



## Devyani International Limited Q4 FY22 Earnings Conference Call May 2, 2022

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**Moderator:** Ladies and gentlemen, good day and welcome to the Earnings Conference Call of Devyani International Limited. Please note that this conference is being recorded. I now hand the conference over to Mr. Anoop Poojari from CDR India. Thank you, and over to you sir.

**Anoop Poojari:** Thank you. Good afternoon everyone and thank you for joining us on Devyani International's Q4 and FY22 earnings conference call. We have with us Mr. Ravi Jaipuria, Chairman of the Company; Mr. Raj Gandhi, non-Executive Director; Mr. Virag Joshi, CEO and Whole-time Director and Mr. Manish Dawar, CFO and Whole-time Director of the Company. We will initiate the call with opening remarks from the management, following which we'll have the forum open for a question-and-answer session. Before we begin, I would like to point out that some statements made in today's call may be forward-looking in nature, and a detailed statement in this regard is available in the results presentation shared with you earlier. I will now request Mr. Ravi Jaipuria to make his opening remarks.

**Ravi Jaipuria:** Good afternoon everyone. A warm welcome to you all on our earnings conference call to discuss the business performance for the quarter four and full year ended March 31, 2022. I hope you and your families are keeping safe and healthy. We are emerging from a challenging period with multiple COVID related disruptions last year and the year before and unprecedented inflation in input costs, highly tensed geopolitical situation and disturbed logistics around the world. DIL has shown great resilience during this period, and our unwavering commitment and focus on the growth has translated FY2021-22 into a record year of performance for the company. We opened 246 new stores in FY2021-22, the highest ever for our company. Alongside, we also witnessed record revenues, best margins and record delivery of profits. The year also saw for us a very successful IPO Listing and a strong support from all of you. Our brands achieved significant milestones, whereby KFC India crossed rupees INR 1,000 crore revenue and Pizza Hut clocked more than INR 500 crore revenue this year.

Expansion of our store network and a strong focus on costs have been the key pillars of the performance this year. As of March 31, 2022, we operated 364 KFC stores, 413 Pizza Hut and 55 Costa Coffee stores in India. Our total system store count at the end of the year stood at 938 stores of all our brands. I'm pleased to inform you that strong store additions and the strength of our brands helped us achieve full year revenues of INR 2,084 crore, nearly double the figure last year.

Our core brands - KFC, Pizza Hut and Costa Coffee have performed well, led by new innovative product launches coupled with continuous focus on safety, health and hygiene. Dynamic cost management ably supported the business teams and ensured strong profitability. As an example, due to well-timed forward contracts of key raw materials, we have managed the input cost effectively. This gets demonstrated by the stable gross margins despite multi-year high inflation. In Q4, gross margins at 71.3% remained nearly flat on quarter-on-quarter and year-on-year basis. We pride ourselves on our financial discipline and this has helped us in

expanding our FY22 consolidated pre-IndAS EBITDA margin to 14.4% from 8.1% last year. As a result, I'm very happy to inform all of you, our shareholders, investors and the analyst community that we have posted a net profit of INR 155 crore for the year. We continue to invest in our employees and in our operations, which we believe will support our growth aspirations in the coming years.

Innovation is a key focus area for us. We launched several new products and innovative campaigns within our core brands during the quarter. KFC launched the KFC Bucket Canvas campaign and released a unique product, the KFC Biryani Bucket. Pizza Hut came out with multiple innovations during the year like Momo Pizza, Hand Tossed Pizza, original San Francisco Thin crust pizza and new sides. All of these new launches reported strong consumer acceptance and we look forward to upscaling this as we go along in the future years. Costa Coffee too is set to launch a whole new range of drinks and refreshers for this summer season.

Along with our operations, we are equally focused on diversity in our business to give greater opportunity for the growth of our women employees. We are opening women-only stores across our core brands of KFC, Pizza Hut and Costa. We are currently operating more than 20 women-only stores as on March 31, 2022 and are also working on increasing the number of women team leaders across our business.

As we are all aware, external macro environmental continues to remain challenging and we do foresee certain headwinds. Cost of key input materials and capital items continue to see significant inflation, and this is likely to persist for some time. We are also witnessing early signs of a potential resurgence in a new COVID variant. With a PAN India footprint, we are closely monitoring the developments. Our scale, brand strength and experience give us the confidence that we will be able to effectively face these challenges. Despite the ensuing headwinds, we remain firm believers in the potential of food service industry and more particularly the QSR segment in India.

Significant growth opportunities are available for a well operated and a well-capitalized player. Our brands are geared to cater to the young Indian consumers' expectations, meeting their challenging lifestyle and eating out habits. We confidently look forward to another year of growth. With this, I would like to conclude my address and I will now hand over to Manish for his comments. Thank you.

**Manish Dawar:**

Thank you, Mr. Jaipuria. Good evening, everyone. A warm welcome to all of you for your valuable time and presence on our FY22 earnings conference call, our third results call post the listing in August 2021.

As mentioned by the Chairman earlier, we had a record FY22. We added a total of 246 net new stores during the year, led by 116 stores for Pizza Hut, 100 stores for KFC and 11 stores for Costa Coffee. Aspiration for Western QSR food goes well beyond the metros and tier-one cities in the new India. Recognizing this, we've expanded our footprint to nearly 50 new cities this year, and we are now present in 200 plus cities PAN India. Non-metro cities now constitute a marginally higher share of our revenue, compared to what we've done historically. Our international business also added nine net new stores bringing our total system store count to 938 at the end of March 2022.

Mirroring our strong store opening performance, our revenues for FY22 grew almost 84% year-on-year to reach INR 2,084 crore versus INR 1,135 crore in FY21. Gross profits increased 88% year-on-year to INR 1,484 crore versus INR 790 crore last year. Store level profitability further benefited from leverage on higher sales and continuing benefits from long-term initiatives that we've taken in the last two to three years. Brand contribution margin, a key KPI for us, improved to 19.9% in FY22 versus 14.4% last year. This helped us drive the pre-IndAS EBITDA to INR 300 crore, the highest figure ever, with margins also markedly improving to 14.4% versus 8.1%

a year earlier. As a result, net profit from continuing business stood at INR 155 crore for the year versus a loss of INR 81 crore in FY21. Please bear in mind, that the net profit number of INR 155 crore includes the recognition of deferred tax asset during Q4.

Our core brands demonstrated great resilience and continued strength this year. At KFC, as I said earlier, we added 100 new stores to reach 364 stores at the year end. Average daily sales (ADS) for the year came in at nearly INR 117,000 per store, representing 49.4% SSSG over FY21. Again, we need to bear in mind that FY21 numbers were not fully representative because the year got impacted due to COVID situation. But again, there have been some impact of COVID in the current year also, and therefore, the numbers are, to that extent, a little incomparable. Full year revenues came in at INR 1,219 crore, 89% higher compared to last year. Operational leverage and better cost management helped improve brand contribution to 21.3% from 18.3% a year earlier.

Pizza Hut added 116 net new stores to reach 413 stores at the year end. SSSG at 45.4% for the year helped brand post ADS of INR 43,000. Revenues at INR 532 crore increased 85% year-on-year. Profitability for Pizza Hut was again stronger with brand contribution margin at 16.3% versus 12.9% a year ago.

At Costa Coffee, we added 11 net new stores to reach the year-end head store count of 55 stores. SSSG came in at 95.2% and was amongst the best out of our core brands, albeit it came from a lower base. Costa continues to post impressive brand contribution margin of nearly 30%, giving us the confidence to scale up this brand very rapidly.

Coming to Q4 performance, we would like to point out that the quarterly performance has been impacted by COVID related restrictions. As you know, COVID wave three, which is the Omicron wave hit us around the end of December, beginning of January, and the entire impact of COVID wave three impacted our performance by almost about four to six weeks out of the entire quarter. As a result, despite very strong year-on-year performance, DIL witnessed a small dip in revenues on a sequential basis that is quarter-on-quarter basis. We maintained the store expansion pace opening 54 new stores. KFC led the store addition for the quarter with 25 new stores, followed by Pizza Hut with 22 new net new stores and Costa added 5 net new stores during the quarter.

Q4 revenues grew 36% year-on-year to reach INR 591 crore. Timely pricing action and efficient sourcing strategies helped us to maintain gross margins at 71.3% for the quarter. Brand contribution margin improved 50 basis points year-on-year to 21.2%, helping us post a 40% higher brand contribution of nearly INR 125 crore.

Pre-INDAS EBITDA at INR 98 crore, improved 44% versus the last year figure of INR 68 crore, with margins improving further to 16.5% versus 15.7% in Q4 FY21. Reported EBITDA for the quarter came in at INR 143 crore, nearly 20% higher on a year-on-year basis.

Amongst the core brands, performance has been very encouraging, considering that nearly half the quarter was impacted by COVID. While ADS dipped and SSSG was a little lower, strong store additions led us to significantly grow the business on a year-on-year basis. Effective cost management has also helped us in managing the profitability at the brand level. KFC revenues came in at INR 353 crore for the quarter, up 39%. Q4 ADS was INR 113,000, representing a SSSG of 3%. Gross margin at 69.3% was stable. Brand contribution margin came in at 21.8%, a slight decline both year-on-year and on a sequential basis. This was primarily due to deleverage on lower sales in the quarter.

As expected, off-premise sales were a little higher at 41% versus 36% in Q3 because of the COVID restrictions in Q4. The launch of Biryani Bucket has been well received by the consumers and is also generating a lot of buzz for the brand. KFC brand in India across both

the franchisees reached an important milestone of 600 stores. To celebrate this milestone, the brand collaborated with India's young budding artists across 150 cities to present a unique expression of art that we've replicated on KFC buckets as KFC Bucket Canvas.

Pizza Hut posted Q4 revenues of INR 146 crore, growing 41% year-on-year. ADS for the quarter was INR 41,000, representing a SSSG of 2.3%. Gross Margin at 75.5% and Brand Contribution at 17.5% remained stable on a sequential basis. Constantly innovating, Pizza Hut has recently launched the much-awaited San Francisco Handcrafted Crust option for our consumers. The new crust along with the assorted new options on the sides have been very well received by our consumers.

Revenue from Costa Coffee grew 61% year on year to reach INR 14 crore. Gross profits stood at INR 11 crore, with improved margins at 81.6%. Brand contribution stood at INR 4 crore and margin at 30%.

Our team's performance is recognized globally. DIL won the award for Best Overall Performance and Most Improved Taste Scores at Yum EFTS Conference in Asia. Our team also won The Most Admired Food Court Operator at the IMAGES Food Service's awards. We continue to add all new women's stores in our portfolio. Pizza Hut has opened two more all-women stores, and we now operate 20 plus all-women stores and 13 stores operated by differently abled employees. We believe such initiatives will allow our diversity hires to step up and play a greater role in our organization as we grow in future.

Looking ahead, we remain cautiously optimistic at the unfolding macro situation. We have taken necessary pricing adjustments already and we are in the process of adjusting the prices even going forward as well to mitigate the impact of input costs inflation and we continue to monitor further developments very closely.

On that note, I would like to request the moderator to open the forum for any questions or suggestions that we may have from you. Thank you so much for your time.

**Moderator:** Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Nihal Jham from Edelweiss. Please go ahead.

**Nihal Jham:** Thank you so much and congratulations to the management for this performance. Three questions from my side. Starting over the first one. Manish, maybe if you could help on this, if I look at our cost items, whether it is specifically for the brands, or even on an overall reported basis; say, the employee or the other expenses, I noticed that despite us opening a significant number of stores versus the last quarter, we still managed to see some reduction. So, if you could just highlight how we managed to achieve that?

**Manish Dawar:** So, Nihal, as you know, the cost buckets are divided into two predominant costs. One is the variable cost and the other one is the fixed cost. Variable Cost obviously has moved in line and that's the reason the gross margins are again stable, if you look at the previous quarter. Therefore, at the store level, the costs are in line. As we grow further, the fixed expenses will get leverage over larger base.

But two things that I would like to remind you here, one is obviously on the international side, our cost base has performed very well. And that's the reason we are getting some arbitrage of that in the overall context. So that, you can call that as a mix effect. And secondly, because of the January impact of Omicron and all, there have been some true-ups on the variable provisions that we've had. And that's the reason, the employee costs are a little lower. So that's an exceptional item in the current quarter. But going forward, if you look at the overall year, we will be in line with the overall yearly performance.

Sure Manish. If I might just have a follow up on that, like if I see the employee expenses on an overall level, we will see it is around INR 70 crore and this has obviously fallen by INR 10 crore. While I know that given that Q3 was a festive quarter and you had more employees, is the net impact of that more than say the new employees being added this quarter because of the store openings?

**Manish Dawar:** So, the new employees that will get added because of the store openings, it is part of the overall brand contribution line and not at the EBITDA line.

**Nihal Jham:** Understood. And even on the corporate overheads, I see that we've managed to reduce those expenses. So, any specific initiatives we've taken that has helped to see that run rate also come down?

**Manish Dawar:** Nihal, that is more to do with the true-up of all the costs towards the year end.

**Nihal Jham:** Understood. And the second question was, you did highlight that there was an impact of Omicron at least for four to six weeks. Would it be possible to get a sense that what is the impact on revenue and margins because of COVID, and had the run rate been similar to the normalized expectations and had COVID not happened?

**Manish Dawar:** Nihal, look, this time, it was not an impact of lockdown and shut downs. Impact was majorly due to operating restrictions which were present. So, let's say for example, as we saw in wave one and wave two, there were multiple cities, where, let's say the stores were shut. There were multiple cities where deliveries were not allowed. Whereas let's say now, there were more of these weekend restrictions, they were more of late-night-delivery restrictions, etc. So, it's difficult to kind of measure that impact. Plus, if you look at, let's say, COVID wave three was more widespread, although the impact on people was less severe. Therefore, that kind of impacted the overall general sentiment, and people tend to restrict ordering and prefer to consume food at home. Let's say, when somebody's sick at home, you avoid having food from outside. At the same time, the other thing that we observed post COVID wave three, was that the malls were faster to recover, compared to the earlier waves, when we saw that high street stores were faster to recover. So that is the other thing where we saw a little divergence compared to the earlier waves, where high street has taken a little longer to recover post COVID wave three.

**Nihal Jham:** Understood. So was there a significant divergence, say, in the ADS maybe between Jan and March, and if you could just give the closing ADS for PH and KFC?

**Manish Dawar:** So, we did say four to five weeks got impacted because of COVID wave three. And that impacted both - the SSSG numbers as well as the ADS numbers. And if you were to look at, let's say, March numbers, although we don't disclose monthly numbers, but they are back to the pre-COVID numbers. You can't compare it obviously to Q3 numbers, because Q3 was a very high season quarter for us, which is what we talked about in the previous quarter as well. But otherwise, we've seen that in March, the numbers are coming back.

**Moderator:** Thank you. The next question is from the line of Percy Panthaki from IIFL. Please go ahead.

**Percy Panthaki:** Hi sir. My first question is on the Pizza Hut margins. Now what my understanding is that for QSR, Q3 is typically the strongest quarter both in terms of ADS, as well as in terms of margins because of the scale leverage. But what we've seen for Pizza Hut is that, while the ADS has come down in March quarter versus the December quarter as expected, the margins have expanded sequentially. So, what is the reason for this expansion and in light of this expansion, what is the sustainable annual margins for Pizza Hut that you expect?

Sure. So, as you know, Pizza Hut, we've been kind of changing the business model. And therefore, those benefits are still flowing in. As you know, Pizza Hut traditionally was a strong dine-in brand. We used to operate large stores where the overheads were higher, the CapEx was higher, and we've kind of over the period of time shifted the model to smaller, delivery focused stores, which have helped us from a margin perspective, which has helped us to make the brand more efficient. So those effects are still flowing in. And that is the reason you see that at Pizza Hut, the margins are marginally better compared to what we've seen earlier, despite the fact that ADS was lower. So, we think now on Pizza Hut, we've managed to kind of completely restructure the brand, all the benefits that are supposed to be had as a result of that restructuring have already flown in. And going forward, we will be more or less in line with how the top line is behaving and performing.

**Percy Panthaki:** So, would you say that the current margins which are around 17.5% for Pizza Hut, that's a fair representation for what the margins would be on an annual basis?

**Manish Dawar:** Yes, that's a sustainable number and therefore, let's say, depending on what happens in a given quarter, it could kind of vary a little bit, but otherwise it's pretty representative of the performance going forward.

**Percy Panthaki:** Okay. Secondly, we did a small exercise as a consumer trying to sort of place an order on Zomato for both Pizza Hut and Domino's for various orders, including whatever discounts offers, etc., available on the platform. And what we found is on an average, Pizza Hut, for comparable pizzas with Domino's, there is a premium of about a low double-digit percentage. Just wanted to understand, is this sort of premium going to continue into the future? And given that there is such a significant premium, why is it that the gross margins are very comparable for both the brands?

**Manish Dawar:** Okay, so traditionally, Pizza Hut has been positioned to be a more premium brand. We believe that we offer a superior product quality and that's the reason the consumers kind of keep on coming back to us again and again. And that actually comes in from the ingredients, how we offer our experience at the store level and all. And we think that kind of justifies a small premium, which is there. Having said that, obviously, our endeavor is to continue to innovate, and continue to bring that margin down, so that we are able to fight the competition much harder. And we've managed to bring that price gap down to a great extent. So therefore, our endeavors continue as we are going forward. And we would love to offer a great quality pizza at competitive prices to our consumers.

**Percy Panthaki:** What is the total CapEx that we should be taking for FY23, overall including international, all the domestic formats, etc?

**Manish Dawar:** So, the CapEx, as you know, is based on the store openings that we are planning. So we've talked about in the past that we will look at about 200 to 250 stores for the next few years and we continue to stay with the same guidance. And therefore, let's say even if you were to kind of look at on the upper side, which is 250 stores, we are looking at a CapEx guidance of close to INR 300 crore.

**Percy Panthaki:** So, INR 300 crore for 250 stores and this INR 300 crore would include any IT, corporate, refurbishment CapEx, etc. also?

**Manish Dawar:** Yes, because I'm talking about the new store opening targets, there are some refurbishments which are supposed to be done, which is a combination of some stores getting into minor refurbishment, some stores getting into major, but that's a small amount in the overall context.

**Percy Panthaki:** So around INR 300 crore, plus or minus 10% would be a fair assumption?

Yes, that's the right way to look at it.

**Moderator:**

Thank you. The next question is from the line of Devanshu Bansal from Emkay Global Financial Services. Please go ahead.

**Devanshu Bansal:**

Congrats on a good set of numbers, and thanks for giving me the opportunity. Sir, wanted to understand from channel sales perspective, KFC performed relatively better, versus Pizza Hut, if we think in terms of sustainability of delivery revenues. So how should we read this, as in dine-in focus formats, which were pre-COVID, will benefit more upon full unlocking? Is this the correct inference?

**Manish Dawar:**

Hi, Devanshu. So, if you see the previous quarter, KFC off-premise consumption was close to 36%. In the current quarter it moved to 41%, and that predominantly happened because of the COVID wave three restrictions that I talked about earlier. So, as we kind of open up and we get into normalized situations, this will come down. We expect KFC to be stable in terms of deliveries, anywhere between 35% to let's say a 37% - 38% kind of number. And obviously, that will benefit us more from a dine-in perspective.

Coming to Pizza Hut. As you know, pizza as a category is more of a delivery portfolio. And that is what we've pivoted our brand focus from dine-in to delivery and that's the reason, you'll see that the numbers are pretty much kind of stable from that perspective. And those numbers would more or less remain at the same level.

**Devanshu Bansal:**

Sure. So, while KFC delivery sales are more or less stable, but Pizza Hut delivery sales have seen dips sort of from Q3 to Q4. So to understand this.

**Manish Dawar:**

No, Pizza Hut has not seen a dip. If you see Quarter Three, Pizza Hut delivery was 58%, quarter four was 59%. So, it is not a dip. But let's say given the fact that quarter four was a COVID impacted quarter, and therefore the impact could have been higher. I think Pizza Hut as a business is now stabilizing towards that number. And that is what we are seeing.

**Devanshu Bansal:**

Sure. That's helpful. Second is, wanted to understand in terms of product innovation, is there any identifiable portfolio gap, which you would like to fill versus the leader in the Pizza Hut space?

**Manish Dawar:**

On Pizza Hut side, we introduced a new dough called San Francisco Dough, which is a hand tossed pizza compared to let's say, the pan pizza that we have in our portfolio. This filled in a big gap that we had in our portfolio. Because apart from pan we have handcrafted dough pizza also and it is sour dough, which is what kind of makes the pizza even lighter. So, that is one. As you would have seen in the previous quarter, we introduced completely novel products in the shape of Momo Mia pizza, which was very well received by the consumers. We will be looking at a Momo Mia version two towards the back end of the year.

Similarly, on the sides also, we've introduced two more innovative items in the shape and form of tear and share, which is cheese filled kind of garlic bread. And then we've also launched a Mexican garlic bread, which is a different flavor, again, something we did not have before. So, as things have opened up, we are introducing new innovations in Pizza Hut brand, which we did not do over the last one and a half, two years because of COVID and all of that.

**Devanshu Bansal:**

Sure. On the tax guidance, if you can provide any color on what should be the rate we should bake in into our estimates going ahead?

**Manish Dawar:**

I think Devanshu the way we look at it, next year, we will be able to recoup our losses, if let's say our business conditions are normalized and there is no COVID impact and the situation in the country is normal. And therefore, you can assume the normal marginal rate from that

perspective. In this quarter, we had to recognize the deferred tax assets which were sitting and we had not recognized earlier, because of the COVID related uncertainties. But the auditors kind of evaluated the entire thing again. Even now, as you know, COVID wave four fears are still there, the input inflation fears are still there, the geopolitical situation is there. So therefore, we've not recognized the entire deferred tax asset. We've discussed that with the auditors. And we've kind of taken a call that not to recognize also would not be prudent. And that's the reason we've kind of agreed on somewhere a middle path. So, we've recognized about, two years' worth of deferred tax assets. But I would say as we go along, you can recognize the marginal tax rate as the normal tax rate.

**Moderator:** Thank you. The next question is from the line of Jay Kumar Doshi from Kotak. Please go ahead.

**Jaykumar Doshi:** At roughly about INR 41,000 ADS, Pizza Hut is already clocking 17% margin. So, what is the ADS that you think you need to get for you to report similar margins at KFC or the market leader, our understanding is that store-level margins will be around 23%. What is the ADS increase that can get you at that level?

**Manis Dawar:** Hi, Jay. So, on Pizza Hut, we are looking at about 7% to 8% kind of SSSG numbers year-on-year. The quarters have been kind of little up and down because of the COVID related uncertainties and COVID impacts. So that has not been stable but otherwise we are targeting a 7% to 8% SSSG numbers. And with that, we think from a restructuring point of view, we've kind of picked up all the low hanging fruits and Pizza Hut margins are there. But we also need to bear in mind that if you look at the KFC ADS numbers, it is almost two and a half to three times where Pizza Hut sits. So, it'll be difficult to kind of target those ADS numbers, because I mean KFC is a different product category with no competition. Whereas in pizza category, we are not the market leaders, we are the followers. So, our endeavor is to kind of bridge the gap versus the competitor. But it's going to take a long time. It's not going to happen overnight. So the margins, I think we've done a good job on margins, and you can expect sustainable margins going forward.

**Jaykumar Doshi:** Sure, maybe I'll take that offline. Second question is, you've taken about 12% price increase in KFC in the last six months. Is there any impact on demand, because of price increase, or any down trading or any such behavior that you have seen?

**Manish Dawar:** So Jay, we took a price increase in April, to the extent of about 8% to 9%, not 12%.

**Jaykumar Doshi:** There was one 2% to 3% in October, November also, right. So if combine those.

**Manish Dawar:** Yes. That has kind of got absorbed very well in the market. So that is now history. So therefore, we've not seen any impact because of that. Whereas, the price increase that we've taken in the month of April, was about 8% to 9%, which is the second price increase that we took. And obviously, I mean, April is not a key kind of metrics to look at, because as you know, in April there were Navratris and during Navratris, the chicken consumption kind of tends to fall, especially in the northern part of the country. At the same time, within April, we also saw Roza coming in. And there also the consumption gets a little bit impacted. So therefore, we are looking at May month to see as to how consumers have accepted that from a price increase perspective, and maybe let's say when we talk next, we'll be able to give you a better color on that.

**Jaykumar Doshi:** Correct. And this price increase takes care of all the inflation that you're facing till date, right, for KFC?

**Manish Dawar:** Not really, Jay. There will be margin dilution to some extent because we don't think we've managed to pass on the entire input inflation to the consumers, because at 8% to 9% itself, we

thought it was a very challenging price increase from consumer perspective. So, let's see how the situation pans out. But we've not managed to take the entire price increase.

**Jaykumar Doshi:** Can you give us an idea of what is the overall RM basket inflation that you are facing on a YOY basis, both for KFC and Pizza Hut?

**Manish Dawar:** Pizza Hut is relatively small. So let's say if you look at Pizza Hut also, we took a small price increase in the month of April. And we are taking another price increase over the next few weeks, so therefore Pizza Hut, we are well covered as far as the input inflation is concerned. On KFC, we are not fully covered. We are in the wait and watch mode, if let's say the prices were to come down both from a chicken and edible oils, which is where we've seen a major inflation coming in. So, let's see how that pans out. And we'll take the next steps based on that.

**Moderator:** Thank you. The next question is from the line of Ashish Kanodia from Ambit Capital. Please go ahead.

**Ashish Kanodia:** So, the first question is on the margin front. I remember in the DRHP, there was a disclosure that there are some benefits which Yum will provide, given you're able to meet some of the store expansions guidance. So is it possible to quantify what are the margin benefits you're getting from Yum? And secondly, what is the tenure or the duration for the same?

**Manish Dawar:** So, Ashish, yes, there are some small incentives that we get as a result of meeting the targets, but we've maintained even around the DRHP time and post that during the calls, that these margins are very insignificant, and therefore they do not impact the P&L in a great way. So whatever margins that you're seeing as far as both KFC and Pizza Hut, are concerned, are sustainable, and the impact is really small.

**Ashish Kanodia:** Sure. And you talked about some of the true ups and expenses. So, is it possible to quantify and where these expenses are sitting because sequentially there is a decrease in employee cost on a per store basis as well as other expenses on a per store basis. So, are there true ups sitting in both these line items and possible to quantify?

**Manish Dawar:** Look there are two things that impact on a per store basis, Ashish. One is obviously there is a true up, which is a small number. But at the same time, if you look at the number of stores, which have kind of opened, as you say, we've opened almost 150 stores during the entire year. And that's a meaningful number to be able to get that leverage on the fixed employee expenses. So that is the other big contributor as to why per-store numbers look much better now compared to what they were looking earlier. And as we kind of go ahead and open more stores, obviously, this will look even better, but the impact of true ups is small.

**Ashish Kanodia:** Sure Manish, that is helpful. And just last question, in terms of same store sales growth. Now, current quarter had some COVID impact, and the base quarter of Q4 FY21 also had a base impact because Q4 FY20 was impacted from COVID. So, if we want to analyze it versus pre-COVID level so we would need the Q4 FY20 SSSG. So is it possible to share the Q4 FY20 SSSG for KFC and Pizza Hut?

**Manish Dawar:** Ashish, let me just look at the numbers and connect with you separately.

**Moderator:** Thank you. The next question is from the line of Rahul Agarwal from InCred Capital. Please go ahead.

**Rahul Agarwal:** I had three questions. Firstly, on Pizza Hut, on the ADS levels, it's still far from the leader, but the margins are still much better. There's a long way to go for Pizza Hut to reach the leader level ADS, but in your mind, would you have a specific three to five year's target, which you are working with on ADS?

Rahul, as I said earlier, I mean, obviously, our aspiration is to kind of bridge the gap from ADS perspective versus the market leader. It's going to take time, so the target that we have set for ourselves, is about a 7% to 8% SSSG growth on Pizza Hut. We continue to innovate, continue to introduce new product categories, continue to give the consumers a great quality pizza, this will help us bridge the gap. Having said that, because we've kind of restructured the entire portfolio, from a focus perspective, because earlier it used to be a dine-in brand and now it is a delivery focus brand that has really kind of helped us from a margins perspective. And on margins, because the restructuring has now completely managed to get all the margin advantages, and therefore, now it has to grow and it has to move as the brand performs.

**Rahul Agarwal:** The ADS, even at a 7%-8% growth will still be far off, right. So, it can be much faster is what my sense was.

**Manish Dawar:** Yes, let's see, I mean, this is what we are targeting. So, the market leader has kind of been able to establish themselves over a long period of time. Because right from the beginning, they kind of focused on delivery, which is where we lag behind. We've kind of re-pivoted the model now. In the last two years because of COVID, we could not innovate much. So, we've kind of gone in for aggressive innovation also. So, let's see how the consumer acceptance is. But you're right in saying that it will take a long time out at these growth rates to kind of bridge that gap. We are conscious of that. We recognize that. And I agree with you.

**Rahul Agarwal:** Secondly on Costa, the ADS number is still about INR 30,000 on the quarter. For the year also, it's pretty similar. I think the traction here what we should assume is firstly, it has to go back to where it was pre-COVID which is INR 37,000, INR38,000 and then you know look at further growth. Similar question, on Costa, what is your thought process in terms of where do you want this ADS to settle down and how would that happen really?

**Manish Dawar:** So, Costa as you know, we signed the new agreement, which was pending for a few years around September 2021. And post that we've hired a new CEO for Costa. We are building up the teams, we are working on the store pipeline. So, all of that takes almost about six to seven months' time. So, we are seeing a strong traction. We opened about let's say five stores in the previous quarter. We are looking at Costa as a brand to be built again. We are looking at five flagship locations, as you know I mean flagship locations are difficult to come by. Because the Indian prime real estate commercial market is short in supply and whenever such vacancies are there, there are multiple brands who are in queue for such stores. So, it takes a little bit of time to get to the prime real estate, and the prime flagship location. But in the middle of all of that, wherever we are getting the opportunity, we are kind of plugging the Costa stores in. So therefore, as a combination of various things, we are confident that we will be able to get to, let's say, an INR 40,000 ADS for Costa in the next couple of years.

**Rahul Agarwal:** And there is going to be a mix of food and beverage both right?

**Manish Dawar:** Yes. So currently, beverage is very strong in the mix. Our endeavor is to kind of get to a good food contribution, because that will help us from a brand loyalty perspective, as well as with the ADS because as you know, I mean in food, the per capita ticket item is higher than the beverage. So therefore, that is how we are working on the plan.

**Rahul Agarwal:** Lastly, on cash flows, as I could understand looking at the statement, free cash flow is near breakeven. I'm adjusting for lease rentals in form of principal and interest. And over and above that you have INR 570 crore of cash. There are two sub questions here. One is, can this cash be used more aggressively for growth because I'm assuming that all your CapEx, which you mentioned INR 300 crore, INR 350 crore will be funded through, assuming no COVID next year, will be funded through your operations and then you still have this cash to be utilized. And second is, any plans outside of your core brands or any other thoughts which are thinking outside of these three brands which we generally talk about?

So, Rahul, you're right in saying that our focus is to kind of fund the entire expansion through the internal cash accruals and that is what we are doing. Right now, again, as you know, we are highly underpenetrated as far as the Indian market is concerned, we have to do a lot better in terms of the three core brands that we have. So, we are focused on India's geography, we are focused on the three brands that we have. So, we are not looking out very aggressively in terms of the other opportunities, at the right time, we will, and if any opportunity were to come by which kind of makes sense, we of course will evaluate

**Rahul Agarwal:** So, this INR 570 crore of cash right now, what do we do with that? Essentially, can we use it more aggressively for growth within the core brands if not outside?

**Manish Dawar:** Rahul, INR 570 million is the net cash that we have which is the overall cash and then we have a small net debt also. So on the net debt, net cash basis, we will be at about INR 57 crore, INR 60 crore. So, it is not INR 570 crore.

**Moderator:** Thank you. The next question is from the line of Rushabh Doshi from Proinvest Nirmithi Investment Advisors. Please go ahead.

**Rushabh Doshi:** How are some costs divided between you and your sister company, which is Sapphire? So, something like menu card innovation, building certain digital assets, for their website or the app, or advertisement. So, how does that exactly work?

**Manish Dawar:** It's not a sister concern, we are two franchise partners for Yum in this country. So, that is how it works. So, anything to do with the consumer facing, the philosophy that Yum follows is basically the consumer should not be able to make out whether a store is operated by a franchisee X or the store is operated by a franchisee Y. So therefore, anything to do with consumer, whether it is how the brand gets represented, whether it is the menu, or the offerings, or the deals or the pricing, or the look and feel of the store, the brand experience, brand colors, everything is followed on the basis of guidelines given by Yum, just to make sure that the consumer experience is absolutely uniform across all the stores in the country. So from that perspective, the items related to let's say advertising and marketing are in a way they operate on a co-op model, which is a three-way model between us, Yum, and Sapphire. And that's how kind of we contribute to a common kitty and the funds get spent for the entire country as a whole.

**Rushabh Doshi:** Could you just share like what are your plans on developing your own app? Because what we see is that Domino's has built a great app and they have a lot of downloads which might be helping them in their delivery business. So could you just shed some light on what is our plan?

**Manish Dawar:** So we have our own app for both the brands, which is KFC and Pizza Hut. And we are shortly going to be launching an app for Costa Coffee also. So, as I said anything to do with the consumer, it is common between us and Sapphire, and therefore even this app also gets kind of regulated in a way from Yum's side. And they are the ones who host this app. And it is, again, between us and Sapphire, it is a common experience, as far as it goes, it is one uniform app for the consumers. Whenever you place an order, the nearest store, irrespective of which franchisee is operating, that gets picked up for delivery. So, we have our own app, it contributes to the overall delivery sales. But as I've stated in the past, that our strategy is to more work with the food aggregators, rather than through our own delivery for us. The biggest priority remains to open and roll out more stores, because that is very important to be able to bring the delivery times, to be able to get the stores closer to the consumers. So therefore, our single focus remains to expand the number of stores in the right locations, right profitability locations, and that is what we are focused on.

**Rushabh Doshi:** We have rights for delivery only stores for pizza across India, except Tamil Nadu. So, are we planning anything like are the per store economics viable without dine-in?

Yes, of course. So, let's say when we say without dine-in that does not mean that the delivery focus store is only supposed to do a delivery and there is no dine-in. So all of our stores are omnichannel. Each and every store, barring a handful of stores, which will be a lower single digit number of stores, all of the stores would have 35 to 40 seats. So, a consumer can walk in, they can take away at on their own, they can sit and eat there if they want. And the pizzas can be delivered also from there. So, a delivery focused store basically means a smaller size store. That does not mean that there is no dining available there.

**Rushabh Doshi:** My question was that we have some separate rights for Pizza Hut only, where we can just open delivery stores.

**Manish Dawar:** Yes. So, it's a delivery focus store.

**Ravi Jaipuria:** The delivery store means that you cannot give table service. And basically, it's a smaller format and it is not more than 40 seats. So, if somebody wants to take a pizza and sit on the table and eat there is no restriction to it. But we will not give him plates and cutlery and crockery, and there will be nobody coming to serve at the table.

**Moderator:** Thank you. The next question is from the line of Vinod Malviya from Union Mutual Funds. Please go ahead.

**Vinod Malviya:** Can you just provide the rental costs for the entire company for FY22?

**Manish Dawar:** Okay. So, it'll be roughly around 11%.

**Vinod Malviya:** This is basically after netting of a discount or any concession that you would have got?

**Manish Dawar:** Within the quarter, there could be some credits, depending on how the quarterly situation is. We've not seen any major credits in the current year, because there has not been a case of a complete lockdown or a shutdown. So therefore, it's pretty much a normalized rental cost.

**Vinod Malviya:** Going forward, do you expect a similar kind of run rate to continue or there could be some escalation?

**Manish Dawar:** Our newer portfolio that we are signing is coming at a better rent-to-revenue ratio. So therefore, marginally you could see a small improvement as we go along.

**Moderator:** Thank you. The next question is from the line of Madhu Babu from Canara HSBC. Please go ahead.

**Madhu Babu:** Just on the RM, I mean, the chicken and edible oil as well as cheese and all, what is the YoY increase in the major cost items. If you can share that percentage?

**Manish Dawar:** We have not specified Madhu, the percentages separately, but as I said earlier, as far as KFC is concerned, we did see a double-digit input inflation. We've managed to pass on some increase to the consumers back in September, October where we took a small price increase. We took another price increase beginning of April. But still, it's not that we've taken all of the price increase, because we think the price increase that we've already passed on to the consumers, we cannot do any more. So it's a wait and watch situation. Let's say the input inflation also will ease a bit as things stabilize. And at the same time, if things don't, then we will be looking at another price increase somewhere middle of the year.

**Madhu Babu:** In the next one and half year perspective, what are the kind of products expansion we're looking at within our brands?

It's a continuous process, both for KFC and Pizza Hut. We continue to innovate, we continue to kind of introduce the new products in the market. So on KFC side, we introduced some good range of burgers last year. We've introduced a Biryani Bucket this year. On Pizza Hut, we introduced Momo pizza last year, we've introduced the SFO craft this year. We've introduced the new sides recently. So, it's a continuous process that is part of the brand DNA.

**Madhu Babu:** Early days, but how do you see the competition, Popeyes from Jubilant, which was launched in Bangalore? What are your takes on the competition that is likely to come up?

**Manish Dawar:** I would say, too early to comment on that. We've not seen any big impact on our neighborhood store so far. But Popeyes is a formidable brand globally. Let's see how they kind of do in India. Whatever we've seen in the past, if you were to look at, I mean, all of these new brands and new product categories help expand the market. We've seen that with pizza category, we are seeing the same with the chicken category also. So therefore, it is good that we have multiple players who are kind of working on to expand the market. And that kind of helps all the players who are in that market.

**Moderator:** Thank you. The next question is from the line of Sanjaya Satapathy from Ampersand Capital. Please go ahead.

**Sanjaya Satapathy:** You have given some indication about SSSG growth of Pizza Hut. Can you share the same for KFC?

**Manish Dawar:** KFC, we're looking at about 4% to 5%.

**Sanjaya Satapathy:** Understood. And so I was just looking at your Pizza Hut growth plan. So, pre-COVID, your main competitor used to grow on an average by 7% or 8% or even more during that period, so when you're looking at bridging the gap with 7%, 8% growth, are you looking at relatively modest overall industry growth or some kind of saturation, which is why you're looking at this kind of growth?

**Manish Dawar:** Look, pizza, as you know, is a large category and it is still growing. We believe let's say chicken, for example, if you look at the country demographics from a consumption perspective, India is a 70% non-vegetarian country. And if you were to look at south and east, the two regions are almost 94%-95% plus as far as the non-vegetarian consumption is concerned. Whereas if you were to look at, let's say, the QSR portfolio offering to the consumers, it's the other way around. So, I'm talking about the overall QSR as a market, 70% to 75% offering to the consumer is a vegetarian offering and about 20% to 25% is non vegetarian offering. So that's the reason we are more bullish on KFC because the basic consumption demographics are very different to the consumption and secondly, pizza as a category is already a highly penetrated, large category and therefore, it is growing slower than what the opportunity is there on the chicken side.

**Sanjaya Satapathy:** I understand why you are giving a higher growth target for a Pizza Hut, that is because you are far smaller at this point of time. So, my limited point is that this Pizza Hut, pre-COVID, SSSG growth used to be a lot higher. So is there some kind of change you are looking at?

**Manish Dawar:** So, if you see, we were limited as far as stores were concerned, and we are now kind of correcting that situation by opening more stores. Because obviously as you know, I mean, they would be to some extent, the impact of the new stores coming on to the overall portfolio. So, let's say the way I look at it, yes, SSSG is very important, but we are aggressively opening the new stores as well.

**Sanjaya Satapathy:** If you can give us some indication as to what are the annual store growth plans for both the categories?

So as we've talked in the past, we are looking at about 200 to 250 stores for next year also. So, we've indicated that we will open about 100 stores for KFC, 100 stores for Pizza Hut and the remainder 50 stores between Costa Coffee and Vaango, more heavily tilted towards Costa than Vaango. So, we are staying with the same guidance and we are hoping we'll be able to deliver on that as well in the next year.

**Sanjaya Satapathy:** You have been talking about Pizza Hut being a much premium product and now that you are trying to expand it more rapidly. So, will you continue to have that kind of strategy or you will come up with a different pricing plan? And lastly, overall for both KFC as well as Pizza Hut, are you really in a position to bring in a lot more product innovation or it is like having a shorter menu and a lot more efficiency in operations? What really will be the main focus area?

**Manish Dawar:** As I've said earlier that innovation is the key cornerstone of what we do in the brands. That's the DNA of the brand that I've said. And we've introduced a lot of innovations once let's say the COVID has started to recede, which I said earlier. We've introduced Momo pizza last year. We introduced SFO pizza recently. We've introduced new sides. So that continues to kind of go well. Similarly, we've had new introductions in KFC also. Last year, we introduced new burgers. This year, we've introduced KFC Biryani. So that remains one of the cornerstones of our growth strategy, and that will continue going forward as well.

**Moderator:** Thank you. My next question is a follow up from the line of Percy Panthaki from IIFL. Please go ahead.

**Percy Panthaki:** This question is in the light of your pricing on KFC, where you mentioned that you haven't taken up prices to the extent that you've seen cost inflation. In light of that, how do you see the brand contribution for KFC for FY23? And if I compare it with the average of the last three quarters of FY22, I'm leaving out Q1 anyways, but what we've done or let's say the last two quarters where we've done like 15% 16% kind of brand contribution for KFC, is there a risk that we will see this margin compressing in FY23?

**Manish Dawar:** So, Percy, as I said in my opening comments, that we are cautiously optimistic, so we don't see the margins getting compressed, but you will not see a growth in the margins in the KFC category, both from let's say gross margin standpoint or the brand contribution. So, we are going to be bringing in efficiency, because the brand is expanding. At the same time, we believe that the input inflation will kind of come down towards the back end of the year. We are banking on that. If that does not happen, we are prepared for another price increase also. So therefore, we need to kind of balance the entire portfolio in a very delicate manner. And we are kind of monitoring that on a day-to-day basis. So, we are hopeful that the margins should not come under pressure. But we cannot bank on margins growing in this year.

**Percy Panthaki:** The total price increases that you've taken on KFC in the last 12 months is low double digit kind of price increase?

**Manish Dawar:** Yes, you can see that. We took about 2% to 2.5% back in August, back in September-October of last year. And we've taken another 8% to 8.5% now. So, you are right.

**Percy Panthaki:** What my understanding is that this kind of price increase has been seen even in the pizza cuisine. It is not by you, by the market leader. It's a similar kind of price increase, which has happened. Fried chicken, the only sort of national brand is KFC. And given that currently, pizza is a more competitive industry than fried chicken, don't you think KFC should have a higher pricing power than the pizza segment? And I mean, why are you worried on KFC pricing going beyond the current level compared to the pizza which is already at this level?

**Ravi Jaipuria:** I think we've already taken, as Manish said, 8.5% to 9% price increase, and anything immediately further would affect the transaction. So, at the moment, I don't think we need to

take immediate pricing action. And I think the volumes are coming back. So, I think our margins will not get effected. And if we feel that the inflation continues, and we need to take another price increase, then we will do it at the end of the first quarter.

**Manish Dawar:** And Percy, again, what you need to also note and bear in mind that the kind of input inflation which is happening now, there is no precedence for that because in the past, if you go back to the history, we've seen inflation hitting various categories at different points in time. Whereas let's say if you look at this time round, I mean, there is an all-round inflation which is impacting the consumer wallets, and therefore, to that extent, it is a little different and everywhere the consumers are getting impacted, and therefore it will impact the consumption to some extent.

**Moderator:** Thank you. Ladies and gentlemen, that was the last question for today. I now hand the conference over to the management for closing comments.

**Raj Gandhi:** Thank you, Chairman, all the investors, analysts who have been on the call. I do hope that we have managed to respond to your questions satisfactorily. Should you need any further clarifications or would you like to know more about the company, please feel free to contact our Investor Relations team. Thank you once again for your time today to join us on this call and participate in our growth journey. Thank you very much.

**Moderator:** Thank you. Ladies and gentlemen, that concludes this conference call for today. On behalf of Devyani International Limited, we thank you for joining us, and you may now disconnect your lines.

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