

Westlife Development

13 June 2020

Reuters: WEST.BO; Bloomberg: WLDL IN

Near-term uncertain; Medium term vision stays strong

Westlife Development (WLDL) continued to deliver an encouraging performance in 4QFY20 till Feb'2020 (SSSG for Jan-Feb'2020 stood at 12.3% with sales growing by 20.3% YoY) but was impacted by Covid related lockdown in March. WLDL's 4QFY20 topline declined by 0.9% YoY to Rs3.4bn (est. 6.5% growth to Rs3.6bn) as SSSG declined by 6.9% YoY (est. flat SSSG). Gross margin expanded by 210bps to 65.6% (est. 66%). High employee cost as a % of sales (+190bps YoY) along with increase in other expenses as a % of sales (up 250bps YoY) led to EBITDA margin sharply contracting by 230bps YoY to 5.5% (est. +120bps to 8.5%). Restaurant operating margin (RoM) stood at 10.8% (down 280bps YoY). EBITDA declined by 30.4% to Rs185mn (est. 23.8% growth to Rs307mn). The company reported a loss of Rs50mn at Recurring PAT level (est. Rs107mn profit). In 4QFY20, the company made provision of Rs166.3mn towards write-off for food inventory and related onerous commitment as an exceptional item. WLDL added 4 new restaurants during the quarter (number of restaurants as of FY20 stands at 319) and extended McCafe's to 5 new restaurants (reaching 223 restaurants till date; 70% presence now). While there are near term growth concerns for the sector, we remain structurally positive on the stock and retain Buy rating with a revised target price (TP) of Rs350 (Rs375 earlier) based on EV/EBITDA multiple of 24x (on FY22 EBITDA), below our pre-Covid multiple of 28x.

FY20 performance (ex-IND AS impact): Sales, EBITDA and Recurring PAT grew by 10.4% (led by SSSG of 4%), 15.8% and 71.8% YoY, respectively. EBITDA margin expanded by 40bps to 9.3%. RoM stood at 14.6% (up 20bps).

Outlook and valuation: Overall operating environment will continue to be weak in the near term for the QSR sector at least for the next two quarters with higher impact on dine-in sales and recovery would be gradual. While the company has taken various initiatives to continue its non-dine-in business, it won't be enough to compensate for the sharp decline in dine-in (~50% of sales). We revise our earnings downwards by 54.6%/15.4% for FY21/FY22 due to a sharp cut in SSSG and the corresponding cut in EBITDA margin (due to lack of operating leverage) for FY21. WLDL's focus on value platform, superior performance of brand extensions, continuous menu innovations and high focus on customer initiatives make us believe that the company can actually gain market share in the current environment and eventually achieve a sustainable high single digit SSSG once the market condition stabilizes. Improvement in gross margin and operating leverage beyond FY21 should lead to sharp improvement in operating margins. On operating margin front, the company eventually aims to get back to the previously guided trajectory for FY22. WLDL will take a pause on store expansion at least till 1HFY21 after showing decent aggression last year. We remain structurally positive on WLDL from a medium to long term perspective and thus retain our Buy rating with a revised TP of Rs350 (Rs375 earlier) based on EV/EBITDA multiple of 24x (on FY22 EBITDA), below our pre-Covid multiple of 28x.

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BUY
Sector: Quick Service Restaurant

CMP: Rs297

Target Price: Rs350

Upside: 18%

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Key Data

Current Shares O/S (mn)	155.6
Mkt Cap (Rsbn/US\$m)	46.5/613.4
52 Wk H / L (Rs)	500/257
Daily Vol. (3M NSE Avg.)	371,321

Price Performance (%)

	1 M	6 M	1 Yr
Westlife Development	2.7	(14.8)	(7.1)
Nifty Index	7.7	(17.3)	(16.8)

Source: Bloomberg

Y/E March (Rsmn)	4QFY19	3QFY20	4QFY20	YoY (%)	QoQ (%)	FY19	FY20	YoY (%)
Net sales	3,393	4,329	3,364	-0.9	-22.3	14,020	15,478	10.4
COGS	1,239	1,472	1,158	-6.5	-21.4	5,116	5,382	5.2
% of sales	36.5	34.0	34.4	-2.1	0.4	36.5	34.8	-1.7
Gross margin %	63.5	66.0	65.6	2.1	-0.4	63.5	65.2	1.7
Employee costs	378	428	437	15.7	2.1	1,453	1,690	16.3
% of sales	11.1	9.9	13.0	1.9	3.1	10.4	10.9	0.6
Other expenses	1,511	1,908	1,584	4.8	-17.0	6,209	6,966	12.2
% of sales	44.5	44.1	47.1	2.5	3.0	44.3	45.0	0.7
EBITDA	265	521	185	-30.4	-64.5	1,243	1,439	15.8
EBITDA margin %	7.8	12.0	5.5	-2.3	-6.5	8.9	9.3	0.4
Depreciation	210	222	220	4.6	(1.3)	797	866	8.6
EBIT	55	298	-35	-	-	445	574	28.8
EBIT margin %	1.6	6.9	-1.0	-	-	3.2	3.7	0.5
Interest expenses	49	34	31	-36.8	-8.0	177.3	148.5	0.0
Other income	12	45	-14	-	-	84	69	-18.1
PBT	18	310	-80	-	-	352	494	40.4
Tax	5	82	-29	-	-	139	128	-8.1
Effective tax rate %	27.8	26.6	36.7	8.9	10.1	39.5	25.9	-13.6
Recurring PAT	13	227	-50	-	-	213	366	72.0
PAT margin %	0.4	5.2	-1.5	-	-	1.5	2.4	0.8
EPS	0.1	1.5	-0.3	-	-	1.4	2.4	71.8

Source: Company, Nirmal Bang Institutional Equities Research; Excludes IND AS 116 impact

Please refer to the disclaimer towards the end of the document.

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
Net revenues	11,349	14,020	15,478	12,626	17,195
YoY growth (%)	21.9	23.5	10.4	-18.4	36.2
SSG	15.8	17.0	4.0	-20.6	30.0
EBITDA	755	1,243	1,439	1,232	2,211
EBITDA margin (%)	6.7	8.9	9.3	9.8	12.9
Recurring PAT	167	213	242	207	897
EPS (Rs)	1.1	1.4	2.4	1.3	5.8
YoY growth (%)	(237.4)	27.8	71.9	-43.5	334.0
RoCE (%)	1.1	5.8	7.3	3.1	14.0
RoE (%)	3.1	3.8	6.3	3.5	14.0
P/E (x)	327.8	226.5	126.3	223.7	51.6
P/BV (x)	10.1	8.3	8.0	7.7	6.7
EV/EBITDA (x)	73.9	39.7	32.3	38.0	20.8

Source: Company, Nirmal Bang Institutional Equities Research

Note: Excludes IND AS 116 impact

Exhibit 2: Our estimates versus actual performance

Y/E March (Rsmn)	4QFY19	3QFY20	4QFY20	YoY (%)	QoQ (%)	NBIE estimate	Variation (%)
Net sales	3,393	4,329	3,364	-0.9	-22.3	3,612	-7%
EBITDA	265	521	185	-30.4	-64.5	307	-40%
EBITDA margin (%)	7.8	12.0	5.5	-2.3	-6.5	8.5	-3.0
Recurring PAT	13	227	-50	-	-	107	-147%

Source: Company, Nirmal Bang Institutional Equities Research

Excludes IND AS 116 impact

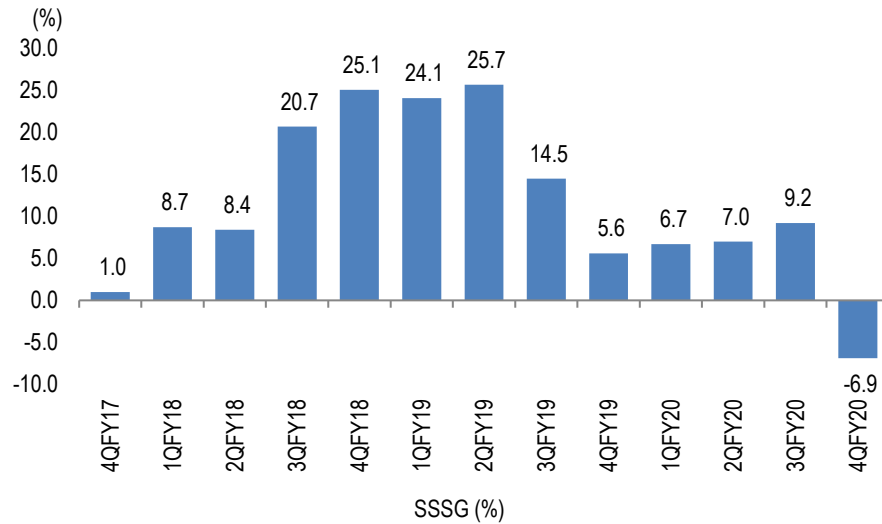
Exhibit 3: Change in our estimates

Y/E March (Rsmn)	Old estimates		New estimates		Change (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Net sales	16,906	20,200	12,626	17,195	-25.3	-14.9
EBITDA	1,789	2,586	1,232	2,211	-31.1	-14.5
EBITDA (%)	10.6	12.8	9.8	12.9	-0.8	0.1
Net income	603	1,136	274	961	-54.6	-15.4

Source: Company, Nirmal Bang Institutional Equities Research

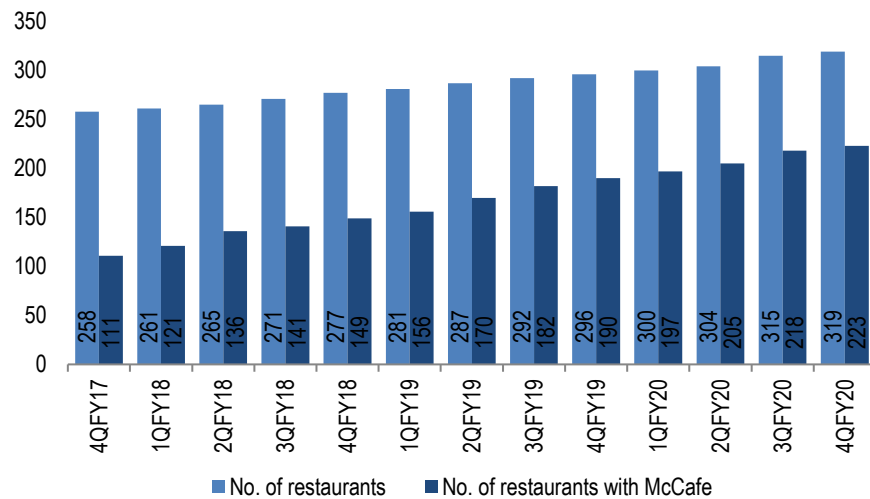
Note: Excludes IND AS 116 impact

Exhibit 4: 4QFY20 saw negative SSSG of 6.9% after 18 quarters of consecutive positive SSSG



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: 4 new restaurants and 5 McCafes were added during 4QFY20

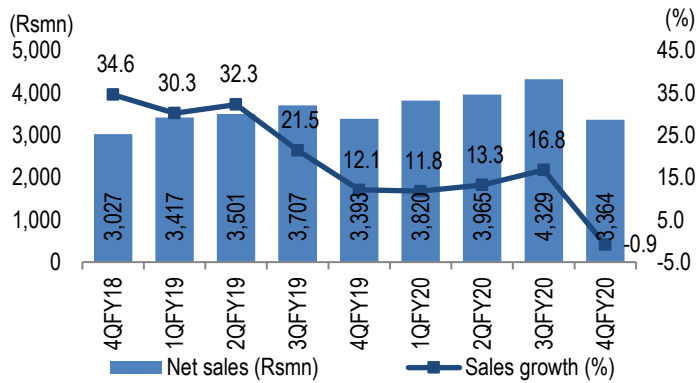


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: No. of stores operational as on FY20

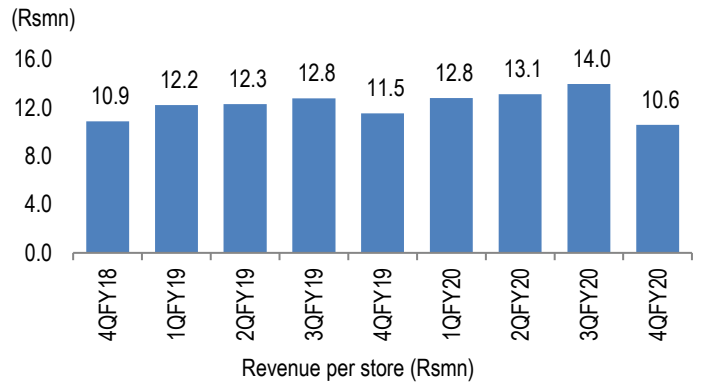
Business channel	No. of stores operational
Delivery	203
Takeaway	203
Dine in	128
Drive Thru	56

Exhibit 7: Sales declined 0.9% due to lost days in March..



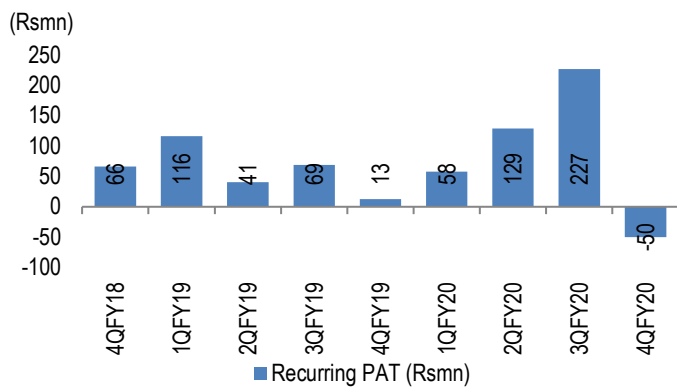
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: ...leading to decline in revenue/store



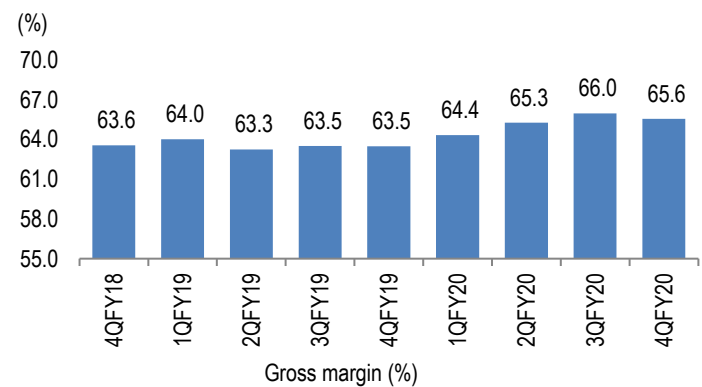
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 9: WLDL posted recurring loss of Rs50mn in 4QFY20



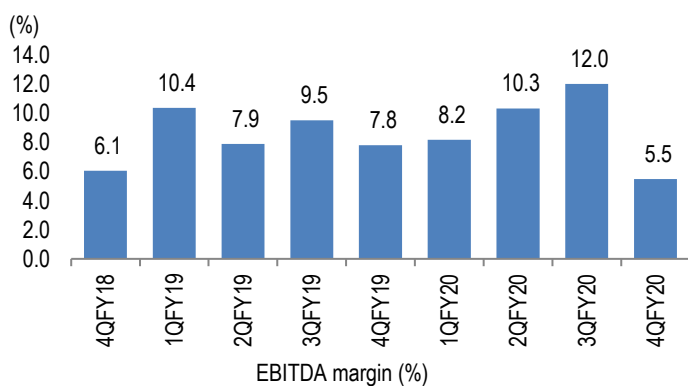
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 10: Gross margin expanded ~210bps YoY



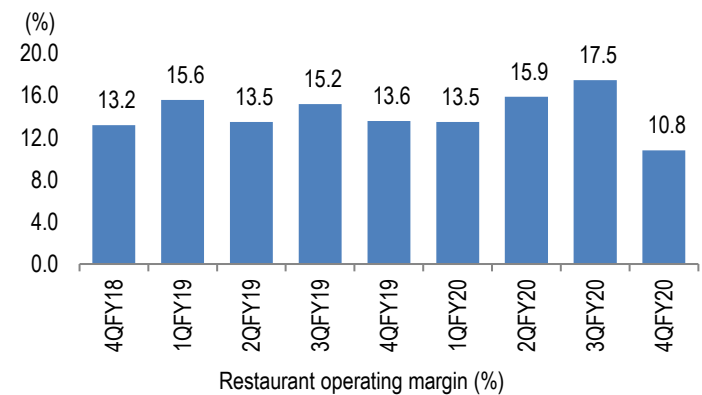
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: EBITDA margin contracted ~230bps YoY



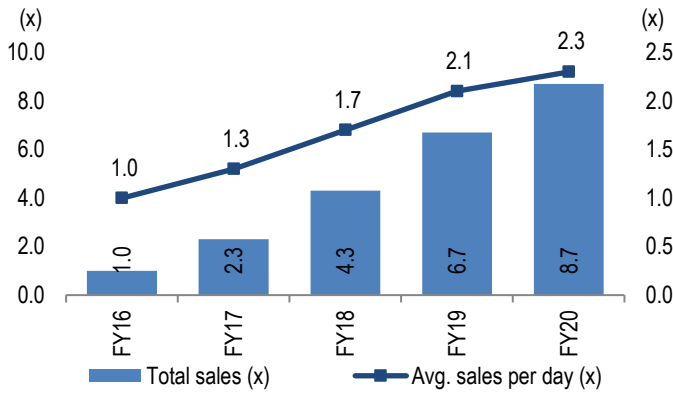
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 12: ROM shrinks due to committed & fixed costs



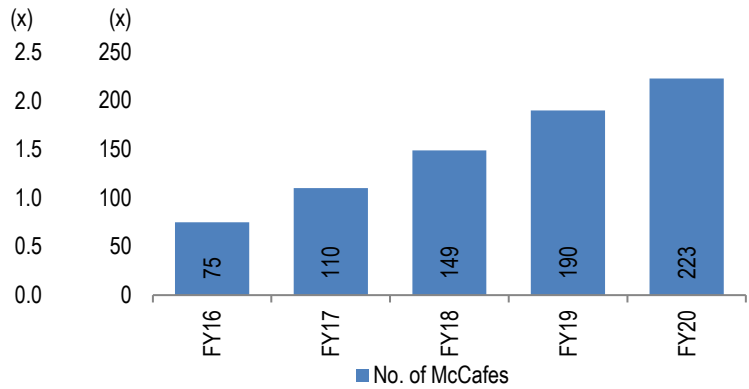
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 13: McCafe sales increased ~8x over 4 years with...



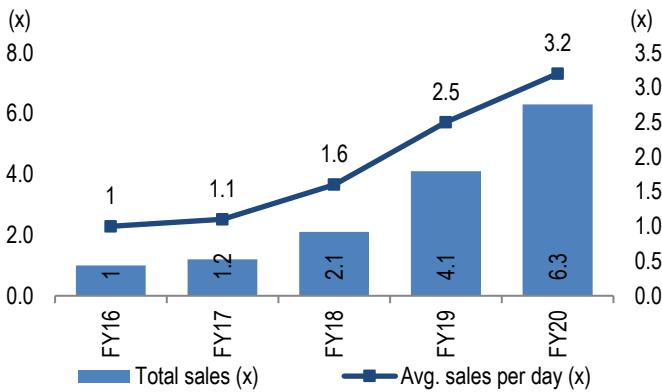
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 14: restaurants base increasing ~3x to 223



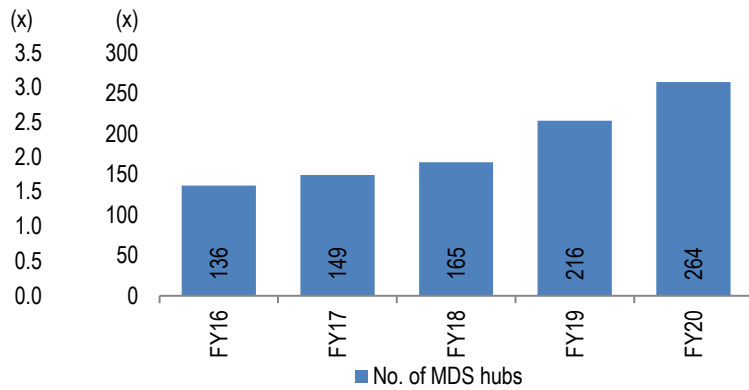
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 15: McDelivery sales increased ~6x over 4 years with....



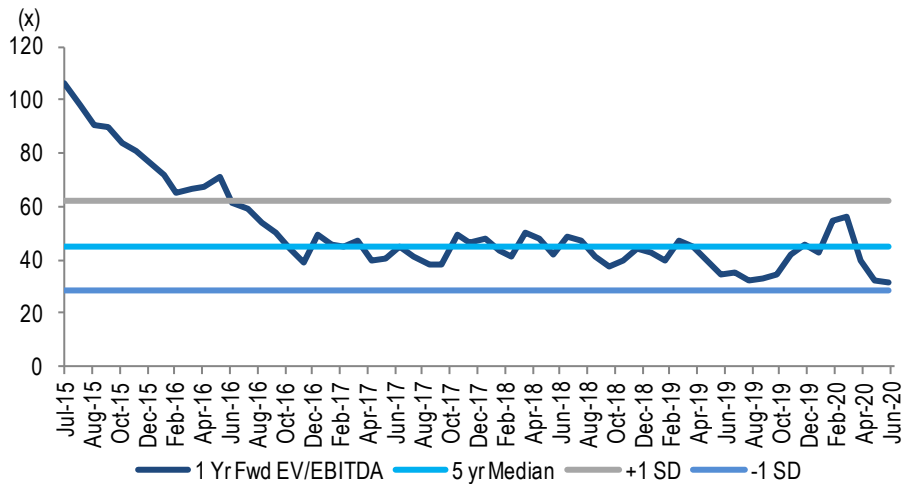
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 16: delivery network increasing ~2x to 264



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 17: 1-yr forward EV/EBITDA



Source: Company, Nirmal Bang Institutional Equities Research

4QFY20 Con-call and presentation highlights

Performance during 4QFY20/FY20 and overall demand environment

- SSSG during 4QFY20/FY20 was -6.9%/4.0% respectively. For 2 months Jan-Feb FY20/11 months YTD FY20, SSSG stood at 12.3%/8.3%. After 18 consecutive quarters of positive SSSG, WLDL reported negative SSSG for 4QFY20.
- Sales growth during 4QFY20/FY20 was -0.9%/10.4% respectively. For 2 months Jan-Feb FY20/11 months YTD FY20, sales growth stood at 20.3%/15.1%.
- Sustained momentum in same store sales resulted in higher average sales per restaurant (AUV) in every quarter, except in 4QFY20, which was impacted due to COVID-19. Excluding Mar'20 (due to Covid-19), AUV has grown more than 60% over the last five years.
- In FY20, WLDL expanded its footprint and opened 24 new restaurants, including 4 in 4QFY20, taking the total restaurant count to 319. Additionally, 5 new restaurants were ready but not operationalized at the time due to mandatory lockdown and will open on priority basis once normalcy returns hopefully somewhere in the second half of the year. The company added 33 new McCafés in FY20, taking the total number to 233.
- During the year, the company continued to invest in strengthening its digital backbone through McDelivery app. The app, which was launched in January 2019, has over 3mn downloads now. Management believes that access to this kind of customer base also gives a competitive advantage in the digital phase that the industry will operate in going ahead.
- In response to the onset of COVID-19, the company anticipated consumers' need for assurance and convenience and was among the first companies (the first QSR) to launch 'Contactless Delivery'.
- As the states get ready to ease the lockdown, WLDL has launched 'Contactless Take out'. In the coming quarters as customer assurance and convenience will be the key focus areas, the company has implemented a 42-point checklist across its dine-in, delivery and take-out to ensure highest standards of food safety and hygiene across all channels.
- High quality of real estate portfolio, long term lease structures and strong backward integrated supply chain continue to serve as a competitive advantage for the company and have given it the ability to bounce back quickly and minimize the disruption caused by COVID-19.
- According to the management, 50% of pre-COVID sales contribution was coming from convenience channels, including delivery, take-outs and drive-thrus and these will be the biggest drivers of business in the foreseeable future. With over 264 delivery hubs and strong partnerships with aggregators, the company is well positioned to cater to the demand. Number of delivery hubs standing at 264 may rise to 280-290, not to 320. As of now, there are 70 drive-thrus.
- Partnership with aggregators has helped significantly to get through the last 3 months.
- WLDL has a diversified restaurant portfolio located across high streets, standalone, drive-thrus and malls. The company is probably the only QSR with long term leases and sales linked rental agreements, which has proved to be another competitive advantage and helped the company to conserve cash.
- In the new normal, even as the market size may shrink, the company's market share is likely to increase.
- The company is seeing day on day, week on week growth in sales as consumers are moving from panic to caution.
- WLDL is looking to restart journey to pre-COVID growth rates from the 2HFY21.
- McCafe & McBreakfast have a diversified product portfolio and service many generators including home, work, education etc. McDonalds is one brand that is not skewed towards IT parks as the company believes in having multiple generators. Of the 230 McCafes, the company would have 20 linked to offices but the remaining are linked to other generators.
- Smaller towns are doing better than they used to do.

- Malls being shut doesn't bother the company much as it has a very strong and diversified portfolio, including retail locations (Eg: Mumbai 100 locations of which malls may be 20-30). Reach of stores has increased as few stores have covered the whole city and there is less traffic.
- The company will continue with the value for money platforms even though many players are taking away discount/promotions.
- WLDL will look to partner with Amazon if it enters the market as a delivery aggregator.

COVID-19 impact on 4QFY20/1QFY21 and response

- The onset of the COVID-19 pandemic brought forth the agility and customer forward strategies of WLDL.
- The company stepped up its already stringent hygiene and safety practices across its operations and ensured that similar processes were also being followed by the suppliers at their end.
- On the cost optimization front, the management is looking at its real estate portfolio very carefully, including all the stores that are laggards and as to what can be done about them. Fixed costs including corporate G&A is a very big focus in terms of reducing cost and the company is also revisiting supply chain to improve efficiencies. Management will be able to guide clearer in in the next quarter.
- As large part of the dine-in business could not be made operational due to lockdown, revenues have been adversely impacted. The business has continued to incur committed expenditures, especially with respect to its employees and other expenditures not directly linked to revenues. This has significantly impacted profitability during this lockdown period. However, the company has witnessed encouraging customer traction through food deliveries and other convenience channels.
- As an outlook for FY21, focus is on survival during lockdown and revival as normalcy returns wherein cash conservation, optimizing operating costs and targeting a healthy balance sheet remain number one priority.
- The company is trying to work on a model and see if it can optimize cost in such a way that it can maintain margins with 20% less sales and eventually get back to previously guided trajectory in FY22.
- Maharashtra, Tamil Nadu, Telangana and Gujarat that constitute more than 75% of total stores are among the worst hit states by COVID-19. However, the company has been able to assure business continuity by activating convenience channels. WLDL will have 1000+ touch points with all customers through its convenience channels. These channels have performed extremely well during the last few months. For example: Business in drive-thru channel in a store at Bharuch last month was same as it's dine-in sales last year, and a store in Hyderabad has been breaking its own record in sales through convenience channels.
- The company partnered with many NGOs and corporates to distribute safe and hygienic food to police officers, healthcare workers, daily wage earners and slum dwellers.

Brand extension highlights:

- McCafés: McCafé sales have increased more than ~8x in the last 4 years i.e. from 1.0x in FY16 to 8.7x in FY20. Average sales per day more than doubled in the last 4 years i.e. from 1.0 in FY16 to 2.3x in FY20. During the year, the in-house coffee chain grew to become the second-largest coffee chain by units in the region. It also achieved the milestone of serving more than 10mn cups of coffee.
- McDelivery: McDelivery sales have increased more than ~6x in the last 4 years i.e. from 1.0x in FY16 to 6.3x in FY20. Average sales per day more than tripled in the last 4 years i.e. from 1.0 in FY16 to 3.2x in FY20. Significant growth from digital channels and tie-up with aggregators continues to be accretive.
- McBreakfast: Breakfast combos introduced to increase trials and frequency.
- Continued investments in EOTF allow restaurants to make completely contactless delivery.

Financial performance

- Continuous increase in volume and operating efficiencies has driven gross margins.
- ROM for Jan and Feb 2020 stood at 15.4%, but lockdown in March brought down the 4QFY20 ROM to 10.8%.
- WLDL has a large pool of part time workers, i.e. 60%, to help the company manage the peak timings of lunch and dinner. Part timers are offered to work for minimum of 4 hours and maximum of 8 hours a day and have been giving tremendous flexibility to the company to manage its employee costs.
- WLDL always takes partnership approach with malls, where it has a revenue share-based deal for ~20 years with more than 90% malls. On high street locations, the company has either a minimum guarantee or revenue share plus minimum guarantee deal and the company has been working closely with the landlords where they can help the company to get through this year.
- The company had to provide for an exceptional item amounting to Rs166mn towards provisions for inventory write-offs (due to risk of expiry of products because of lower demand).

Outlook/guidance/other takeaways

- The management will be re-evaluating capex investments but will continue to re-image restaurants and expand EOTF footprint.
- Vision 2022 still holds but the number of stores might become a challenge and the company will come back with more clarity during the second half of the year. Final endeavor is to get margins move back to previous levels.

Financials (Consolidated)
Exhibit 18: Income statement

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
Net sales	11,349	14,020	15,478	12,626	17,195
% Growth	21.9	23.5	10.4	-18.4	36.2
SSG %	15.8	17.0	4.0	-20.6	30.0
COGS	4,275	5,116	5,382	4,179	5,513
Staff costs	1,721	1,453	1,690	1,449	1,886
Other expenses	4,597	6,209	6,966	5,766	7,586
Total expenses	10,593	12,778	14,039	11,394	14,985
EBITDA	755	1,243	1,439	1,232	2,211
% growth	60.9	64.5	15.8	-14.4	79.4
EBITDA margin (%)	6.7	8.9	9.3	9.8	12.9
Other income	248	84	69	160	167
Interest costs	151	177	149	125	100
Depreciation	673	797	866	992	1,082
PBT (before exceptional items)	180	352	494	276	1,196
Exceptional items	0	0	-124	0	0
Tax	13	139	128	69	299
PAT (before exceptional items)	167	213	366	207	897
PAT	167	213	242	207	897
PAT margin (%)	1.4	1.5	1.6	1.6	5.2
% Growth	(237.4)	27.8	72.0	-43.5	334.0

Source: Company, Nirmal Bang Institutional Equities Research
 Note: Excludes IND AS 116 impact

Exhibit 20: Balance sheet

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
Share capital	311	311	311	311	311
Reserves	5,111	5,519	5,459	5,666	6,562
Net worth	5,422	5,830	5,770	5,977	6,874
Total debt	1,891	2,339	1,837	1,700	1,550
Deferred tax liability	0	0	-214	0	0
Total liabilities	7,258	8,169	7,394	7,677	8,424
Gross block	9,552	10,752	12,024	12,774	14,274
Depreciation	3,815	5,727	6,592	7,584	8,666
Net block	5,737	5,025	5,431	5,190	5,608
Capital work-in-progress	0	1,210	1,161	1,161	1,161
Investments	1,843	2,024	1,576	2,150	2,400
Inventories	337	410	411	276	631
Debtors	64	98	47	91	97
Cash	109	92	30	114	498
Loans & advances	1,161	1,278	465	1,120	1,350
Other current assets	41	105	8,296	7,189	6,889
Total current assets	1,712	1,982	9,249	8,789	9,464
Creditors	1,084	1,178	1,280	644	1,924
Other current liabilities & provisions	950	895	8,743	8,969	8,285
Total current liabilities	2,034	2,073	10,023	9,612	10,209
Net current assets	-322	-91	-774	-823	-744
Total assets	7,258	8,169	7,394	7,677	8,424

Source: Company, Nirmal Bang Institutional Equities Research
 Note: Excludes IND AS 116 impact

Exhibit 19: Cash flow

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
PAT	167	213	366	207	897
Depreciation	673	797	866	992	1,082
Other income	(248)	(84)	(69)	(160)	(167)
(Inc./dec. in working capital)	267	(79)	(564)	106	719
Cash flow from operations	858	847	600	1,144	2,531
Capital expenditure (-)	(930)	(1,297)	(1,222)	(750)	(1,500)
Net cash after capex	(72)	(450)	(622)	394	1,031
Inc./(dec.) in invest. & other ass.	105	(280)	(6,861)	38	(13)
Cash from invest. activities	(825)	(1,576)	(8,082)	(712)	(1,513)
Dividends paid (-)	0	0	0	0	0
Inc./(dec.) in total borrowings	(13)	448	(502)	(137)	(150)
Cash from financial activities	5	461	7,847	(348)	(634)
Others	0	251	(302)	0	0
Opening cash balance	71	109	92	30	114
Closing cash balance	109	92	30	114	498
Change in cash balance	39	(17)	62	84	384

Source: Company, Nirmal Bang Institutional Equities Research
 Note: Excludes IND AS 116 impact

Exhibit 21: Key ratios

Y/E March	FY18	FY19	FY20	FY21E	FY22E
Per share (Rs)					
EPS	1.1	1.4	2.4	1.3	5.8
Book value	34.9	37.5	37.1	38.4	44.2
Valuation (x)					
P/Sales	4.8	3.4	3.0	3.7	2.7
EV/sales	4.9	3.5	3.0	3.7	2.7
EV/EBITDA	73.9	39.7	32.3	38.0	20.8
P/E	327.8	226.5	126.3	223.7	51.6
P/BV	10.1	8.3	8.0	7.7	6.7
Return ratios (%)					
RoCE	1.1	5.8	7.3	3.1	14.0
RoE	3.1	3.8	6.3	3.5	14.0
Profitability ratios (%)					
Gross margin	62.3	63.5	65.2	66.9	67.9
EBITDA margin	6.7	8.9	9.3	9.8	12.9
EBIT margin	0.7	3.2	3.7	1.9	6.6
PAT margin	1.4	1.5	2.4	1.6	5.2
Liquidity ratios (%)					
Current ratio	0.3	0.4	0.8	0.5	0.7
Quick ratio	0.2	0.3	0.7	0.4	0.5
Solvency ratio (%)					
Debt-to-equity ratio	0.3	0.4	0.3	0.3	0.2
Turnover ratios					
Total asset turnover ratio (x)	1.6	1.7	2.1	1.6	2.0
Fixed asset turnover ratio (x)	2.0	2.8	2.8	2.4	3.1
Inventory days	27.3	26.6	27.8	30.0	30.0
Debtor days	1.8	2.1	1.7	2.0	2.0
Creditor days	79.7	80.7	83.3	84.0	85.0

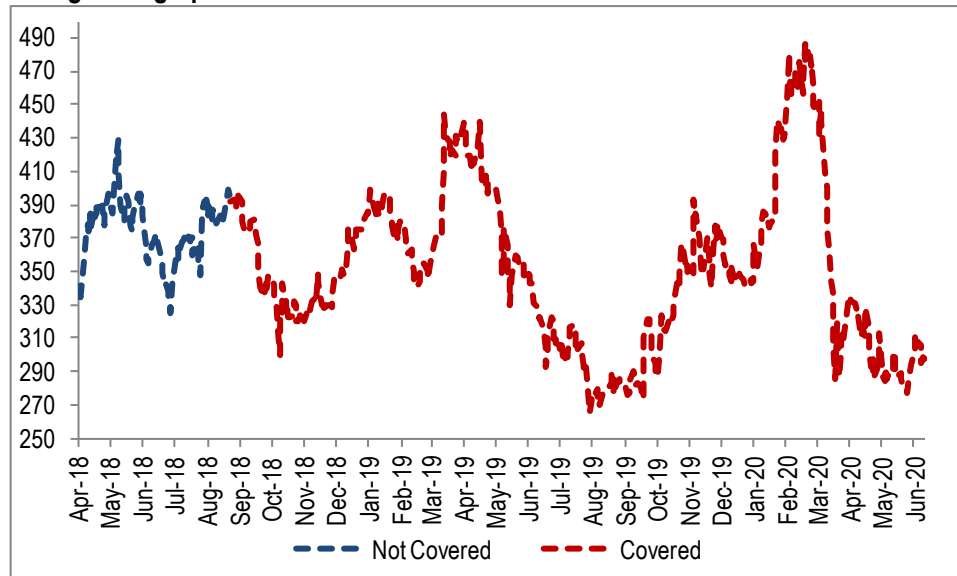
Source: Company, Nirmal Bang Institutional Equities Research
 Note: Excludes IND AS 116 impact

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
6 May 2015	Buy	296	403
11 May 2015	Buy	293	403
5 June 2015	Buy	280	403
10 August 2015	Buy	295	356
9 November 2015	Buy	238	335
8 February 2016	Buy	222	280
9 May 2016	Buy	202	282
9 June 2016	Accumulate	237	246
8 August 2016	Accumulate	214	219
24 August 2018	Buy	395	485
29 October 2018	Buy	320	420
4 February 2019	Buy	380	440
4 April 2019	Buy	420	490
15 May 2019	Buy	349	450
26 July 2019	Buy	291	370
25 Oct 2019	Buy	347	425
01 Nov 2019	Buy	350	425
24 Jan 2020	Buy	421	485
20 April 2020	Buy	326	375
13 June 2020	Buy	297	350

*Coverage taken over by Vishal Punmiya from 25th Oct'19

Rating track graph



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Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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