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December 08, 2017 RE-INITIATING REPORT VOL-3, NO-25

Westlife Development Limited

BUY

CMP: Rs. 366 **TARGET PRICE: Rs.425** **TIME : 12 months**

REINITIATION REPORT

We had initiated coverage on Westlife Development Limited on August 24, 2017 (Vol-3 No-15) at the price of Rs266 and target of Rs350. Post our coverage, the stock has breached our initial target of Rs350, revised to Rs425.With the positivity received about the future plans and the line of action chalked by the company, we re-initiate a BUY call on the stock at CMP of Rs.366 and target of Rs425 over a horizon of 12.

About the Company:

Westlife Development Limited (WDL) focuses on putting up and operating quick service restaurants (QSR) in India through its subsidiary, Hardcastle Restaurants Pvt. Ltd. (HRPL). Its restaurant categories include freestanding, food court, in-store and mall stores. The Company operates a chain of McDonald's restaurants in West and South India. (McDonalds has two master-franchisee in India – Westlife (in its 100%-subsidiary in West & South and Connaught Plaza Restaurants (unlisted) for North & East). Starting as a JV in 1995, WDL got Development License in 2010 – this means that WDL could develop sites at its own cost and pay a specified royalty to McDonald's. The Company, through its subsidiary HRPL, operates McDonald's through approximately 261 restaurants across over 30 cities. Its service formats and brand extensions consist of restaurants, Breakfast, McDelivery and kiosks at various transit points. The Company has operations in Telangana, Gujarat, Karnataka, Maharashtra, Tamil Nadu, Pune, Kerala and parts of Madhya Pradesh. The company has Mr. B.L. Jatia as the Chairman and Mr. AmitJatia as the Vice-Chairman.

INVESTMENT RATIONALE

Strong Supply Chain:

Supply Chain (SC) built around the concept of "farm-to-fresh" model remains the backbone for the company. There are sourcing centres feeding resources into strategically-located distribution and warehousing centres (four centres located across each corner of the geographic footprint), which in turn feed various restaurants. Moreover, the Company continues to address and ensure the supply to meet any kind of emergencies. To deal with the price volatility and weather vagaries; the company undertakes contract farming in a small way; leading to price predictability for McDonalds and assured return for the farmers. HRPL has a wide distribution network with stringent requirements on timely deliveries and strict temperature control. There is a swift network carrying material from suppliers to the distribution center (DC) and from the DC to the restaurants. The company also has almost 10,000 sq. ft. of cold storage infrastructure across its strategic procurement and consumption cores. This enables it to capitalise on attractive pricing, stocking for future needs and managing product shelf-life better. Thus, the company is always on toes with respect to the back end support, avoiding any hindrance and vouching for a smooth overall working.

The other factors leading to growth:

a. Store addition:

The Company stands at total count of 265 restaurants, with a healthy mix between West and South India, very much on track with the target to add 25-30 new restaurants in the current financial year. The strategic initiatives taken by the company are actually yielding results and building the baseline sales evident through the fact that the company has reported nine consecutive quarters of positive same store sales growth.

Source: Company Presentation

SNAPSHOT	
52 week H / L	Mcap (INR mn)
370/152	57,000
Face value: 2	
BSE Code	NSE CODE
505533	Not listed

Annual Performance				
(Rs mn)	FY15	FY16	FY17	FY18E
Sales (Net)	7,643	8,334	9,308	10,692
EBITDA	152	426	470	781
EBITDA (%)	2.0%	5.1%	5.0%	7.3%
Other Income	165	97	200	185
Interest	102	150	154	193
Depreciation	504	577	637	710
PBT	-290	-203	-121	62
PAT	-291	28	-121	53
Equity	311	311	311	311
EPS (INR)	-1.9	0.2	-0.8	0.3

Quarterly Performance				
Parameters (Rs mn)	Dec-16	Mar-17	Jun-17	Sep-17
Sales (Net)	2,417	2,249	2,623	2,647
EBITDA	140	98	137	193
EBITDA (%)	6%	4%	5%	7%
Other Income	43	60	66	45
Interest	41	37	39	36
Depreciation	160	162	160	169
PAT	-17	-41	2	21
Equity (Rs mn)	311	311	311	311

Ratio Analysis				
Parameters (Rs mn)	FY15	FY16	FY17	FY18E
EV/EBITDA (x)	380.3	136.7	125.1	75.5
EV/Net Sales (x)	7.5	7.0	6.3	5.5
M Cap/Sales (x)	7.5	6.8	6.1	5.3
M Cap/EBITDA (x)	376.0	133.8	121.4	73.0
Debt/Equity (x)	0.1	0.2	0.3	0.4
ROCE (%)	-3%	-1%	1%	5%
Price/Book Value (x)	10.7	10.6	10.8	10.7
P/E (x)	-195.8	-277.0	-469.6	1073.1

Share Holding Pattern as on 30th September, 2017		
Parameters	No of Shares	%
Promoters	9,67,27,488	62.2
Institutions	3,41,78,897	22.0
Public	2,46,66,620	15.8
TOTAL	**15,55,73,005**	**100.00**

Source: Annual Report

Note: All the data is calculated as per Market Price on 8th December 2017

Please Turn Over

Investment rationale (contd.)

Brand extensions:

There are various initiatives taken by the company for increasing its presence and ramp up on the target customers. The efforts across each of the below are seen to be contributing to the growth of the company.

McCafe:
The Company has launched above the line (ATL) campaign. It has embarked on building brand awareness through radio and outdoors for the McCafe platform. This has helped, build the brand proposition resulting in McCafe being a strong contributor to same store sales as well as helping augment our gross margin through better product mix. As of Q2FY18, there are total of 136 McCafe's with 15 added during Q2FY18. The company targets to have 10-150 by the end of FY18E and it seem to be well on track to achieve the same. This segment is a significant margin lever for the company

Breakfast menu:
After the initial success across the restaurants that offer breakfast menu, the company is expanding beyond that. The new menu seems to have resonated well with the customers. The company takes it as a 2-3 years horizon opportunity which should gradually become an essential component of the revenues

Desert kiosks:
Being economical and having a variety to offer, these are an important drivers in increasing the market penetration of the company

Mc Delivery:
Mc Delivery continues to be the robust growth engine for the company in the existing restaurants. It is making all the efforts to tie up with food aggregators which prove to be revenue accretive.

New ventures:
The everyday value introduction has been gaining gradual momentum and leading to significant footfalls. Also menu innovation has borne positives for the company.

New happy price menu:
This has been the feather in the cap for the company driving sales and footfalls with the newly launched Chatpata Nan been a huge hit. Also the product range under the Flavors of borders (12 new products developed and launched) that was launched in the festive season was a hit with strong addition to the customer base.

c. ROP 2.0:

The implementation of ROP (Restaurant Operating Platform) 2.0 has ensured that new restaurants break-even in a shorter span of time; this has aided margin expansion and lead to strong cash flow and profit growth. As the company opens more and more new restaurants under ROP 2.0 which is the new Restaurant Operating Platform, the overall profitability and cash flows continue to improve.

Update on the Mr. Vikram Bakshi case:

As indicated earlier, McDonalds had terminated the agreement with Connaught Plaza (CRPL), its franchisee for North and East India, which had been facing issues. McDonald's had terminated its agreement with equal joint venture partner CPRL on August 21, stating that CPRL would not be authorized to use the McDonald's branding, trademark, design and marketing policy rights within 15 days of the termination notice, starting September 6. However, the board of CPRL under the chairmanship of Justice GS Singhvi had passed a resolution on September 17 to reopen 21 restaurants for which health licences have since been received, and 18 of those restaurants in Delhi have reopened. Many of the 169 stores across the north and east region have been operating even past the deadline set by the termination notice. The tiff between Bakshi and Mac Donalds continues with Mac Donald being head strong on not doing business with Bakshi. As and when it unfolds, Westlife would stand to benefit from the same.

Wrap up FY18E:

The Company plans to add 25-30 restaurants by the end of the year. It maintains the confidence of clocking high single digit SSG. This should also lead to expansion of operating margins. The company continues to have menu innovation and brand differentiation as the key. The focus would be on the profitable growth. The company aims to optimize and capitalize on the opportunities with a constant evaluation of the restaurant portfolio and offerings.

Westlife Development Limited

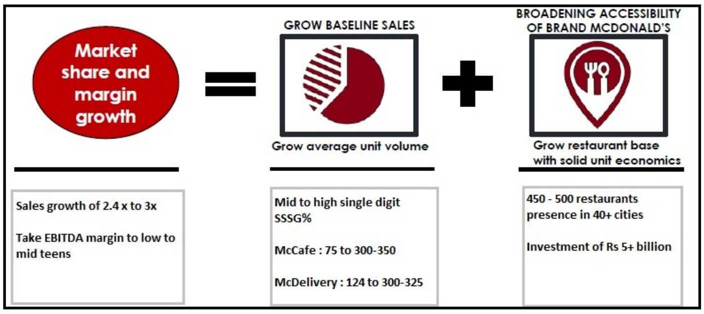
BUY

CMP: Rs. 366 TARGET PRICE: Rs. 425 TIME : 12 months

Where does the company stand on the 2022 vision :

WDL aims to touch mid to high same-store sales growth or SSSG by 2022 and achieve EBITDA margin in early or mid-teens.

- Increase McDonalds store count from 261 currently to 450-500 stores across more than 40 cities.
- Increase stores having McDelivery from 124 to 300-325 by 2022.
- McCafe expansion from 121 to 300-350 outlets.
- Achieve savings of Rs1.2bn-Rs1.5bn in capex by reducing capital cost per store by 20%.
- To reduce restaurant break-even period from 18-24 months currently to 12-18 months.
- Target cash ROI of above 20% in 18-20 months.
- Make investment of Rs.5bn to set up restaurants
- Achieve sales growth of 2.4x-3.0x from current levels



Source: Company Presentation

Above are mentioned some of the targets that the company has set for itself reaching 2022. It is encouraging to see that the company is very much on track towards achieving the same

Financials:

Reduction of GST from 18% to 5% is a positive for the company. To deal with the hike, the company had increased the base price to keep the overall prices the same. The input tax credit on the other hand has been taken away which needs to be adjusted with the reduction in GST. Overall the move is positive for the company and should be passed on to the customers.

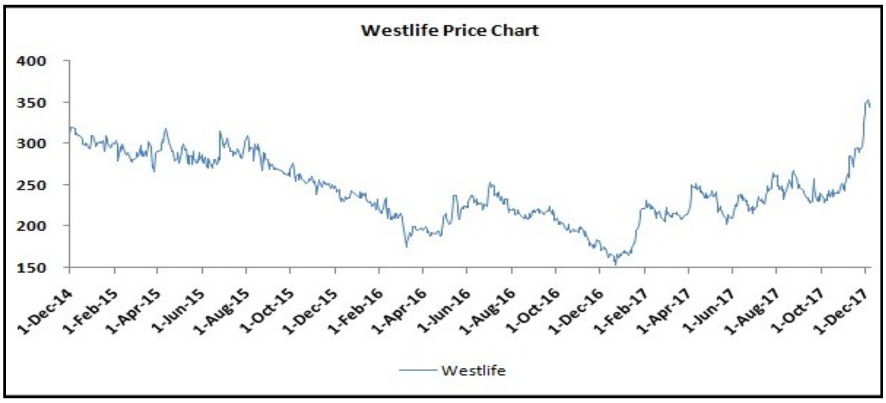
Risks and concerns:

- Slowdown in the economy and rise in inflation: This can impact the food industry as it is related to the disposable income of the customers. Also an increase in inflation would lead to pricing pressures.
- Consumer sentiment: weaker consumer sentiment could impact the discretionary nature of the products offered by the company.
- Increase in competition: New players trying their hands into the food industry with delivery at lower prices could be negative for the company.
- Health conscious approach: With the increase in the health awareness, customers may seek healthy options which could impact the company.
- Supply chain: Any disruption in the supply chain can adversely impact the supply of ingredients to the restaurants and the freshness of finished products.
- Manpower dependence: The QSR industry has high dependence on manpower and this is critical for the success of WDL. In case of higher inflation, it could actually eat into the margin expansion assumption
- Rise in royalty: As per the agreement with McDonald's, WDL pays a specified royalty which was supposed to rise at a pre-determined rate. Any increase in this would impact the company profits.

Outlook and valuations:

We had initiated the report with the key understanding that the customers in India will prefer McDonald's stores due to value for money, accessibility, brand, and a desired combination of food and beverages; leading to WDL being one of the key beneficiaries of the growth consumption story. We stand by the same with the assumptions fructifying gradually. The company continues to build the business on the four strategic levers being broadening accessibility, growing the baseline, margin expansion and growth through people. Keeping in mind the positive scenario and the well-established positioning of the company in the industry, we re-initiate a BUY on the stock with a revised target price of Rs425 (Rs350 achieved) over a 12 months horizon.

Price Performance:



Source: Ace Equity

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