mentioned currently McCafé we are trying it out in Mumbai and as we get into those cities they have already been provision for and the McCafé model will be incorporated as we roll into those cities.

Vikash Mantri Okay, just another question on the gross margins. Can you give us a broad guideline of in the next two years or so how much further improvement can we think about?

Amit Jatia We do not give specific guidance around that. All I can say is that trend line wise it will trend towards high gross margins, we expect in the next two to three years this trend to continue.

Vikash Mantri Any numbers to this sir.

Amit Jatia No, sorry.

Moderator Thank you. As there are no further questions from the participants I now hand the floor back to Mr. Amit Jatia for closing comments.

Amit Jatia Thank you very much for participating in the call and we appreciate your time to attend and hear us patiently. I look forward to talking to you over the next quarter's earning call. If you have any further questions, please feel free to email Ankit, all his details are with you and we will be happy to answer any more questions if you have. Thank you.

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.