Q1 FY2018 Earnings Call Transcript – Aug 1, 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 Q1 FY18 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, Karuna. Welcome everyone, and thank you for joining us on Westlife Development Limited earnings conference call for the first quarter ended June 30th, 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. It gives me immense pleasure to be on this call today. I am extremely pleased to announce that all our strategic levers have yielded results and we have posted strong double digit total sales growth for this quarter. This also marked the 8th consecutive quarter of positive comparable sales growth that is 24 months of straight growth despite significant macroeconomic disruptions like demonetization and weak consumer sentiment. What has really worked for us has been our unwavering focus on building platforms rather than offering deals and promotions to retain our customers even during difficult times. The value platform has clearly emerged the star this quarter and our new Happy Priced Combos platform has shown excellent traction.

Building on the foundation of strong unit economics McCafé, McDelivery, Menu and brand innovation have continued to grow substantially and have yielded better than expected results. In fact McCafé's average daily sales have been the highest ever since its inception. All this has reinforced our faith in building a strong foundation to boost baseline sales. We are determined to continue this momentum. The company is working on evolving continuously to draw, retain and enhance our customer base. We have managed to grow our market share in all significant markets and have grown our geographic reach as well. We launched 3 new restaurants and reimaged/refreshed 8 restaurants in this quarter. We at brand McDonald's always believe in reinventing our consumer proposition continuously, to remain relevant to our consumers.

The launch of the experience of the future store, the new breakfast menu and the Happy Priced Combo are all a part of this exercise. Consumer response to our new reimaged stores, wholesome healthier menu option and sustainability efforts have been very encouraging. Customer first has always been the ideology of the company and we have reinforced this in the agility with which we respond to the needs of our consumers. In another bold step, we have used GST as an opportunity to make our pricing uniform across all our markets. McDonald's is the only organized sector brand that has changed its menu board to an all inclusive price with the mantra being 'what you see is what you pay'. Our consumers are absolutely loving it. We hope uniform pricing and the all inclusive menu boards will help enhance consumer trust on brand McDonald's.

ROP 2.0 has been a strong enabler for restaurant growth. It has helped us considerably in creating profitable stores. There is a strong focus on reimaging existing stores as it gives us a good return on investment. After the reimaging, our restaurants are offering a modern and contemporary experience with sleek interiors, digital menu boards, self-service drink machines and many more utility initiatives that have helped us optimize our utility cost. Based on all these initiatives, we have successfully managed to grow our margins through the quarter. I am happy to report that the cash flow grew by about 35% and also started the first quarter with a net profit. As our comparable sales momentum builds, we expect to see further expansion of margins and are confident that we are well on our way to delivering our target of vision 2022. I now hand over to Smita and Suresh to take you through the specific results for Q1.

Smita Jatia Thank you, Amit and good afternoon everyone. Please could you all move to slide #3.

As we started the new fiscal, we continued to build our business on our four strategic levers being broadening accessibility, growing the baseline, margin expansion and growth through people. Key focus areas for FY18 will be that growth remains a key priority. Growth will come from brand extensions, menu innovation, platform based approach and not deals and discounting. Thus, this will drive operational and sustainable profitability.

With the start of the year, we are very happy to announce our scorecards for the first quarter. We have achieved a total sales growth of 14% with 8 quarters of positive same store sales clocking 8.7% for this quarter, achieved a positive PAT of 2.2 million aided by a gross margin at 60.1% and an operating EBITDA improvement of 90 basis points. This leading to a cash profit increase of 33.8%.

If we now look at the quarter-on-quarter trends, the eighth quarter of positive comparable sales of 8.7% was on top of 3.4% last year same quarter. This is clearly showing that our baseline is increasing. Total sales growth is now moving back into the mid and high teens growth. Our restaurant base stands at 261 stores with major presence in the key cities of Mumbai, Pune, Ahmedabad, Bangalore, Telangana and Chennai. Our growth has come from platforms starting with the McCafé platform, we added 10 new McCafé, taking count of McCafé's to 121, driving robust sales and margin growth. We clocked the highest average daily sales per store in the quarter since inception.

On the delivery platform, we upgraded our website to give a better interface to the user as well as convenience to them. Both the app and the website drive more than half of our delivery GCs. Our partnership with third party aggregators like Swiggy is also helping in growth in deliveries and thereby providing convenience to our customers.

And finally, we rebuilt our everyday value platform supported with very strong consumer insight. The customer now has flexibility in choosing his or her favorite product and bring at a value price. At the same time, we added new news with a Kebab burger and a wrap again at a value price. This helped in getting trials to the brand and new customers into the fold.

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

Suresh L

Thank you, Smita. Thank you all for joining us on this call. I will now take you through the financial performance for the first quarter ended 30th June 2017.

As regards the top line growth, the financial performance has been very heartening across all the line items for Q1 FY18. We reported our strongest comparable sales quarter in over 4 years by delivering a robust same store sales growth of 8.7% in Q1 FY18 compared to 3.4% in Q1 FY17. We grew the sales by 14% in this quarter. Increase in sales has been largely led by increase in footfalls across our restaurants and our continued work around expansion of McCafé and contribution of MDS coupled with addition of new restaurants.

Overall, we are very encouraged with the sales momentum coming back in our business and with the kind of start we saw in Q1, we have strategic levers in place to deliver better sales performance in FY18 compared to the previous years. On gross margins, our continuous work around driving better product mix management aided by McCafé, product line extensions and menu innovations driven by our new value platform along with other usual levers of menu price hike & supply chain efficiencies etc. ensured that we remain stable at 60.1% gross margin in Q1 FY18 compared to Q1 FY17.

The restaurant operating margin saw an impact of 30 basis points largely on account of higher payroll and employee expenses impacted by hike in minimum wages coupled with lever augmentation which we carried out over the last 12 months to gear up for overall pickup in demand and sales growth. This was partially offset by ROP 2.0 restaurant led efficiencies across utilities expenses which augurs well from a foundation standpoint. We have been able to drive leverage across G&A in Q1 FY18, therefore largely on account of lower G&A expenses, we have seen an improvement of 90 basis points in our operating EBITDA margin this quarter. The operating EBITDA margin for the quarter stood at 5.6% compared to 4.7% in the same quarter last year.

The slide 16 is a graphical representation of the operating EBITDA improvement in Q1 FY18 driven by the levers which we just discussed earlier. Lastly, we declared profit of 2.2 million in Q1 FY18 compared to loss of around Rs. 21 million in the same quarter last year. This resonates well with our target of being PAT profitable in FY18.

Moving on to slide 17, it is quite encouraging to showcase our progress and commitment to drive better cash profit year-on-year as we move towards our journey of having profitable growth every year. Our hard work around driving efficient capex and opex largely led by ROP 2.0 restaurants and improved EBITDA margins, we have been able to almost double our cash profits over the last 24 months and we registered a healthy increase of ~34% in cash profits in Q1 FY18 compared to the previous year same quarter.

Lastly, we shall continue to build on our strategic initiatives & progress which we have embarked up on with an encouraging start to FY18 to help us deliver better profitable growth in this year and moving forward.

With that said, I would now hand over back to Amit who would take you through strategy and outlook for FY18 and beyond and give the closing remarks.

Amit Jatia Thank you, Suresh. From a broader consumer environment perspective, we see an overall uptick in the consumer sentiment. Our focused efforts on menu innovation and providing everyday value to our customers has resonated well, which is helping us to strengthen brand affinity. We remain committed to being the most accessible brand and therefore focus on bringing additional footfalls to our existing base of restaurants while opening 25 to 30 new restaurants in FY18 to serve future demand. We stay on track to take our restaurant footprint to 450 to 500 by 2022. We shall keep our focus on strengthening our brand by catering to local preferences and providing our guests with a superior McDonald's experience through our experience of the future restaurants.

To conclude, our pipeline for growth is strong and we have various initiatives under test for future growth. The idea is to make sure we remain connected and relevant with the fast evolving consumer. We believe our consistent and long term approach will help us accelerate momentum and positions us well to deliver significant profitable growth to our shareholders.

With this said, I open it up for question and answer.

Moderator Thank you very much, sir. Ladies and gentlemen, we will now begin the question and answer session. First question is from the line of Abneesh Roy from Edelweiss. Please go ahead.

Abneesh Roy Sir, this 8.7% SSG, how much of this is favorably impacted because of the early sale season by the fashion retailers and what portion of your stores are in the mall. Also, with higher focus on Swiggy, Zomato etc., how much you are getting aided by that, if some numbers you can give on that, it will be very helpful.

Amit Jatia Yes. Most of the data we do not share. But all I can tell you is that it is our 8th quarter of consecutive same store sales growth and this is on top of the 3.4% that we had in Q1 last year. So we feel this is based on platforms and foundations rather than early end of season sale. Of course that helps, but basically we focus at McDonald's on building baseline sales and when you deliver sort of the 8th quarter which is 2 years in a row, what you are doing is on top of the 3.4% same store sales growth last year, we added another 8.7% on top of that. And that we have been doing consistently. So I feel that these are platforms that are working, rather than shifting, that happens every year, sometimes Ramzan this year shifted a bit early which had its impact on business as well because typically Ramzan takes your business a bit down. Answering your second question on Swiggy, Zomato, we do not share the breakup of that. But essentially I have always maintained that we are an open platform. It is like seeing McDonald's in any mall. So we like to be as accessible to our customers as possible and wherever customers are shopping, even for food to be delivered to their home, as the McDonald's platforms evolve, it is more opportunity for the consumer to order McDonald's and that is what working for us because delivery continues to grow at the same pace it has been growing in the last 2-3 years. So that has also worked quite well for us.

Abneesh Roy Sir, 5 quarters back also you saw 8% plus same store growth but then the next quarter it was just 3.4% growth. Now in July because the sales season was preponed in June, obviously July will see impact and there is GST related issue also. So in Q2, can your SSG again come down. So are you confident that this recovery is structural or it is more of the base effect, of course 3% was there in the base but how do you see in terms of recovery for the coming quarter and then the balance of the year?

Amit Jatia See first and foremost comparable sales are called comparable because they are compared to the last quarter of the same period, not necessarily to the previous quarter or the next quarter. So the fact of the matter is that therefore the 8.7% cannot be compared to 1% last quarter. You know, while I do not want to talk about the future quarter, what I want to say is the previous year, we had 8.4% in Q4 of FY16 and in Q4 of FY17, even after demonetization in that specific quarter we had 1%. So having delivered effectively 2%, if you take that extra day of February out, I think it is called baseline building where even with demonetization we were able to grow same store sales. So I would say the same thing holds truth for the next quarter. Obviously, GST is again a major disruption and one is going to see how that will impact business in the future. As I have said, we maintain that mid-to-high single digit is roughly what we think we want to consistently deliver from a market point of view.

Abneesh Roy Sir my second and last question is on the expansion, you have plans for 25-30 restaurants in FY18. Q1 you have done 3, so wanted to understand are you confident of meeting that. Second sir, if you see some of the pizza players have cut down drastically their expansion plan. So in that context would you like to increase your expansion plan or we would also take some learning from there that now maybe next 2-3 years demand is a bit slow, so let us not expand too much, let us try to do it from the existing stores.

Amit Jatia See, we have always followed a consistent strategy and we don't tend to follow other people, we keep our eyes open on what is happening in the market place. If you look at the history of every conversation we have had, I maintained that McDonald's focuses on sustainable growth and therefore we sustainably grown at 25 to 35 over the last 3 years. We have neither gone to 70 and then come down to 30 nor have we gone to 20 and then gone to 30. We believe for the current frequency of eating out in India and for the current circumstances, our strategy of 25 to 35 works for us. We continue to invest very heavily in reimaging and opening 40-50 McCafé's a year. We are quite confident of delivering our vision of 2022 that we stated and like I said we follow our own thoughts and we evaluate the market based on market data that we do in terms of lot of research. So you will continue to see 25-35 restaurants from McDonald's.

Abneesh Roy And only 3 was because of some bunching up malls or what is the issue?

Amit Jatia See, the way I see the store opening it is a capital thing. It is not a revenue thing. So what happens is I do not look at quarter-to-quarter openings in terms of stores because there are malls, they shift, sometimes mall shift by 6 months. Sometimes things come in early. The important thing is if you look at last quarter as well, we had our ups and downs but net-net we delivered the 25 stores. Similarly, this year we are confident of delivering anywhere between 25 to 35 stores. The point is that just for the pressure of 30th June, we do not want to open where mall is not ready or we do not want to open a restaurant where other retailers have not come into play and so and so forth. So the important thing for us is to do the right thing.

Moderator Thank you. The next question is from the line of James Sheridan from Bay Capital. Please go ahead.

James Sheridan Couple of questions if I could. First of all, I assume that not much of the 8.7% same store sales was coming from price, can you just outline whether there was anything unusual about pricing activity in this period that would enhance further?

Amit Jatia In fact, Jim it has been the lowest price increase, the last price increase we took was very minor in January 2017, so this quarter there was zero price increase effectively.

James Sheridan So even stronger, that is interesting. On page 15 of the restaurant operating margin performance, you talk about a hit of about 30 basis points, a lot of this coming from this previously identified payroll and employee expense number, I wanted you to talk a little bit about that because I am surprised to hear that. I am looking at inflation generally coming down the country, so I wanted to understand why labor expenses are coming back to be a problem. But more importantly, can you talk about ROP 2.0 and how many units you have now converted. How many more do you have to convert, I thought it would have added more to the restaurant operating margin performance. Can you just talk about that roll out? Could you talk about 2.0 roll out, is it now half way through and we are not seeing the profit that we should have seen. Can you just talk about those two offsetting factors?

Amit Jatia Sure, Jim. So firstly ROP 2.0 is working extremely well for us. Our base of new restaurants as I mentioned in my last call, all of last year had positive cash flow versus FY16 and FY15 having negative cash flow. So that is working extremely well for us. The learning out of ROP 2.0 continues to be implemented in older stores. Obviously, it takes time because it involves lot of capital work that needs to go into the restaurant and it is an operating restaurant. So we in fact, as you will see that in the occupancy and other operating expenses, we have actually been able to get a pretty good gain and that all stands from a lot of these things that I have just talked about and there is a way to go on that. So we do expect to see continued gains coming out of the ROP 2.0 platform other than the fact that it is allowing us to opening these stores profitably to start with. The labor thing was more a minimum wage impact that came which I talked about in the last call as well and essentially as I had mentioned in many of my calls while the utility has been a big challenge for us in the past and through ROP 2.0, I think we captured that aspect. In fact, utility has been a big factor in offsetting some of this gain. So the problem with payroll is that we cannot deal with it in a short term basis and we are quite confident that we have initiatives in the pipeline that is working on labor initiatives at this point in time, but it is a challenging area for us and we think that over the next 2 to 3 quarters we might be able to sort of get a better handle of that. However, we are quite confident that we will overcome that with continued same stores sales growth and as the ROP 2.0 platform continues to roll out into older restaurants as well.

James Sheridan Okay. Then a general topic of GST, you talked a little bit about this simplification pricing, I didn't realize that was an issue across the country. So I was interested to hear in details how GST is impacting you and then may be a general comment from the macro perspective as a businessman operating in India, how do you feel about the implementation of GST so far?

Amit Jatia So I feel the GST is a good reform and we are generally quite pleased with it because it has made administration and our life much easier. I think in the more medium to longer term, we will see logistics benefits. But we think that we can do more also with movement of goods, remember we do chilled, frozen and dry. So for us logistics is extremely important and we think that the time that we are going to save in movement of goods is going to sort of come back to us as a big benefit over the next 6 months or so. Meanwhile, the good thing for us is that one uniform tax and McDonald's is the only brand at least in the QSR space that has gone price inclusive of GST that shows our faith in what the government is trying to do as well, but the customer feedback on trust is fantastic because we have always been getting demand from the consumer that what they see is what they want to pay and we took this bold call and the feedback that we have with us is pretty good. However, with any major reforms it is not that from day 1 everything works smoothly. I do believe that you got to give time, just like demonetization which was even more severe, you got to give like a quarter to settle down. The fact is demonetization was a big event and if liquidity is out of the system, the fact that on top of 8.4% if you deliver even a 1% comparable sales, while if you look at the rest of the industry, I thought we did a pretty phenomenal job. Similarly I feel that GST will have a short term impact. We have seen that from its implementation in Australia, Malaysia and other markets. It is hard to tell what that might be, but foundationally, I feel that the brand is quite well entrenched in what I am seeing right now, I am quite confident we will overcome that and I feel the consumer sentiment is looking good. So I am quite confident of sort of moving in the direction that I talked about maintaining at least mid to high single digit same store sales growth.

Moderator Thank you. Next question is from the line of Avi Mehta from India Infoline. Please go ahead.

Avi Mehta I just wanted to understand this quarter, despite a very strong growth in McCafé, gross margins are flattish. Any reason for this and if you could kind of just share your comments on that?

Amit Jatia Avi, it is 3 months. So you know something up or down, some commodity, slight impact here or there. The important thing is quarter-on-quarter you are going to see the benefit. So if you just give us few more quarters, you will continuously see that. Also, we do not like to do knee jerk reactions. We are here building a sustainable business and a preferred brand for the consumer. So for example right now onion and tomato prices are up and down. McDonald's does not change its price just because for one month tomato prices have gone up or down. We deal with it in a different way and we work with our suppliers and build contingency and we ensure that next year the impact will be even lower. So we have good experience with managing all that. So do not focus on just the quarter alone. I am quite confident you will see benefits in the coming quarters.

Avi Mehta Okay, perfect. That is good to hear. And second is you have indicated that there is a sentiment improvement that you have highlighted. If a) I am assuming uptick in consumer environment, is that correct, can you kind of clarify it and b) given this kind of trajectory in terms of SSSG growth that you now consistently delivering, how should we look at a medium-term margin guidance, would you still say a mid double digit kind of endeavor is what you would kind of like to be, any number you could share on that, that would be helpful in the medium terms?

Amit Jatia: See, the first thing if you heard my opening commentary, that happy price combos have played a huge role for us in going beyond the normal delivery of say mid single digit comparable sales. So we feel that if you recollect, we had the happy price menu for many years and along the way as I had mentioned that in the industry people had caught up with our value platform and we have basically reinvented this and we had done this test last year in couple of our markets and the results we got out of the test was good enough for us to execute this across the board. So I feel that has been very helpful for us. I think I can see positivity in the consumer side. This is a feeling, it is hard for me to give you any data for it. But I do expect a short term or slight impact in the coming quarter, it is just a thought while it may or may not pan out. But trajectory wise, I see it getting better. So I will give you an example. In my October call, I had said that I can start seeing consumer sentiment move well. Then of course demonetization came and I had mentioned that it is going to take at least a quarter and I sensed at least based on what data we were seeing and through our consumer footfalls we were able to evaluate, that roughly by April things will start getting better. So it panned out for us that by April things started getting better. Other than the GST bit, I do see consumer sentiment get better. So if I were to leave short term out, if I were to leave out the quarter to quarter thinking, I feel we are moving in the right trajectory with consumer sentiment.

Avi Mehta Okay and sir the medium term like FY22, you have indicated strong store addition guidance, is there a similar guidance you could share on margins and similarly on ROCEs, you have been also doing a lot of work on reducing your capex per store. So any guidance on both these metric would be useful?

Amit Jatia Sorry, I missed the margin question. We feel that as the operating leverage is playing out, as you can see, if I look at over 22 months in the same quarter, we have doubled our cash flow. So we feel that this trajectory will continue which is why I have confidently said that we are not doing capital raises to fund our expansion. We are quite confident and, in fact in this quarter we have actually brought our gross debt down. Even though we are net cash, we do maintain a little bit of debt as well. So our cash flows have been strong enough for us to pay back and remain in the positive cash territory for the quarter. So we have also sort of given an indication that we think that the SSG will aid our operating margin expansion. I want to resist from giving you a specific number that is what you are looking for. But all I can tell you is that we feel confident about moving forward with margin and maintain the sort of cash flow growth that we have seen in the past.

Avi Mehta Even on the capex front, is there a number you could share now sir, how is the ROP 2.0 playing out?

Amit Jatia ROP 2.0 is the reason we are able to consistently deliver store openings. I think ROP 2.0 has just absolutely converted our ability to keep the growth moving forward. For now, the focus is not to reduce further cost. Our first focus has been to take the elements of the experience of the future restaurants and like we did with McCafé, where the first McCafé we built was for about 7 million. But by the time we started accelerating its rollout, we were building it for Rs. 2.5 million. That is McDonald's for you. So when we will first implement a concept, it will be world class and global standards and then we spend 3-6 months in localizing the elements and right now our focus is to ensure that we can bring the cost of experience of the future stores to a level where a big base of our restaurants can be part of that. If you go online to check McDonald's Nariman Point store and some of our other EOTF stores, the customers are speaking for themselves on how they love the concept and it clearly tells me that is where we need to put our energy to keep the cost structure right to grow. And therefore with ROP 2.0, the whole idea is to maintain that cost, not let it go up. The idea is not to focus on bringing that down any further. But the idea is to take EOTF elements and making sure the cost is affordable for us to grow that. I hope you get the context of what I am saying.

Avi Mehta: Yes. I get it sir. The focus is largely on driving growth in brand extensions and other innovation investments and let the margins be derivatives, that is the way I see it.

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

Umang Shah So, I just wanted to ask you one question, that you said that you are going to increase the footfall on your restaurants. Now clear trajectory is that you are focusing on developing customer interest in your restaurants. But how many more restaurants you are going to renovate, I missed that part and any other initiatives apart from restaurant renovations?

Amit Jatia The whole idea is today we have a pretty good store base that is modern and contemporary because of the last 3-years work we have done on reinvesting and reimaging even though the consumer sentiment was tough, I would say 60%-70% of our restaurant today reflect today a contemporary platform. I am just trying to think roughly around 20 restaurants we are reimaging every year. So we feel that in the next 2-3 years, we will be up to date with the older restaurants being converted to today's platform and then of course the cycle continues because the restaurant that we first reimaged, will come back in the cycle. So I do not know if that answers your question but roughly 20-25 restaurants a year is what we are reimaging and when we reimage, we add a McCafé as well.

Umang Shah Right. Sir my question was more concentrated towards how are you looking at increasing the footfall in your restaurants?

Amit Jatia Footfall is all the reasons I have just given you earlier, primarily value plays a huge role in footfalls. So that was the reason of good traction in the last quarter in terms of footfalls. Like I mentioned earlier on my calls, that McCafé has been a new occasion driver, the delivery business is another new occasion because if people do not want to go out, I would have lost that business otherwise. But we are able to get that business because we have a strong delivery platform. So we are increasing footfalls on account of all the things I talked about, outside of which we do line extensions, like Mexican Aloo Tikki, the Piri Piri Fries, for example last quarter again the

Chicken Kebab Burger was a new addition to the menu and that drives new news to the consumer which again drives footfalls back into the restaurants. So it is a circle. All of these things together are what driving footfall to McDonald's.

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

Sanjay Singh Just wanted to know what will be the capex for this year?

Amit Jatia It would be the same between 100-120 crores.

Sanjay Singh So do you think we should be able to manage with the cash flow or it would amount to some amount of debt?

Amit Jatia Like I said so far, we have remained positive cash. So we are able to manage it. So we are working very hard to ensure that we do not go with debt. So we want to remain maximum 10-20 crores of net debt. So that obviously tells you that we are working very hard to drive cash flow up.

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

Latika Chopra The first question is on your breakfast menu, how many stores are offering that today and how do you see the expansion going forward?

Amit Jatia So the new breakfast menu is being offered largely in the Mumbai and Pune market at this point in time. So it would be around 60-70 stores. Like I said, 2013 McCafé was where breakfast is today. We think breakfast is a tougher business but we feel that as we have seen in other emerging markets, it is a rock solid business to really focus on. So we think over the next 2-3 years, breakfast will take the role that McCafé is playing today. Therefore we have seeded it in most stores in Mumbai and Pune. The idea is over the next 1-2 years to expand that across the rest of our markets.

Latika Chopra And how many stores on an annualized basis you will be adding this to?

Amit Jatia We are working on market by market, so like I said this is more sort of pipeline stuff. As such we have breakfast in about 120 restaurants, of which maybe 60-70 would have the new breakfast platform. The new breakfast platform is settling quite well and by end of the year, the target is to expand this across more markets. Because, only when we get scale then we can start advertising and we can start building the day part.

Latika Chopra And just one check, the price increase that you took in January was that about 2%-3% or was it less than that?

Amit Jatia Slightly less than that. We have done quite well on price increases. We have not taken too many increases and yet we have been able to expand our margins with it.

Moderator Thank you. The next question is from the line of Amar Kalkundrikar from HDFC Mutual Fund. Please go ahead.

Amar K Sir I have just one question. What have been the price changes in menu post GST? As I can see some of the happy price SKUs have actually seen 4%-5% price reduction. So how have we gone about it and what has been your rationale for those calls?

Amit Jatia See, basically the happy price combo we look at that as a menu in totality, of course in many places where taxes have come down we have given the benefit to the consumer. So we followed the directive that we got. But we have ensured that in doing all this, we have tried to maintain the value of individual products, so we do a lot of research around price sensitivity. So we have used a lot of modeling and we combine that with GST together to change the menu prices. Even if you look at our menu boards, we are changing that completely too as we have gone to digital menu boards and the menu is now more day part driven rather than just the same menu board being there across the whole day. So there is a lot of art and science in there and there is a lot of opportunity to benefit both the consumer and us. It is a big exercise, hard for me to give you any specifics. But essentially we try to ensure that every product has a certain value rating for the consumer and that is done based on our research.

Moderator Thank you. We take the next question from the line of Mayur Gathani from OHM Portfolio. Please go ahead.

Mayur Gathani Sir, just wanted to check what is the cost for the refurbishment?

Amit Jatia Now it depends on store to store because that is a hard number to give because it depends on the age of the store. So there is no real specific number to that.

Mayur Gathani Okay. And on the new wage bill, where the center is supposed to bring this bill to the parliament, how would it impact us because you have been talking in the last 2-3 quarters about the state governments increasing the minimum wages. Now it will become the uniform all through the country. Where do we stand?

Amit Jatia I have to yet examine what that exactly means for us. But we believe that labor is a key cost item that we need to reinvent ourselves for the future. As we did in 2 years ago with ROP 2.0 where we fixed both labor and utilities, we are quite confident that we have enough work in the pipeline around looking at how we can grow productivity to offset for this labor increases that are going to come. So it is going to remain a challenge for us over the next 2-3 quarters. But I feel in the medium term we will be able to overcome that through our design work.

Mayur Gathani So can you give us an average wage per employee, what is it like?

Amit Jatia No, we do not share that details, but you know the minimum wage and is different state by state. So it is hard for me to give you are specific number.

Mayur Gathani And the number of employees today?

Amit Jatia About 8,000 employees.

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

Bhavesh Shah Sir my question is that if you look at on a sequential basis that is 4Q of last year versus 1Q of this year, our store level margins have remained more or less flat and despite a big pickup in the SSG in the current quarter, so can you just share some thoughts here?

Amit Jatia It is hard to compare that with quarter-to-quarter because of business is seasonal and there are some quarters that are down and there are some quarters that are up. Fact of the matter is that yes, there are some impact that we got because of labor which has taken us a little bit longer time to recover but foundationally all the efforts around utilities and some other line items have worked in our favor. We are hoping that in the quarters that you will see moving forward, you will see the flow through and the operating margin come below. But we are saying that net-net operating margin and operating EBITDA we have to grow quarter-on-quarter. So I am quite confident that next quarter and the quarters ahead, you will be able to see the flow through as we maintain our SSG particularly.

Bhavesh Shah And secondly sir, could you give some thoughts on royalty payment for FY18?

Amit Jatia 4%. Same as last year.

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

Manjeet Buaria I have just one question, in the opening remarks you mentioned that you gained market share and I am not aware against what to benchmark this market share, so if could you just explain that once?

Amit Jatia We have a global research that we do across all our key cities and therefore we understand what is the eating out frequency in that market. So let us say Mumbai would have a specific eating out frequency and we look at our market share and our competitor market share against that frequency. So that is something that we track and we do not share that data but typically it is moving in the right direction for us and that is what I meant by that.

Manjeet Buaria Sure sir. Without sharing any numbers, could you just explain us to what is the peers that you look, is it only burger chains or pizza chains, what is the peer set basically when you compare this?

Amit Jatia We look at the eating out frequency for WFF i.e. Western Fast Food, Coffee Shops and Indian Fast Food. So we look at that. And then, we look at our shares against every player then in the Western Fast Food business both against eating out in totality and within Western Fast Food category. It is a private research, we have been doing it for last 20 years basically.

Moderator Thank you. The next question is from the line of Manish Poddar from Renaissance Investments. Please go ahead.

Manish Poddar Amit, can you just call out the SSG for restaurants with or without the McCafé additions?

Amit Jatia We do not break up our comps.

Manish Poddar Because last year about 35% of the outlets have McCafé and now about 50% of the outlets have McCafé.

Amit Jatia It is growing, average volume is also growing, but net-net we still don't break out our same store sales growth by individual platforms.

Manish Poddar Okay. What sort of additions are we looking in McCafé, let us say going ahead?

Amit Jatia McCafé as we have said, one, we are on track to deliver what we had promised, 140-150, we are already at 121. Typically we are adding about 40 McCafé's a year. So the whole idea is we have to add about 40-50 McCafé's a year.

Manish Poddar So 40-50 for the next 3 years probably, right.

Amit Jatia Correct.

Moderator Thank you. Next question is from the line of Rohit Lala from Centaur Capital. Please go ahead.

Rohit Lala So my first question is, can you give a breakup of what is the revenue from delivery as a percentage of total revenue?

Amit Jatia No, we do not share the breakup of our brand extensions as a part of our total revenue, unfortunately.

Rohit Lala Sir my second question is how many of our stores are present in airports because we are witnessing very high passenger growth equal to 20%, so I wanted to understand the numbers if you can say?

Amit Jatia So, you see while the passenger growth is high, there are other aspects around. So we have one restaurant in Hyderabad at the airport.

Rohit Lala Okay and any plans to put out the brand in multiple airports just for visibility?

Amit Jatia We do not do things for visibility but it should make financial and business sense because you know airports while they have footfalls, they have their own peculiarities and therefore it is not necessary that because you are at the airport, financial and unit economics makes sense. So we are pretty careful. We talk to them all the time, because I think as a good food operator and most airports would love to have us. If it makes business sense, then we will get there. If it does not we will not.

Moderator Thank you. As there are no further questions from the participants, I would now like to hand over the floor to Mr. Amit Jatia for his closing comments. Over to you sir.

Amit Jatia Just wanted to say thank you for being on the call today and for all your questions and patiently listening to us, we appreciate it. Thank you.

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