INDIA

Retail

Jubilant FoodWorks

Initiating coverage **14 June 2010**

Sell

Target Price: Rs230

CMP: Rs282*

Downside: 18.4%

**as on 11 June 2010*

'Pizza mania' overdone

We initiate coverage on Jubilant FoodWorks (JFW) with a Sell rating and a target price of Rs230 (implied P/E of 27.3x FY12E), indicating downside potential of 18.4% from current levels. Though we are confident regarding the company's ability to cash in on the growing affluence and changing lifestyle of the Indian consumer, we consider the current valuations overstretched due to unrealistic market expectations of higher growth.

- **Current valuations expensive:** DCF valuation method suggests fair value of Rs230 (implied P/E of 35.2x FY11E and 27.3x FY12E). At CMP, the stock trades at a PE of 43.1x FY11E and 33.5x FY12E, which we believe is a huge premium primarily ascribed for higher-than-expected growth from the company's existing operations and over-enthusiasm in anticipation of earnings growth accretive tie-up. Our analysis suggests such run-up in prices is unwarranted and unsustainable and would result downward re-rating in stock prices.
- **Competition to intensify:** Though we are positive on the company's strategy to extend its reach in Tier 2 and Tier 3 cities, we remain a bit cautious on the competitive landscape that would emerge after another two to three years, since we expect a large number of organized players to realize and tap this opportunity and compete for this market.
- **Market expectations of higher IRR from a possible QSR tie-up may be unrealistic.** Our analysis suggests a tie-up with coffee (generating store IRR of 15.4%) and burger (IRR 25%) chains would be IRR decretive for the company, whereas a tie-up with a sandwich chain (IRR of 33.2%--higher than JFW's 29.9%) is the only option that would be IRR accretive.
- **Absence of free cash flow deployment to be ROE decretive:** Free cash flows generated and not deployed would result in 1,516bps decline in ROE to 31.6% over FY10-12E.
- **Profitable and scalable business model:** We believe the dual strategy of increased penetration in Tier 2 and Tier 3 cities and multiple price points (cheapest pizza at Rs39) would enable the company to clock 27.9% CAGR sales and achieve same-store-sales growth (SSSG) in the higher single digits over FY10-12E.
- **Key risks:** Upward: New tie-ups, if value accretive, would result in upward earnings revision.

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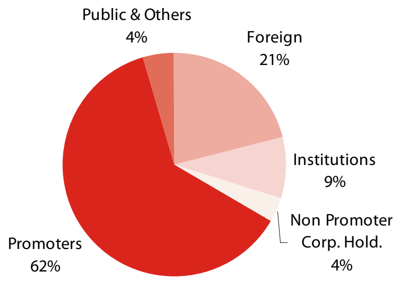
Key Data

Bloomberg Code	JUBI IN
Reuters Code	JUBI.BO
Current Shares O/S (mn)	64.0
Diluted Shares O/S(mn)	64.0
Mkt Cap (Rsbn/USDmn)	18/385.2
52 Wk H / L (Rs)	425/145
Daily Vol. (3M NSE Avg.)	2,870,843
Face Value (Rs)	10

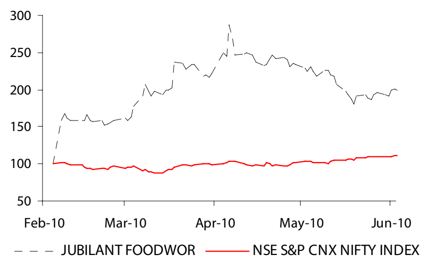
USD = Rs46.9

Shareholding Pattern (%)



As on 31st March 2010

One Year Indexed Stock Performance



Price Performance (%)

	1M	6M	1Yr
Jubilant FoodWorks	(13.9)	-	-
NIFTY	(0.3)	0.0	10.4

Source: Bloomberg, Centrum Research
**as on 11 June 2010*

Y/E Mar (Rsmn)	Rev	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY (%)	Fully DEPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY09	2,806	32.9	351	12.5	79	(11.7)	1.4	38.8	20.8	208.2	48.9
FY10	4,242	51.2	665	15.7	331	319.8	5.2	46.8	36.3	54.5	27.1
FY11E	5,583	31.6	892	16.0	419	26.5	6.5	31.4	30.8	43.1	19.9
FY12E	6,940	24.3	1,150	16.6	538	28.6	8.4	31.6	31.0	33.5	15.0
FY13E	8,369	20.6	1,429	17.1	693	28.8	10.8	31.9	30.4	26.0	11.5

Source: Company, Centrum Research Estimates

Please refer to important disclosures/disclaimers in Appendix A

Shareholding pattern (%)

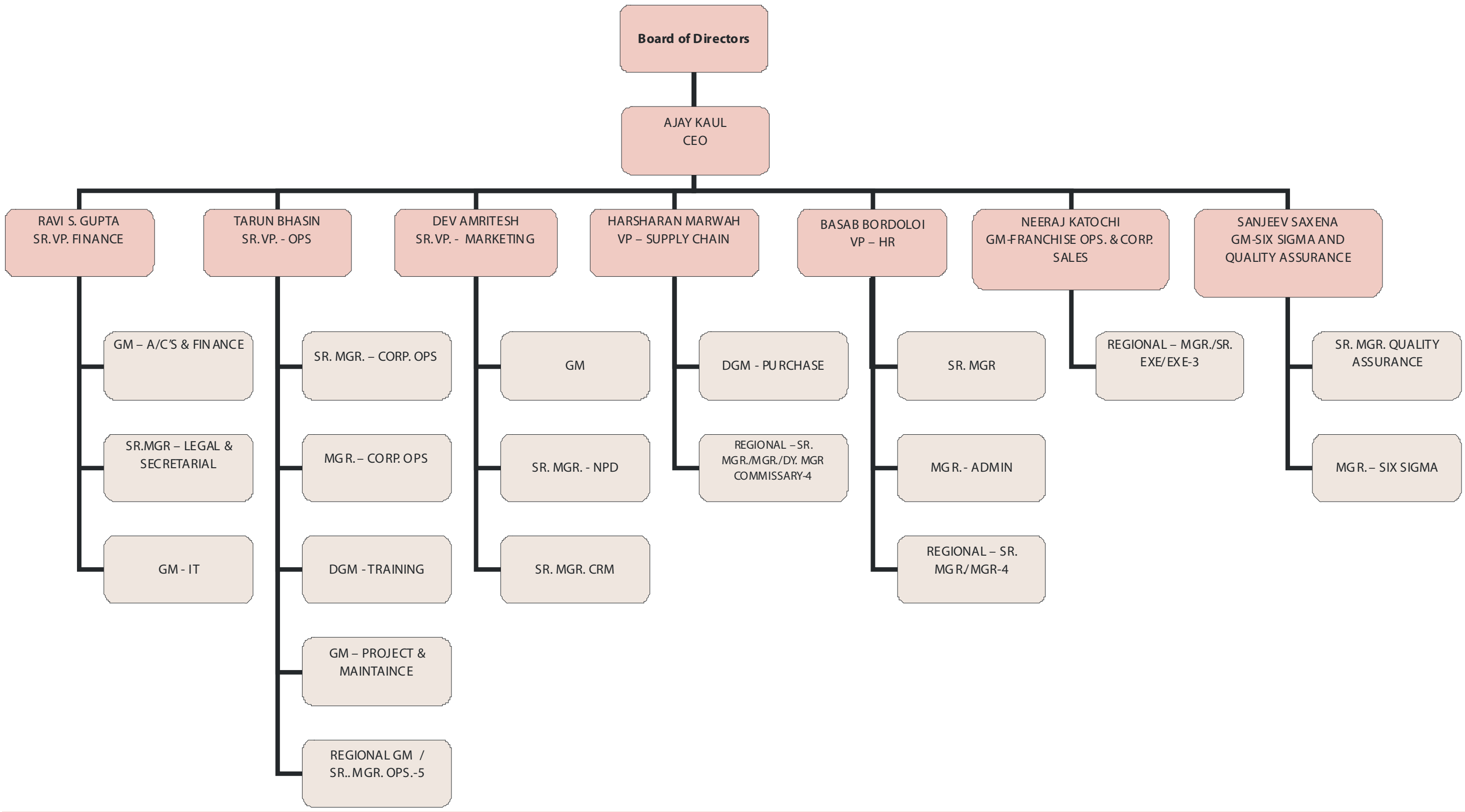
Y/E March	Q3FY10	Q4FY10
Promoters	62.1	62.1
Institutions	29.9	29.9
Public & Others	8.0	8.0
Total	**100.0**	**100.0**

Source: NSE

Company Background

Jubilant FoodWorks (JFW) runs the Dominos Pizza chain in India through an exclusive franchisee for Domino International (DI). The company handles operations and store openings, while major advertising and promotional campaigns are reviewed by DI. JFW commands over 50% share of the organised branded pizza market in India. Under the franchisee agreement, JFW's subsidiary, DP Lanka Pvt Ltd (DP Lanka) operates five outlets in Sri Lanka. The company also has the right to open Dominos outlets in Nepal and Bangladesh. The company has a pan-India presence through an established network of over 300 stores and over 8,000 employees.

Organization structure



Source: Company

Key management personnel

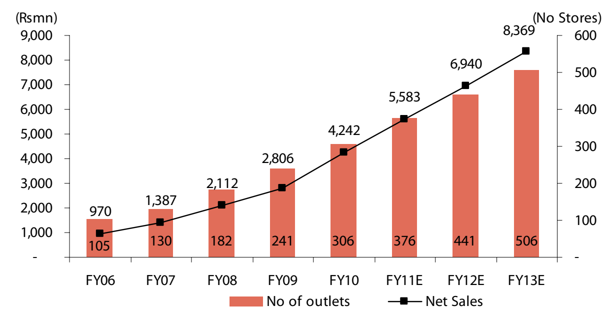
Name	Position	Profile
Mr Shyam Bhartia	Chairman and Founder Director	Mr. Shyam S. Bhartia, aged 57 years, is the Chairman and founder director, holds a bachelor's degree in commerce and is the fellow member of the ICWAI. He has over 22 years of experience in the pharmaceuticals and specialty chemicals, food, oil and gas, aerospace and IT sectors.
Mr Hari Bhartia	Co-chairman and Founder Director	Mr. Hari S. Bhartia, aged 53 years, is the co-Chairman and founder director, holds a bachelor's a degree in chemical engineering from IIT, Delhi and has over 20 years of experience in the pharmaceuticals, food, oil and gas, aerospace and information technology sectors.
Mr Ajay Kaul	CEO & Whole time director	Mr. Ajay Kaul, aged 46 years, is the CEO and whole time director and holds a bachelor's degree in technology from IIT, Delhi and an MBA from XLRI, Jamshedpur. Mr. Ajay Kaul has over 20 years experience in industries such as financial services, airlines, express distribution and logistics and food retail. Past experience includes stint with TNT Express, Modiluft and American Express TRS.
Mr Ravi Gupta	Sr VP - Finance	Mr. Ravi S. Gupta, aged 42, joined the company on April 15, 2002 and heads the accounts and finance, legal and secretarial and information technology department. He holds a bachelor's degree in commerce and is also a fellow member of the ICAI and is an associate member of the ICWA and ICSI. He has over 18 years of experience in corporate finance, strategy and accounting.

Source: Company

Investment Rationale

- Currently trading at steep valuations
- Competitive pressure to intensify in Tier 2 and Tier 3 cities.
- Market expectations of higher IRR from a possible QSR tie-up may be unrealistic
- Scalable and profitable business model
- 88bps expansion in operating margins over FY10-12E; not very significant

1.4x increase in average store count



Source: Centrum Research estimates

Summary Financials

Y/E March (Rsmn)	FY09	FY10E	FY11E	FY12E	FY13E
Key income statement data					
Net Sales	2,806	4,242	5,583	6,940	8,369
-Growth (%)	*32.9*	*51.2*	*31.6*	*24.3*	*20.6*
EBIDTA	351	665	892	1,150	1,429
-EBIDTA margin (%)	*12.5*	*15.7*	*16.0*	*16.6*	*17.1*
Depreciation	169	243	311	374	429
EBIT	182	422	581	776	1,000
Interest expenses	99	91	15	10	10
PBT from operations	83	330	567	766	990
Other non operating income	4	1	10	33	70
PBT	87	332	577	798	1,060
-PBT margin (%)	*3.1*	*7.8*	*10.3*	*11.5*	*12.7*
Provision for tax	8	1	159	260	367
Effective tax rate	9.2	0.2	27.5	32.6	34.6
Exceptional items	6	-	-	-	-
PAT	73	331	419	538	693
Adjustment for extra ordinary items	6	-	-	-	-
Adjusted PAT	79	331	419	538	693
-Growth (%)	*(11.7)*	*319.8*	*26.5*	*28.6*	*28.8*
-Net profit margin (%)	*2.8*	*7.8*	*7.5*	*7.8*	*8.3*
Key balance sheet data					
Shareholders fund	240	1,174	1,495	1,907	2,438
Debt	824	86	(0)	(0)	(0)
Total capital employed	1,064	1,260	1,495	1,907	2,438
Fixed assets	1,155	1,429	1,659	1,733	1,736
Net current assets	(90)	(169)	(165)	174	702
Total assets	1,065	1,260	1,495	1,907	2,438
Key ratios (%)					
ROCE	*20.8*	*36.3*	*30.8*	*31.0*	*30.4*
ROIC	*21.5*	*37.9*	*35.3*	*45.5*	*65.6*
ROE	*38.8*	*46.8*	*31.4*	*31.6*	*31.9*
Turnover ratios					
Asset turnover ratio (x)	3.2	3.6	4.1	4.1	3.9
Working capital cycle (days)	(30.9)	(33.7)	(31.4)	(29.7)	(28.0)
Average Inventory period (days)	23.9	21.9	23.7	23.4	23.1
Average collection period (days)	1.6	1.8	1.3	1.3	1.3
Average payment period (days)	56.4	57.4	56.4	54.4	52.4
Per share (Rs)					
Basic EPS	1.3	5.2	6.5	8.4	10.8
Fully diluted EPS	1.4	5.2	6.5	8.4	10.8
Book value	4.1	18.4	23.4	29.8	38.1
Solvency ratios					
Debt/equity	3.4	0.1	-	-	-
Interest coverage	2.0	4.6	129.0	NM	NM
Valuation parameters (x)					
P/E	208.2	54.5	43.1	33.5	26.0
P/BV	68.5	15.4	12.1	9.5	7.4
EV/Sales	6.1	4.3	3.2	2.5	2.0
EV/EBIDTA	48.9	27.1	19.9	15.0	11.5
M-cap/sales	5.8	4.3	3.2	2.6	2.2

Source: Centrum Research estimates

Shift from double to single digit SSSG to result in 88bps improvement in EBITDA margin over FY10-12 E

Company estimated to turn debt-free FY11 onwards

Investment Argument

Current valuations expensive

DCF Fair value of Rs230 implying downward potential of 18.4%

Using a DCF valuation methodology, JFW's fair value comes to Rs230, which translates into an implied P/E multiple of 35.2x FY11E and 27.3x FY12E; and implied EV/EBITDA of 16.2x FY11E and 12.1x FY12E. At current market price, the stock trades at 43.1 x FY11E and 33.5 FY12E, which we believe is expensive.

Beta of 0.9x applicable to US based QSR

In our DCF analysis, we have forecast free cash flows (FCFF) till FY17E, after which we have assumed terminal growth rate of 5.0% (accounting for long-term inflation and growth). We have assumed a beta of 0.9x, which is higher than those applicable to Indian FMCG companies, and in line with those applicable to the US-based quick service restaurants (QSR) like Dominos and Starbucks. We have assumed a WACC of 13.8% (since the company is expected to turn debt-free in FY11) and cost of equity at 14.3%.

Exhibit 1: DCF-based valuation of JFW

Y/E March (Rsmn)	2009-10E	2010-11E	2011-12E	2012-13E	2013-14E	2014-15E	2015-16E
EBIT		581	776	1,000	1,242	1,461	1,705
Less: Tax		157	248	340	422	497	579
NOPAT		424	527	660	820	964	1,125
Add: Dep & non-cash exp		312	374	430	480	523	558
Less: Capex		541	447	431	354	323	213
Less: Change in WC		(204)	(189)	(193)	(198)	(219)	(243)
FCFF		399	643	851	1,144	1,383	1,713
YoY Growth (%)			*61.3*	*32.3*	*34.4*	*20.9*	*23.9*
Assumptions							
Terminal growth (%)	***5.0***						
WACC (%)	*13.8*						
Calculation of DCF value per share							
PV of first stage	4,121						
PV of terminal value	10,589						
Net present value	**14,711**						
Less: Net debt	16						
Equity value	14,695						
Nos of shares	64						
Value per share (Rs)	**230**						

Source: Centrum Research estimates

Exhibit 2: Sensitivity analysis

		WACC						
	230	12.3%	12.8%	13.3%	**13.8%**	14.3%	14.8%	15.3%
Terminal Growth	3.5%	243	229	216	205	195	186	177
	4.0%	254	238	225	212	201	191	182
	4.5%	266	249	234	220	208	197	188
	5.0%	279	260	244	**230**	216	204	194
	5.5%	295	274	255	239	225	212	201
	6.0%	313	289	268	250	234	220	208
	6.5%	334	307	283	263	245	230	216

Source: Centrum Research estimates

Mature Indian FMCG companies (immediate comparison), currently grossing an average ROE of 84.2%, and expected to register 17.3% sales, 16.0% EBITDA and 14.1% PAT CAGR over FY10-12E, are currently trading at much lower multiples (i.e. at a PE of 24.2x FY12E).

Exhibit 3: JFW vs FMCG companies

			(Rsmn)	Sales CAGR	EBITDA CAGR	PAT CAGR	P/E (x)			EV/EBITDA (x)			ROE (%)		
Company	**Currency**	**Y/ended**	**Market cap**	**FY10-12E**	**FY10-12E**	**FY10-12E**	**FY10**	**FY11E**	**FY12E**	**FY10**	**FY11E**	**FY12E**	***FY10***	***FY11E***	***FY12E***
CLGT IN Equity	INR	03/2010	110,970	*15.3%*	*9.1%*	*6.7%*	25.6	25.4	22.5	21.2	20.5	17.8	*159.2*	*129.1*	*120.4*
APNT IN Equity	INR	03/2010	219,255	*10.0%*	*9.6%*	*4.4%*	26.2	28.4	24.1	18.1	18.6	15.1	*36.4*	*42.9*	*39.2*
NEST IN Equity	INR	12/2009	278,642	*17.1%*	*18.4%*	*21.0%*	42.5	35.1	29.1	26.5	22.6	18.9	*124.2*	*123.8*	*121.5*
GCPL IN Equity	INR	03/2010	107,701	*27.5%*	*26.0%*	*20.4%*	31.7	26.1	21.9	26.0	18.9	16.4	*46.9*	*38.7*	*36.5*
DABUR IN Equity	INR	03/2010	165,102	*16.7%*	*17.1%*	*17.9%*	32.8	27.9	23.6	25.4	21.6	18.5	*54.4*	*45.2*	*42.1*
Average				*17.3%*	*16.0%*	*14.1%*	31.8	28.6	24.2	23.4	20.4	17.3	*84.2*	*75.9*	*71.9*

Source: Bloomberg, Centrum Research estimates

Premium valuations ascribed for higher growth from existing and potential tie-ups unwarranted

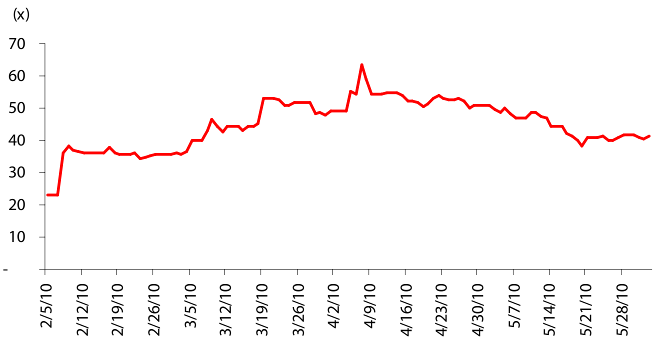
JFW is expected to register higher CAGR of 27.9% in sales, 31.5% in EBITDA, 27.5% in PAT and earn an average ROE of ~30% over FY10-12E. However, we believe the company is trading at extremely premium valuations, i.e. at a PE of 43.1x FY11E and 33.5x FY12E. We believe this over-enthusiasm is a factor of higher-than-expected growth from existing operations and yet to be finalised earnings growth accretive tie-up. We expect the company to register a 20.0% CAGR in store growth (over FY10-12E), taking into account various factors which are evaluated and considered whilst undertaking a store feasibility exercise. These involve finalising better catchments, favourable rentals, higher store ROI etc. In addition, historically (FY07-10), the company (in its early stages of growth and availability of huge opportunity) has restricted itself to 30-60 stores per annum, which we believe makes our assumption more realistic. Secondly, on the new tie-ups, barring branded sandwiches, any other tie-up would be IRR decretive for the company. These arguments strengthen our view on overstretched valuations.

Cash flow yield lower than G-sec rate of 7.8%

Our valuation of Rs 230 (implied P/E multiple of 35.2x FY11E and 27.3x FY12E) is in sync with average differential between valuations for pure FMCG and QSR players since in mature markets, this differential does not exceed beyond 10%.

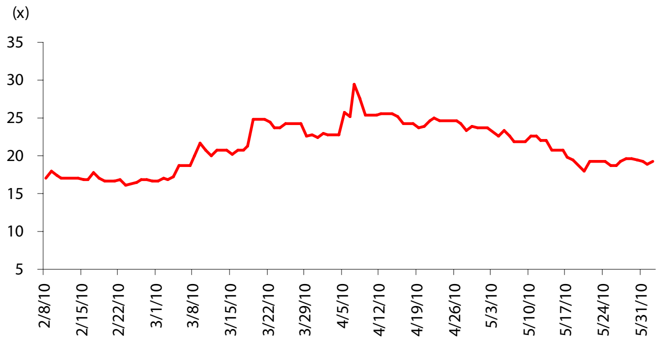
We have further tried to substantiate our view with the cash flow yield methodology on account of efficient working capital deployment (higher cash flows thrown into the system) by the company. In the absence of any organic or inorganic expansion plan, cash flow yield is expected to be 1.4% in FY10 and to steadily improve to 7.3% in FY15, which in our opinion is still lower than the 10-year G-Sec RBI bond yield of 7.8%. Higher cash flows remaining unutilized (after dividend pay-out of 20%) are expected to result in lower cash flow yields.

Exhibit 4: One-year forward P/E (x)



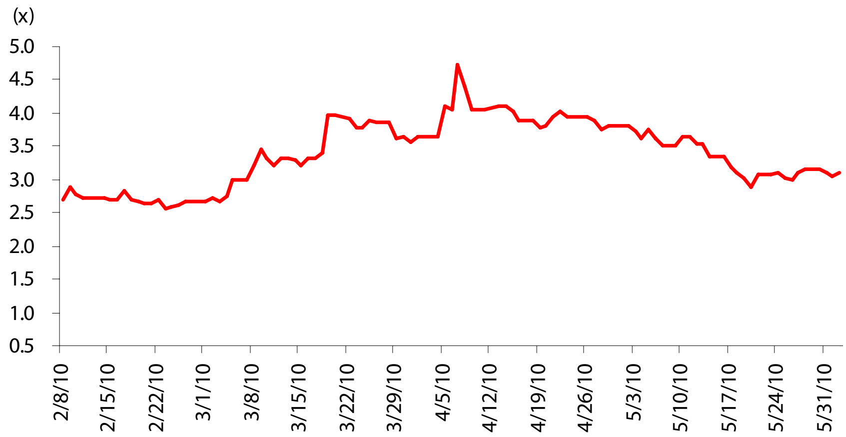
Source: Bloomberg, Centrum Research estimates

Exhibit 5: One-year forward EV/EBITDA



Source: Bloomberg, Centrum Research estimates

Exhibit 6: One-year forward EV/sales chart



Source: Bloomberg, Centrum Research estimates

Competition to intensify

Tier 2 and 3 cities offer higher potential….

Increasing store count to tap spending opportunity in tier 2 and 3 cities

Indian demographics have undergone a change fuelled by rising population, increasing urbanization, higher proportion of woman workforce and a rising middle class. Rising per capita income (Indian real GDP registered 8.5% CAGR growth over FY06-09; Source: Central Statistical Organisation) and evolving food habits (eating out and ordering in account for ~2.3% of the wallet share for social economic class A and B in urban areas) have resulted in the average consumer looking for convenient and reasonably priced restaurants for dine-in or take away.

A comparative analysis of monthly spends on eating out suggests that the proportion of households ordering in from outside and spending an average of more than Rs600 is higher in Tier 1 and Tier 2 cities as compared to Tier 3 cities.

Opportunity in tier 2 and 3 cities

Exhibit 7: Monthly spend on eating out per household

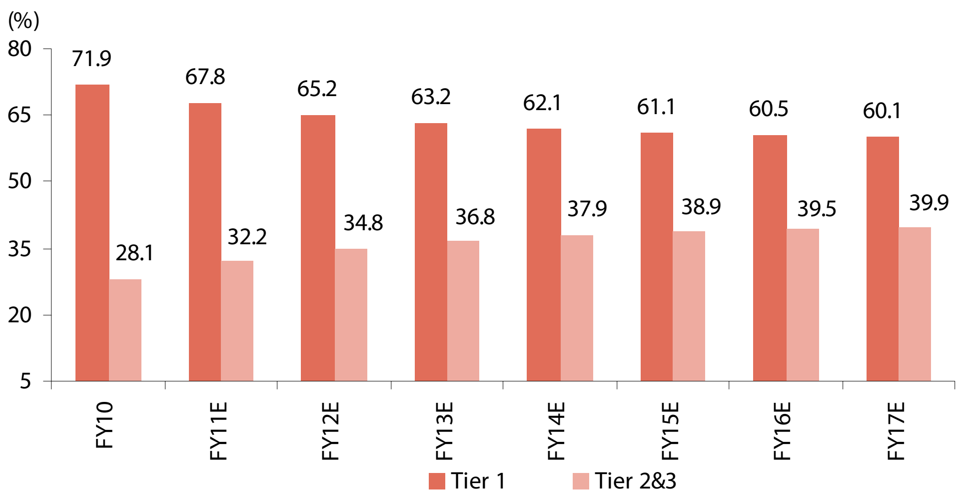
	Population Strata		
Monthly Spend	**Tier 1**	**Tier 2**	**Tier 3**
Avg (Rs)	671	691	351
Upto 50	13	13	20
51 – 100	12	13	17
101 – 200	19	17	22
201 – 300	12	11	13
301 – 600	18	23	14
601 +	26	23	14

Source: Company

To face intensive competition as other players gear up in such cities

Over the past couple of years, the influx of new entrants' viz. (McDonalds, Pizza Hut, TGIF, KFC, Subway, etc) has resulted in higher concentration of QSR players in the metros, which has led to lower energies and resources being expended towards opportunities in Tier 2 and Tier 3 cities. JFW has realized the mass potential offered by these cities and has steadily undertaken expansion activities over the past couple of years to tap this opportunity. Currently, ~ 70% of its stores are located in Tier 1 cities, with the balance spread over Tier 2 and Tier 3 cities. Going forward, the company plans to split store additions equally between Tier 1 and Tier 2 and Tier 3 cities so as to achieve balanced growth. We believe that such a move would increase its store presence in Tier 2 and Tier 3 cities from ~30.0% in FY10 to ~40% in FY17E.

Exhibit 8: Increasing store count in Tier 2 and Tier 3 cities



Source: Company, Centrum Research estimates

…..which may be under-realised on account of intensifying competitive pressure

We remain a bit cautious on the rapidly changing competitive landscape two to three years hence, as we expect a higher influx of existing and new organized players to realize this opportunity and compete for their share in this new pie. Our interaction with a few QSR players indicate that some are already in the process of expansion and others have finalised their strategy and plan to enter Tier 2 and Tier 3 cities over the next couple of years.

JFW's target customer base

Exhibit 9: JFW's target customer base – Urban Sec A & Sec B

		Estimated housholds (mn)			Distribution of households (%)		
Category	**Houshold income**	**All India**	**Urban**	**Rural**	**All India**	**Urban**	**Rural**
Deprived	<120,000	114	18	96	*51.5*	*26.1*	*63.1*
Aspirers	120,000 - 250,000	75	29	46	*33.9*	*42.3*	*30.2*
Middle class	250,000 - 1000,000	28	**19**	9	*12.8*	*27.4*	*6.2*
Rich	Over 1000,000	4	**3**	1	*1.7*	*4.3*	*0.6*
Total		**222**	**69**	**153**	***100.0***	***100.0***	***100.0***

Source: India Retail Report 2009

Urban households account for ~31% of the total household count (average of five members/ household). Of the total urban households (i.e. 69mn) ~ 10% belong to Sec A and 17% belong to Sec B (~ 22mn household of target opportunity). Since JFW is keen on targeting cities with a minimum household count of 20,000, this translates into a potential opportunity of 1,100 stores vs the existing coverage of 306 stores. If we extrapolate the same over the next ten years, then this translates into an opportunity of ~4,000 stores for the company in FY20E.

Store growth to be restricted by various limitations

However, we believe factors such as competitive pressure, availability of better catchments and acceptable store ROI, limitations of back-end to support higher store-count, together with density of population, may restrict the store count to only ~700 stores over the next 10 years.

Exhibit 10: Store-opening potential

Particulars	**FY10**	**FY20E**
Total population (bn)	1.1	1.3
Total household count (mn)	220	254
Urban households (mn)	69	361
Target urban households (mn)	22	112
Total stores (units)	1,100	3,918

Source: Indian Middle Class, Centrum Research estimates

Market expectations of higher IRR from a possible QSR tie-up may be unrealistic

We did a scenario analysis to find out what type of tie-up would be profitable for JFW. We believe a coffee and burger model would be IRR-decretive. Though a tie-up for branded sandwiches could be IRR accretive, it may face staunch competition from already established players (150 outlets for Subway in 25 cities).

Coffee shop model with IRR of 15.4% and Burger business with IRR of 25.0% to be IRR decretive

A closer look at the coffee shop business model reveals that the companies operating in such formats were impacted by lower average ticket sizes and lower volume churn, coupled with lower table rotations (since on average, consumers prefer to order their drinks over a conversation lasting about 30-60 minutes). We expect such formats to turn EBITDA positive after a minimum of two to three years, with a discounted payback period of eight to ten years to recoup investments. For instance, in the case of Café Coffee Day (CCD), its store IRR works out to only 15.4%, which is half that of JFW. We believe JFW should opt for a business model which would yield an IRR equal to or higher than its existing store IRR of 29.9%.

Premium coffee shop tie-up could weaken company's position

Premium coffee shops chains viz. Starbucks typically would require higher capex investment and would entail higher rental cost since they would require premium locations to attract their target customers (essentially SEC A) and would churn lower volumes on account of their premium pricing policy. Hence we believe any move in this direction would only weaken the position of the company.

Exhibit 11: Coffee shop business model IRR

Years	1	2	3	4	5	6	7	8	9	10
(Rsmn)										
Net Sales	2.5	3.2	4.3	4.7	5.0	5.2	5.4	5.7	5.9	6.1
Cost of Sales	2.8	3.3	3.8	4.0	4.2	4.4	4.6	4.7	4.9	5.1
EBITDA	(0.4)	(0.1)	0.5	0.7	0.7	0.8	0.9	0.9	1.0	1.0
EBITDA (%)	*(16.0)*	*(1.9)*	*11.8*	*14.6*	*15.0*	*15.9*	*15.8*	*16.3*	*17.2*	*16.9*
Capex	(2.5)									
NPV	0.5									
IRR (%)	***15.4***									

Source: Centrum research

Other optional models, viz. a burger chain, (in this case Mac Donald's); grossing a store level IRR of 25% is positioned below the rank of JFW. Mac Donald, with its reach of over 169 outlets pan-India, has managed to capture a huge chunk of the burger-eating market on account of its first-mover advantage. Though KFC is the close second, the company has still not managed to scale up its operations in the country. Entering into another burger tie-up would position the company as a third player in terms of positioning in the market and may not be a good proposition for the company.

Exhibit 12: Burger business model IRR

Years	1	2	3	4	5	6	7	8	9	10
(Rsmn)										
Net sales	41.7	50.1	62.6	68.9	72.3	75.9	79.7	82.9	86.2	89.7
Cost of sales	18.5	21.0	22.7	23.9	25.0	26.2	27.2	28.2	29.3	30.5
EBITDA	23.3	29.1	39.9	44.9	47.3	49.8	52.5	54.7	56.9	59.1
EBITDA (%)	*55.8*	*58.2*	*63.8*	*65.2*	*65.4*	*65.5*	*65.9*	*65.9*	*66.0*	*66.0*
Capex	(24.4)									
NPV	20.5									
IRR (%)	***25.0***									

Source: McDonald's India website, Centrum research

A branded sandwich franchiser such as Subway, with a store IRR of 33.2% and a discounted pay back period of 3.5 to 5 years, could be the preferred partner for JFW. However, since Subway deploys a pure franchisee play, it may not be available for partnership with JFW.

Branded sandwiches IRR accretive but may not be available for tie-ups

Exhibit 13: Branded sandwich business model IRR

Years (Rsmn)	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**
Net sales	8.1	9.7	12.1	12.9	13.6	14.3	15.0	15.6	16.2	16.9
Cost of sales	6.9	7.7	9.1	9.6	10.1	10.6	11.0	11.5	11.9	12.4
EBITDA	1.2	2.0	3.0	3.3	3.5	3.7	4.0	4.2	4.3	4.5
EBITDA (%)	*15.2*	*21.1*	*25.1*	*25.5*	*25.9*	*26.2*	*26.5*	*26.6*	*26.6*	*26.6*
Capex	(4.9)									
NPV	7.2									
IRR (%)	***33.2***									

Source: Centrum Research estimates

This strengthens our view that the high valuation premium assigned by the market is on account of expectations of higher IRR emanating from the new QSR tie-up and would not be sustainable (except in the case of the branded sandwich player), and hence may trigger a downward re-rating in the stock.

Airport retailing venture not an exciting opportunity

Airline opportunity to translate in less than 2% of existing sales

JFW has decided to go in for a brand new image by opting for the 20-20 look for most of its expected new store-roll outs. These stores would provide a combination of a youthful and vibrant appeal coupled with better interaction and ordering facilities and bigger dine-in space, which would help the company expand its consumer base. The capex required for such a format would be 5-10% higher than the existing apex per store.

The company's airport retailing venture, a footfall-driven model, is in sync with the strategy of expanding consumer base by opting for institutional tie-ups. The company has entered into a franchisee arrangement at airports, wherein the products (the basic raw materials i.e. flour vegetables etc) would be supplied by the company to the franchisee at a markdown, along with technology and secret recipes, in consideration for a fee (royalty/franchisee income), which we believe would be approximately in the range of 7%-10% (charged by competing pizza brands) and along with a non-refundable deposit.

However, our analysis suggests that this isn't a very significant opportunity, since it would translate into less than 2% of its existing sales. The total airline passenger traffic (pan-India) is estimated at 52.4mn in FY11, with Mumbai and Delhi accounting for ~60% of the pie (~31mn passengers). This translates into total franchisee sales opportunity of Rs0.2bn (Mumbai and Delhi accounting for ~0.1bn). While the company currently has only one store operational at Mumbai airport, it intends to target an additional ~30-40 airports (undergoing upgradation) over the next couple of years. We expect the airport venture to add Rs50-100mn to its topline over the next couple of years.

Exhibit 14: Airline franchisee opportunity

Y/E March (Rsmn)	**FY06**	**FY07**	**FY08**	**FY09**	**FY10**	**FY11E**	**FY12E**
Domestic pax nos (mn units)	25.2	35.8	44.4	39.5	45.9	52.4	57.9
Air pax growth (%)	*29.6*	*42.0*	*24.0*	*(11.1)*	*16.2*	*14.2*	*10.5*
Conversion (%)						*20.0*	*20.0*
Potential opportunity (Rsmn)						10.5	11.6
Average ticket size ~ (Rs)						150	150
Gross opportunity (Rsmn)						**1,572**	**1,737**
Franchisee fee (%)						*10*	*10*
Potential opportunity size (Rsmn)						**157**	**174**

Source: Centrum Research estimates

Scalable & profitable business model (JFW, Garcia & Smokin Joe's)

JFW has deployed a profitable (higher store IRR of 29.9%) and scalable business model (hub-and-spoke model). We believe the company's dual strategy of increased penetration in Tier 2 and Tier 3 cities and offering multiple price points (cheapest pizza at Rs39) would translate into 27.9% sales CAGR and SSSG in the higher single digits over FY10-12E.

Smokin Joes generates highest store IRR at 31.4% but loses out on scalability

We did a store-wise analysis to understand the dynamics and business model of various pizza companies operating in a similar environment. Our peer set includes Smokin Joe's, Garcia and JFW. Smokin Joe's was the clear winner, grossing the highest store IRR of 31.4% owing to its lean-cost structure and lower capex requirements (almost 1/3rd that of JFW). Smokin Joe's is a pure franchisee play, with 52 outlets spread across the country (the highest concentration is in Mumbai). The company's main source of income comprises franchisee fees (~10.3% of total revenues) and non-refundable deposit payable at the time of store-opening.

Unlike JFW, Smokin Joe's is solely reliant on the franchisee machinery to drive growth (it does not undertake aggressive expansion on its own). Also, the Smokin Joe's brand mainly relies on local marketing tactics, resulting in lower recall and brand equity, which in turn fails to attract a critical mass of customers for successful conversion. In addition, heavy dependence on a single metro (Mumbai) implies that an erosion in sales in this market from competition could impact its overall sales. Hence, although we are enthused by Smokin Joe's high store IRR, we have concerns about the scalability of its model.

Garcia at 18.4% a notch lower than JFW

Garcia's, on the other hand, grosses an IRR of 18.4% (lower returns and higher capex investment), positioning it a notch below JFW.

JFW, with a store IRR of 29.9%, distinguishes itself with its pan-India presence, strong brand equity, as well the profitability and scalability of its model. The company caters to a wide section of the population (the target audience ranges from the lower middle class to upper class), with a range of products at multiple price points (lowest price point at Rs39). The company enjoys superior reach (vis-à-vis other pizza players) with ~30.0% of its total stores located in Tier 2 and Tier 3 cities, where there is considerable potential given the scarcity of organized fast food retailers.

JFW also enjoys a higher brand recall and better brand equity, which enables it to clock higher conversion as a result of its efforts to reach out to and update its customers on its latest products (pasta campaign, choco-lava cake, re-introduction of cheese burst pizza and introduction of thin wheat crust) through a multi-pronged marketing effort, the latest being an on-line ordering mechanism.

On the operational front, the company employs the hub-and-spoke model. The four hubs (Noida, Mumbai, Bangalore and Kolkata) cater to the spokes (stores) by routing supplies at regular intervals. Centralized sourcing of materials at hubs ensures consistent quality coupled with better terms and economies of scale at a company level. Each hub (north and west) has the potential to support ~250 stores. Thus, the increase in the number of stores would help the company leverage the back-end cost over a higher number of stores, thereby resulting in operating efficiency. JFW's efficient operating structure, wider reach, increased penetration, multiple price point product offerings and higher brand equity makes it well-poised to grab a huge chunk of the rapidly growing organized food retail opportunity.

Exhibit 15: Smokin Joe's – business model

Years	1	2	3	4	5	6	7	8	9	10
(Rsmn)										
Net sales	**4.8**	**5.2**	**6.0**	**6.3**	**6.6**	**7.0**	**7.2**	**7.5**	**7.8**	**8.1**
Cost of sales	4.0	4.3	4.8	5.0	5.2	5.4	5.6	5.8	6.0	6.2
EBITDA	0.7	0.9	1.2	1.3	1.4	1.5	1.6	1.7	1.8	1.9
EBITDA (%)	*15.7*	*17.4*	*20.3*	*20.6*	*21.1*	*21.8*	*22.2*	*22.7*	*23.1*	*23.4*
Capex	(2.1)	16.7	19.5	19.7	20.2	20.8	21.3	21.8	22.2	22.5
NPV	2.9									
IRR (%)	***31.4***									

Source: Centrum research

JFW enjoys scalability

Exhibit 16: JFW – business model

Years	1	2	3	4	5	6	7	8	9	10
(Rsmn)										
Net sales	10.2	11.7	14.0	14.9	15.6	16.4	17.2	17.9	18.6	19.4
Cost of sales	8.4	9.3	10.5	11.0	11.4	11.9	12.4	12.8	13.2	13.7
EBITDA	1.8	2.4	3.5	3.9	4.2	4.5	4.8	5.1	5.4	5.7
EBITDA (%)	*17.2*	*20.1*	*25.3*	*26.0*	*26.8*	*27.4*	*28.0*	*28.4*	*28.9*	*29.2*
Capex	(6.2)									
NPV	7.6									
IRR (%)	***29.9***									

Source: Centrum research

Exhibit 17: Garcia's – business model

Years	1	2	3	4	5	6	7	8	9	10
(Rsmn)										
Net sales	5.1	5.9	7.0	7.4	7.8	8.2	8.5	8.8	9.2	9.5
Cost of sales	4.6	5.1	5.7	6.0	6.2	6.5	6.8	7.0	7.3	7.5
EBITDA	0.5	0.8	1.3	1.4	1.5	1.6	1.7	1.8	1.9	2.0
EBITDA (%)	*9.1*	*13.3*	*19.1*	*19.2*	*19.5*	*20.0*	*20.2*	*20.5*	*20.8*	*21.0*
Capex	(3.6)									
NPV	1.4									
IRR (%)	***18.4***									

Source: Centrum research

Exhibit 18: Comparison snapshot

Parameters	Domino's	Smokin Joes	Garcia
No of outlets	306	52	20
Average store size	1,100	500	600
Penetration	Tier 1& Tier 2	Tier 1& Tier 2	Only Mumbai
Home delivery (%)	*85.0*	*95.0*	*85.0*
S&D (%)	*5 - 6%*	*2 - 2.5%*	*5%*
Capex per store (mn Rs)	6.2	2.1	3.6
IRR (%)	*29.9*	*31.4*	*18.4*
NPV	7.6	2.9	1.4
Ownership	Own Stores	Franchisee	Own+Franchisee
Royalty	3.0	10.0	7.0

Source: Centrum research

Lower sales in Tier 2 and 3 cities to be cushioned by higher margins

Tier 2 & 3 towns marred by lower volumes

Exhibit 19: Mature Tier 1 and Tier 2 cities (in mature year)

(Rsmn)	Tier 1	Tier 2
Net sales	15	10
Total op cost	11	8
EBITDA	4	3
EBITDA (%)	*25.5*	*26.9*

Source: Company, Centrum research

The company adopts a uniform pricing policy for its product offerings across the country. In the absence of differential pricing, the sales in Tier 2 and Tier 3 cities are lower by ~30% vs Tier 1 cities, primarily on account of lower volumes emanating from lower frequency of orders and repeat visits. Despite lower sales, outlets in Tier 2 cities are able to garner higher operating margins on account of certain operating cost efficiencies (lower staff and administration expense advantages). As a result, these outlets generate higher operating margins than Tier 1 counterparts.

We believe that expanding in such cities would be margin accretive and help the company build scale and salvage its overall operating margins (at company level) in a scenario of intensive competition from other players.

Any increase in sales from such cities would only add to the margins. We expect the overall EBITDA margins to expand by 88bp from 16.0% in FY10 to 17.0% in FY12.

Exhibit 20: Base case and best case scenario for Tier2 and Tier 3 cities

	Base case	Best Case
(Rsmn)	Tier 2	Tier 2
Net sales	10	15
Total op cost	8	9.7
EBITDA	2.8	5.2
EBITDA (%)	*26.9*	*34.7*

Source: Company, Centrum research

Fully-funded for growth

Company auto-funded by internal accruals and working capital

JFW operates on a negative cash conversion cycle, similar to most of the food retailers operating in this segment. This can be attributed to lower debtor days on account of spot cash purchases made by the consumer and higher creditor days (56 days in FY11E) on account of higher credit period extended by its vendors for purchase of consumables /goods. With the help of customer relationship management (CRM) and local sales marketing (LSM) strategies, the company has consistently maintained a higher churn of inventory, resulting in lower inventory days (at 24 days in FY11E).

This frees up the company's cash flows from being blocked in a working capital cycle. Strong internal accruals and negative working capital cycle would help the company augment its cash flows, which in turn could be utilized towards funding its expansion plans. This would elevate the company towards a growth trajectory, whilst enabling it to be self-reliant in meeting its funding requirements. The company is expected to turn debt-free by FY11E and surplus cash is expected to increase by 12.4x to Rs495mn in FY12E from Rs40mn in FY10E.

Exhibit 21: Funded sufficiently by internal accruals and working capital

Y/E Mar (Rsmn)	FY10E	FY11E	FY12E	FY13E	FY14E
Fund generation					
Internal accrual	664	724	879	1,052	1,243
Debt	(739)	(86)	0	0	0
Share capital	605	0	0	0	0
Total fund generation	**531**	**638**	**879**	**1,052**	**1,243**
Fund requirements					
Total capex	517	542	447	433	354
Net working capital	(118)	(204)	(189)	(193)	(198)
Interest	91	5	(0)	(0)	(0)
Dividend	0	98	126	162	207
Total fund required	**490**	**440**	**384**	**402**	**363**
Surplus	**40**	**197**	**495**	**650**	**880**

Source: Company, Centrum Research estimates

Financial Analysis

27.9% revenue CAGR over FY10-12E

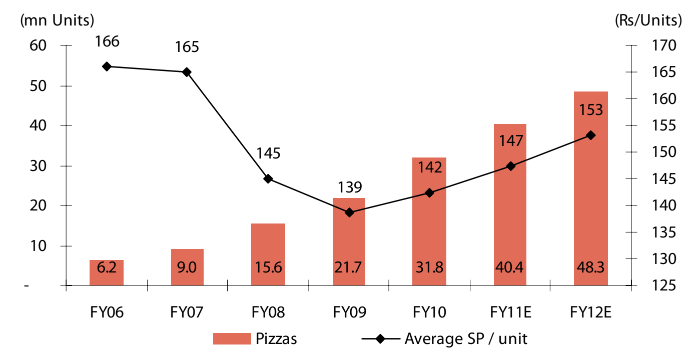
Higher growth from tier 2 & 3 cities due to lower base effect

We expect JFW to clock 27.9% revenue CAGR over FY10-12E to Rs6.9bn on the back of store additions (200 store additions spread over FY10-12E) and 4.5% CAGR in average sales per store over to Rs18.1mn. The growth at store level would be propelled by 23.2% CAGR in pizza volumes and 3.7% CAGR in average selling price per unit. This is in sync with the company's strategy to concentrate on volume growth over price growth.

Our assumption for growth in average sales per store is based on higher growth emanating from Tier 2 and Tier 3 cities over Tier 1 cities on the back of under-penetration and lower base effect.

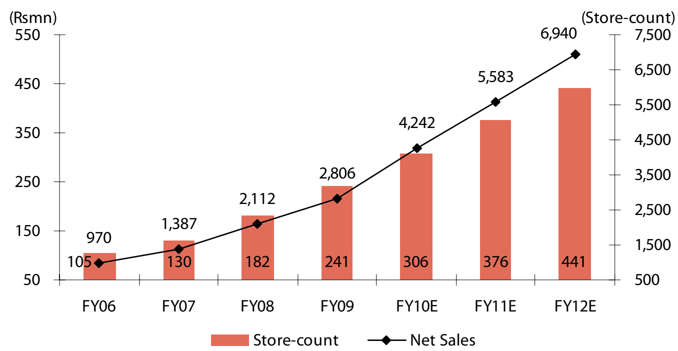
During FY07-09, the company witnessed 55.5% CAGR in pizza volumes over -8.3% CAGR in average pizza prices, primarily driven by introduction of products at lower price points (viz. pizza mania). In FY10, the company has undertaken a miniscule price increase (2.5%) in average pizza price. We believe the company has reached its lowest price point per pizza. Going forward, we expect a steady increase in average price per pizza.

Exhibit 22: 3.7% CAGR increase in average selling price per pizza (FY10-12E)



Source: Company, Centrum Research estimates

Exhibit 23: 1.4x Increase in store-count



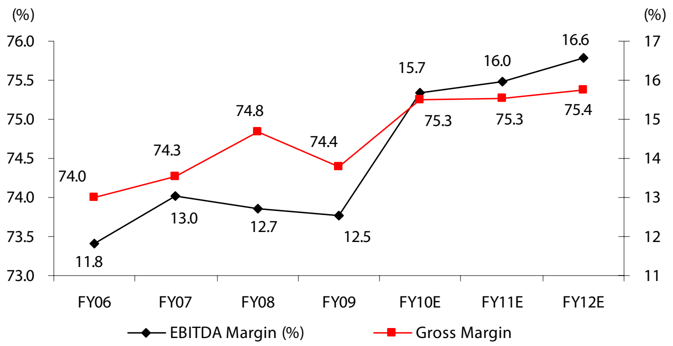
Source: Company, Centrum Research estimates

No significant expansion in operating margins

Company to shift to single digit SSSG

Cheese, chicken and pizza base form the core raw materials required for manufacturing the product. We expect the company's gross margins to remain unaffected, since any increase in cost of raw materials would be passed onto the consumer. The earlier trend where the company's operating leverage was de-leveraged on account of higher proportion of new stores (32.4% of old stores in FY09) is likely to reverse as a higher proportion of old stores are expected to mature and contribute effectively and the proportion of new to average stores is expected to decline. The company is also expected to register higher SSSG, which, coupled with operating leverage, would result in 88bps improvement in operating margin to 16.6% over FY10-12E.

Exhibit 24: 88bp expansion in EBITDA margin



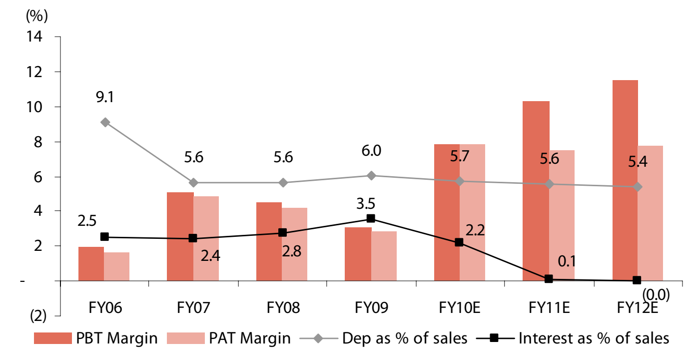
Source: Company, Centrum Research estimates

Exhibit 25: Higher SSSG & lower proportion of new stores

Source: Company, Centrum Research estimates

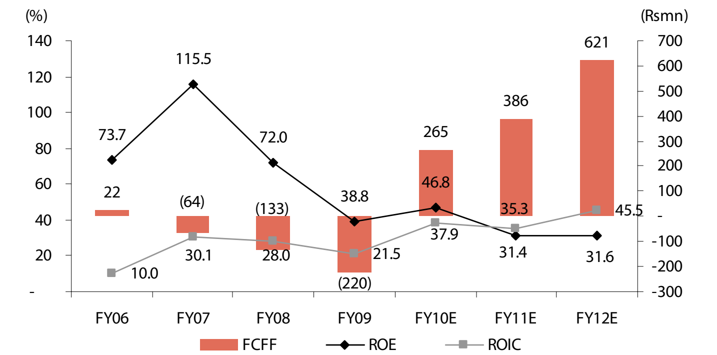
FCFF to turn positive in FY10

Exhibit 26: 369bp improvement in PBT margin



Source: Company, Centrum Research estimates

Exhibit 27: Higher ROIC



Source: Company, Centrum Research estimates

ROE to decline by 1,516 bps to 31.6% in FY12E.

Higher PBT (flowing though higher sales and operating leverage) and negative working capital cycle are expected to help the company generate 16.8% CAGR in operating cash flows over FY10-12E to Rs1bn. We expect the company to turn FCFF positive at Rs265mn (52.9% CAGR over FY10-12E) for the first time in FY10 after a lag of three years. This, together with the IPO proceeds of (Rs580mn), would help the company pay off debts of Rs739mn. This is evident from the debt-equity ratio which has reduced from 3.4x FY09 to 0.1x FY10. Further, in FY11, we expect the company to retire its balance debt and turn completely debt free.

759 bps improvement in ROIC on lower invested capital

We expect the ROIC to improve by 759bp from 37.9% in FY10E to 45.5% in FY12E on the back of lower invested capital (efficiencies emerging from working capital) and higher cash flow entering the system. We expect the ROE to decline by 1,516bps from FY10E to 31.6% in FY12E on the back of lower financial leverage (paid off entire debt) and lower net profit margin, since the company would fall within the purview of the full tax bracket.

Exhibit 28: ROE decomposition chart

ROE Decomposition	FY10	FY11E	FY12E	FY13E
Net profit margin (%)	*7.8*	*7.5*	*7.8*	*8.3*
Asset turnover (x)	3.6	4.1	4.1	3.9
Financial leverage (x)	1.6	1.0	1.0	1.0
ROE (%)	*46.8*	*31.4*	*31.6*	*31.9*

Source: Centrum Research estimates

27.5% adjusted PAT CAGR over FY10-12E

We expect the PAT to grow at a CAGR of 27.5% to Rs538mn. We expect the company to come within the full tax bracket of 34% FY12E onwards on account of carry forward losses that are expected to be offset only by the middle of FY11E.

Conclusion

Though we are impressed by the profitability and scalability of JFW's business model, we believe the current stock price is at a significant premium, primarily factoring in growth expectations from possible new tie-ups, which in our opinion is unwarranted.

We also remain cautious on the competitive landscape emerging over the next two to three years, as a large number of new entrants swarm Indian markets and existing players foray into Tier 2 and Tier 3 cities. We also believe selection of the right format is quintessential for maintaining the overall profitability growth, the absence of which would be detrimental for growth.

Hence, we initiate coverage on JFW with a Sell rating and a target price of Rs230 (implied P/E of 27.3x FY12E), indicating a downside potential of 18.4% from the current levels.

Risks

Upside risks

- Higher-than-expected store roll-outs could surpass our assumption and sales growth.
- New initiatives if value-accretive (ie, higher store IRR), would result in upward revision in earnings.

Downside risks

- Delays in rollout of stores would impact estimates
- Competition from other national and international pizza chains (viz. Pizza Hut, Papa John's Smokin Joe's and Pizza Corner) which would lead to lower demand, downward pressure in prices, reduced margins and inability to take advantage of new business opportunities on account of lower market share could affect our earnings growth assumptions
- Company may enter into tie-up for a format whose business model may be unviable

Annexure

JFW's strengths

Exclusive master franchisee agreement with Dominos International: JFW runs the Dominos Pizza chain in India through an exclusive franchisee for Domino International (DI). It has the exclusive right to develop and operate Dominos pizza delivery stores and the associated trademarks in the operation of stores in India, Nepal, Bangladesh and Sri Lanka. The company entered into a fresh agreement with Dominos International in January 2010, wherein it would be required to open 300 stores over the next 15 years (till FY24). In the absence of its ability to do so, the same would be categorized as a technical default. We expect the company to achieve a total of 300 store additions over FY11E-15E, which would protect the company against any such default.

Scouting for institutional tie-ups and better catchments to promote sales: JFW undertakes financial and operational analysis of the location before opening its stores. Operational aspects include surrounding household count, location visibility, presence of competition; as well as presence of corporate and other institutions. The major financials aspects include rentals and the return on investment generated at the store level. Company's growth strategy includes targeting areas which would give them the advantage of higher footfalls such as:

- Locations near metros – set-up small kiosks and serve off-the-shelf pizzas;
- Tie-ups with institutions and corporate to set up stores in campuses (minimum of 10,000 employees); and
- Inside or surrounding educational institutions.

The company requires a total of 35-45 days of lead time to open stores at a finalized location.

Standardized internal processes, operating discipline to help achieve operational excellence: The company has standardized internal processes which contribute towards improving the average delivery time (existing 22.5min) per order. Apart from undertaking various employee training programs, the company continuously reviews its tore operations, on various parameters viz. compliance with product quality, customer service, store branding, safety and security, sanitation, delivery policies, standards and specifications.

Rewarding employees: JFW encourages its store managers to take on store accountability and motivates them by providing variable incentives linked to their store-wise performance. All costs attributable to a store are charged at the store-level and the store manager has been given the autonomy to take actions to increase sales or reduce costs. Store-level comprises one store manager entrusted with overall store supervision, along with two to three shift managers. The company's comprehensive training program is structured to provide for further development of their employees.

Use of innovative marketing tools:

- **Customer relationship management:** Details of a customer's transactions from point of sale software are utilized to send customized communication including mobile text messages and offers relevant to the consumer in order to stimulate the frequency of orders.
- **Local sales marketing:** Aimed at increasing customer penetration by targeting new customers and increasing frequency of repeat orders from existing customers. This includes address mapping the entire delivery area, weekly area-wise comparative sales analysis and targeting areas with lower sales where sales are lower vide door hangers; fliers, etc.
- **National marketing campaigns on television, print and radio:** National advertising campaigns, which include our "*Hungry Kya*?", "30 minutes or free" and "*Khusiyon Ki Home Delivery*" (Happiness Delivered Home).
- **Web-based order:** The company has forayed into web-based orders in three cities on an experimental basis viz. Mumbai, Bangalore and Delhi. We expect the company to benefit from this new initiative, since it does not entail any corresponding manpower costs and people generally prefer to upgrade their orders online.

Robust supply chain network to promote cost efficiencies: The company has established four regional commissaries based in Noida (Delhi NCR), Mumbai, Bangalore and Kolkata. These commissaries primarily manufacture dough (base of the pizza) and act as warehouses for most of the other ingredients. The company undertakes centralized purchase of primary raw materials (viz. cheese, vegetables and meat) which are then transported to stores within the geographical proximity of one day. This helps the company negotiate better prices with their suppliers and reap economies of scale. The company adopts a multi-vendor policy to minimize over-reliance on a single vendor and ensure steady supply of raw materials. The company also has a dedicated fleet of refrigerated trucks to help timely and temperature-controlled delivery of their ingredients in a timely manner, thereby ensuring quality and minimizing wastage.

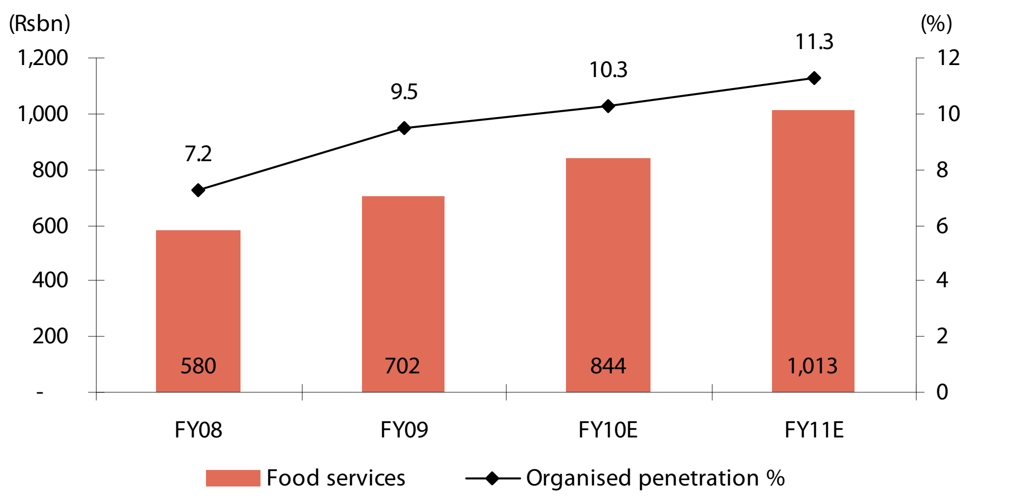
Technology support: The company uses 'Vision', a POS cash register software system, to record store-wise sale transactions and verify sales data. Vision is targeted to the QSR segment with features including food cost indenting and control, labour management, kitchen handling, multiple payment and security options and CRM database. The company's commissaries are currently working on ERP planning-BAAN module. The company has launched an interactive voice response system in Mumbai, NCR of Delhi and Bangalore, which intelligently routes the customer to the nearest store.

Changing demographics to propel QSR growth

As per the *Food Franchising Report 2009* brought out jointly by FICCI-CIFTI and Franchise India Holdings, the Indian food services industry is estimated at Rs580bn. Organized players account for 7.2% of the total industry. Changing demographics (large young population with median age of 24 years, increasing trend towards nuclear families in urban areas, rising number of female professionals and the advent of double-income household) coupled with higher per capita income have propelled the surge in demand for convenient and reasonably-priced fast food restaurants in the country.

Quick service restaurants (QSR) on account of their attributes (high speed service and efficiency, convenience, limited menu choice and service and value prices) measure up to the expectations of the urban population and hence are gaining momentum across the country. We expect this industry to register 20.4% CAGR over FY09-11E to Rs1trn, with the organized sector accounting for 11.3% of the market size in FY11.

Exhibit 29: Food service industry

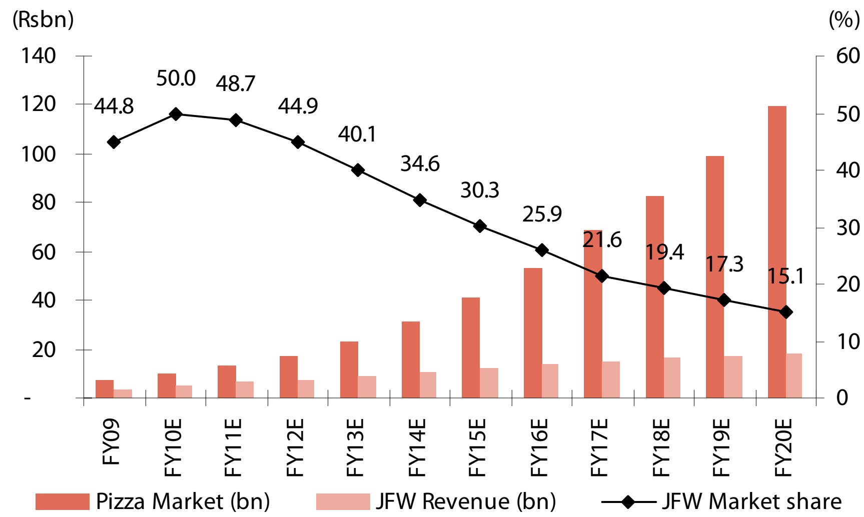


Source: Food franchising report 2009, Images F&B Research and Centrum Research Estimates

Management consultancy firm, Technopak, in its report on the food sector in 2009, estimates that only 2.0% of the monthly expenditure in ordering is spent on pizzas and pastas on a monthly basis. South Indian dishes are the most preferred (44%), followed by North Indian (26%) and Chinese (12%). We believe that with increasing westernization and higher proportion of youngsters willing to experiment with regard to their taste buds, the consumer base for the pizza and alternative westernized product offerings will only improve and achieve wider acceptance, going forward.

The Indian pizza market, estimated at Rs7bn (in FY09), is expected to grow at 35-40% over the next two years to ~Rs17.2bn in FY12E (*Source: Food Franchising Report 2009*). Though the overall size of the market would increase, we expect JFW's market share in overall pizza market to decline, with increased competitive pressure and new entrants embarking into the market, coupled with a shift to single digit average SSSG for the company. We expect JFW's market share to decline from ~50% in FY10 to 44.9% in FY12 and further to 15.1% in FY20.

Exhibit 30: Share of JFW in the pizza market



Source: Food franchising report & Centrum Research estimates

Franchising – An effective way of scaling up

In conjugation with a strong brand equity or critical mass

Franchising presents a great opportunity to grow faster without investing heavily in the business and without losing the entrepreneurial streak which is important to push sales, while managing costs efficiently. Going forward, the retail franchising industry would gain further prominence, with brands and retailers continuing to see franchising as an efficient expansion route once critical mass is achieved. The Indian franchising industry is estimated at US$7.2bn and is expected to grow at a CAGR of ~30% to Rs20bn by 2013E (*Source: Food Franchising Report 2009*). The trend would favour larger/more mature franchisees rather than traditional single-store franchisees, as brands would find it challenging to deal with diverse individual franchisees.

The positive attributes of franchising have already made the concept quite popular amongst the already organized QSR players in the segment. We believe that such engines will only fuel growth by helping companies achieve a wider network and presence.

We, however, believe that a franchisee can only be remunerative if the company enjoys a strong brand equity (domestically or globally) or has reached its critical mass, since implementing a franchisee model by itself (e.g. Smokin Joe's) exposes companies to a higher gestation period to achieve higher absolute sales and profitability.

Key considerations for running a profitable restaurant business

To develop a successful economic proposition for a restaurant business, the top three considerations would be:

1. **Getting in-depth understanding of the core target audience:** It is important to identify the target audience, which would help sharpen the product offering, pricing strategy and brand communication. Age and social status, income or socio-economic category (SEC) and customer mindset are the quintessential parameters in determining the target audience.

2. **Developing a comprehensive offering – food, experience and value:** Apart from food (which is the core product being sold), experience and value (especially in a price sensitive country) plays a critical role in this process. Experience includes the ambience and service standards and should be in line with the classification of restaurants. Depending on the aforementioned factors, there are five categories of restaurants.

Exhibit 31: Categories of restaurants

Categories	Restaurants
Fine dining	Olive, China Club, Indigo, 5-star restaurants
Upscale casual dining	Pizza Express, Pizzeria, Shalom etc
Mid-scale casual dining	Pizza Hut
Fast casual dining	Nirula's, Sagar, Sarvana Bhavan etc
Quick service restaurants	Mc Donald's, KFC, Smokin Joes, Dominos

Source: Company, Centrum Research

Value is the customer's perception of product pricing in relation to the offering.

Value = (Food +Experience) / Price

It is imperative that the restaurant owners try to find the sweet spot, (a price range) where the product is affordable to TA without denting the product credibility. Factors such as low entry points, low exit prices, charging competitive prices for comparable products, charging premium for special and unique product offerings, developing permanent value layers if required may be

3. **Good catchments:** Ability to attract higher footfalls and conversion is also determined by location, which needs to have good visibility, accessibility, closeness to target audience, large frontage etc. In some cases, brands compromising on location in return for revenue-sharing deals with landlords may stand to lose in the long run.

Financials

Exhibit 32: Income statement

Y/E March (Rsmn)	FY09	FY10	FY11E	FY12E	FY13E
Net Sales	2,806	4,242	5,583	6,940	8,369
-Growth (%)	*32.9*	*51.2*	*31.6*	*24.3*	*20.6*
Cost of goods sold	718	1,050	1,381	1,708	2,071
% of sales	*25.6*	*24.7*	*24.7*	*24.6*	*24.8*
Gross profit	2,088	3,192	4,202	5,231	6,297
% of sales	*74.4*	*75.3*	*75.3*	*75.4*	*75.2*
Staff expenses	556	805	1,056	1,315	1,570
% of sales	*19.8*	*19.0*	*18.9*	*18.9*	*18.8*
Manufacturing and admin	887	1,274	1,654	2,028	2,416
% of sales	*31.6*	*30.0*	*29.6*	*29.2*	*28.9*
S&D	199.4	305.3	411.4	505.3	600.1
% of sales	*7.1*	*7.2*	*7.4*	*7.3*	*7.2*
Franchisee Fee	94.5	142.9	188.1	233.8	281.9
% of sales	*3.4*	*3.4*	*3.4*	*3.4*	*3.4*
EBIDTA	351	665	892	1,150	1,429
-EBIDTA margin (%)	*12.5*	*15.7*	*16.0*	*16.6*	*17.1*
Depreciation	169	243	311	374	429
EBIT	182	422	581	776	1,000
Interest expenses	99	91	15	10	10
PBT from operations	83	330	567	766	990
Other non operating income	4	1	10	33	70
PBT	87	332	577	798	1,060
-PBT margin (%)	*3.1*	*7.8*	*10.3*	*11.5*	*12.7*
Provision for tax	8	1	159	260	367
Effective tax rate (%)	9.2	0.2	27.5	32.6	34.6
Exceptional items	5.9	-	-	-	-
PAT	73	331	419	538	693
Adjustment for Extraord. items	6	-	-	-	-
Adj PAT	79	331	419	538	693
-Growth (%)	*(11.7)*	*319.8*	*26.5*	*28.6*	*28.8*
-Net profit margin (%)	*2.8*	*7.8*	*7.5*	*7.8*	*8.3*

Source: Company, Centrum Research Estimates

Exhibit 33: Balance sheet

Y/E March (Rsmn)	FY09	FY10E	FY11E	FY12E	FY13E
Share capital	582	648	648	648	648
Reserves & surplus	(342)	526	847	1,259	1,790
Total shareholder's fund	240	1,174	1,495	1,907	2,438
Loan fund	824	86	-	-	-
Total capital employed	**1,065**	**1,260**	**1,495**	**1,907**	**2,438**
Gross block	1,710	2,238	2,795	3,242	3,689
Accumulated depreciation	644	888	1,199	1,573	2,002
Net Block	1,065	1,350	1,596	1,669	1,687
Capital WIP	89	79	63	63	49
Net fixed assets	1,155	1,429	1,659	1,733	1,736
Investments	-	-	-	-	-
Cash and bank	31	70	279	806	1,526
Inventories	55	71	90	110	131
Debtors	12	29	20	25	30
Other current assets & loans	239	362	417	470	526
Total current assets & loans	337	533	805	1,410	2,213
Current liabilities & provisions	427	702	970	1,236	1,511
Net current assets	(90)	(169)	(165)	174	702
Total assets	**1,065**	**1,260**	**1,495**	**1,907**	**2,438**

Source: Company, Centrum Research estimates

Exhibit 34: Cash flow

Y/E March (Rsmn)	FY09	FY10E	FY11E	FY12E	FY13E
Cash flow from operating					
Pre tax profit from operations	81	332	577	798	1,060
Depreciation	169	243	311	374	429
Interest expenses	86	91	5	(0)	(0)
Dividend income	(0)	(1)	(10)	(33)	(70)
Others	3	-	-	-	-
Operating profit bef. WC change	339	665	882	1,140	1,419
Working capital adjustments	(11)	118	204	189	193
Direct tax paid	(8)	(1)	(159)	(260)	(367)
Net cash from operating	**321**	**783**	**928**	**1,068**	**1,245**
Cashflow from investing					
Capex	(541)	(517)	(542)	(447)	(433)
Investments	(2)	(0)	0	-	-
Int/divid. rcvd/sale of securities	0	1	10	33	70
Net cash from investing	**(542)**	**(516)**	**(531)**	**(415)**	**(363)**
Cash flow from financing					
Proceeds from sh. Cap & premium	-	606	-	-	-
Borrowings/(Repayments)	311	(739)	(86)	-	-
Interest paid	(83)	(91)	(5)	-	-
Dividend paid	-	-	(98)	(126)	(162)
Net cashflow from financing	**228**	**(224)**	**(188)**	**(126)**	**(162)**
Net cash increase/(decrease)	**7**	**43**	**208**	**527**	**720**

Source: Company, Centrum Research estimates

Exhibit 35: Key Ratios

Y/E March	FY09	FY10E	FY11E	FY12E	FY13E
Profitability ratios (%)					
EBIDTA margin	12.5	15.7	16.0	16.6	17.1
PBIT margin	6.5	9.9	10.4	11.2	11.9
PBT margin	3.1	7.8	10.3	11.5	12.7
PAT margin	2.8	7.8	7.5	7.8	8.3
Growth (%)					
Revenue	32.9	51.2	31.6	24.3	20.6
EBIDTA	30.9	89.2	34.2	28.8	24.4
Net profit	(11.7)	319.8	26.5	28.6	28.8
Return ratios (%)					
ROCE	20.8	36.3	30.8	31.0	30.4
ROIC	21.5	37.9	35.3	45.5	65.6
ROE	38.8	46.8	31.4	31.6	31.9
Turnover ratios					
Asset turnover ratio (x)	3.2	3.6	4.1	4.1	3.9
Working capital cycle (days)	(30.9)	(33.7)	(31.4)	(29.7)	(28.0)
Average Inventory period (days)	23.9	21.9	23.7	23.4	23.1
Average collection period (days)	1.6	1.8	1.3	1.3	1.3
Average payment period (days)	56.4	57.4	56.4	54.4	52.4
Per share (Rs)					
Basic EPS	1.3	5.2	6.5	8.4	10.8
Fully diluted EPS	1.4	5.2	6.5	8.4	10.8
Book value	4.1	18.4	23.4	29.8	38.1
Solvency ratio					
Debt-equity	3.4	0.1	-	-	-
Interest coverage ratio	2.0	4.6	129.0	NM	NM
Valuation (x)					
P/E	208.2	54.5	43.1	33.5	26.0
P/BV	68.5	15.4	12.1	9.5	7.4
EV/Sales	6.1	4.3	3.2	2.5	2.0
EV/EBIDTA	48.9	27.1	19.9	15.0	11.5
M-cap/Sales	5.8	4.3	3.2	2.6	2.2

Source: Company, Centrum Research estimates

Appendix A

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