

QSR | Q1FY24 Result Update

Pizza business continues to witness pressure; Maintain SELL

- Sapphire's Q1FY24 results were ahead of our estimate. The company reported 19.8% revenue growth helped by 21.2/11.7% growth in KFC/Pizza Hut while Sri Lanka sales growth improved to 27% in INR terms.
- Sri Lanka business reported 9% growth in LKR terms but 27% in INR terms – due to appreciation in local currency. Also, the business reported 9% EBITDA decrease in LKR terms, it increased 8% in INR. Going ahead, Sri Lanka business would benefit from favorable base.
- The company opened 35 new stores during Q1 (17 KFC, 16 Pizza Hut and 1 KFC and pizza Hut in Maldives), taking the total store count to 778. The company would continue to add 130-160 stores every year going ahead with a cluster based approach and penetration strategy. However, in case of continuous slowdown, the company would slow down store addition pace.
- We have reduced our FY24E EPS estimates to Rs 24.4 to factor in higher tax incidence. However, we have maintained our FY25E EPS estimates at Rs 31.1 as it factors in the expected improvement. We arrive at a TP of Rs 1,246 (40x FY25E EPS). Maintain SELL.

Results ahead of estimate; but quality remains weak

Sapphire's revenue grew 19.8% YoY to Rs 6.5bn despite demand headwinds – came 5.1% ahead of our estimate. GM expanded by 70bps to 68.5%. A 70bps decline in RM was fully offset by 50/180bps increase in RM cost/other expenses resp. resulted in EBITDA margin erosion of 160bps to 18.6%. EBITDA increased by 10.0% YoY to Rs 1.2bn – came 7.1% ahead of our estimate. APAT de-grew by 34.8% to Rs 249mn – was 10.3% ahead of our estimate.

During the quarter KFC reported flat SSSG while pizza hut reported -9% - in line with our channel checks. Increased competition and general slowdown in the industry hampered Pizza Hut performance during the quarter. GM/EBITDAM in KFC improved by 80/50bps led by deflation in key commodities. GM/EBITDAM in Pizza Hut contracted by 20/580bps. Sharp drop in EBITDAM in the pizza business can be attributed to lower operating leverage during the quarter. EBITDAM are expected to remain under pressure with muted SSSG.

Q1FY24 Result (Rs Mn)

Particulars	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)
Revenue	6,544	5,463	19.8	5,604	16.8
Total Expense	5,329	4,359	22.3	4,623	15.3
EBITDA	1,214	1,104	10.0	981	23.8
Depreciation	727	609	19.3	724	0.5
EBIT	487	495	(1.5)	258	89.0
Other Income	75	59	27.2	114	(34.2)
Interest	226	197	14.6	249	(9.2)
EBT	336	356	(5.6)	123	173.8
Tax	88	(25)	(448.0)	(1,232)	(107.1)
RPAT	249	381	(34.8)	1,355	(81.6)
APAT	249	381	(34.8)	1,355	(81.6)
			(bps)		(bps)
Gross Margin (%)	68.5	67.9	65	67.9	57
EBITDA Margin (%)	18.6	20.2	(165)	17.5	105
NPM (%)	3.8	7.0	(318)	24.2	(2037)
Tax Rate (%)	26.0	(7.1)	3309	(1003.2)	102921
EBIT Margin (%)	7.4	9.1	(161)	4.6	284

CMP	Rs 1,342
Target / Downside	Rs 1,246 / 7%
NIFTY	19,527

Scrip Details

Equity / FV	Rs 635mn / Rs 10		
Market Cap	Rs 85bn		
	USD 1.0bn		
52-week High/Low	Rs 1,574/ 1,103		
Avg. Volume (no)	107,305		
Bloom Code	SAPPHIRE IN		
Price Performance	1M	3M	12M
Absolute (%)	(2)	8	12
Rel to NIFTY (%)	(4)	(4)	(1)

Shareholding Pattern

	Dec'22	Mar'23	Jun'23
Promoters	44.9	44.9	44.9
MF/Banks/FIs	25.0	27.5	29.6
FIs	16.5	15.5	18.7
Public / Others	13.6	12.2	6.9

Valuation (x)

	FY23P	FY24E	FY25E
P/E	36.5	55.1	43.1
EV/EBITDA	19.3	14.4	11.4
ROE (%)	20.6	11.6	13.1
RoACE (%)	28.4	19.0	19.9

Estimates (Rs bn)

	FY23P	FY24E	FY25E
Revenue	22.7	27.8	32.9
EBITDA	4.3	5.6	6.8
PAT	2.3	1.5	2.0
EPS (Rs.)	36.7	24.4	31.1

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Exhibit 1: Actual V/s Estimates

Particulars (Rs mn)	Actual	Estimates	Variance (%)	Comments
Revenue	6,544	6,227	5.1	Sri Lanka business performance was better than estimate
EBITDA	1,214	1,134	7.1	better operating leverage than estimate
EBITDA margin %	18.6	18.2	40bps	
APAT	249	225	10.3	Cascading effect of higher EBITDA

Source: Company, DART

Exhibit 2: Change in estimates

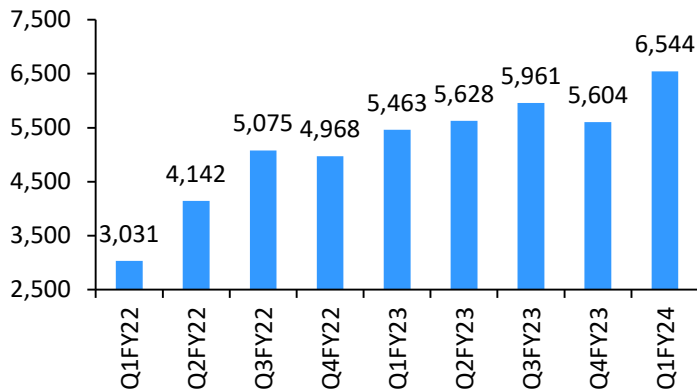
Particulars (Rs mn)	FY24E			FY25E		
	New	Old	Chg (%)	New	Old	Chg (%)
Revenue	27,808	27,808	0.0	32,947	32,947	0.0
EBIDTA	5,597	5,474	2.2	6,756	6,727	0.4
EBIDTA margin (%)	20.1	19.7	40bps	20.5	20.4	10bps
PAT	1,548	1,751	(11.6)	1,977	1,979	(0.1)
EPS (Rs)	24.4	27.6	(11.6)	31.1	31.2	(0.1)

Source: Company DART

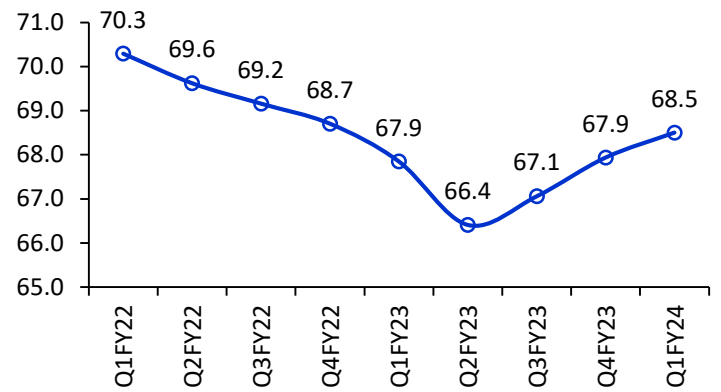
We have maintained our FY24/25E revenue estimates as we believe that the business would report short term hiccups but would post improvement in H2FY24E. We have increased our EBITDA margin estimates to factor in Q1 performance, deflation in RM and better growth in H2FY24E. However, we have reduced our EPS estimates for FY24E to factor in full tax rate. We have maintained our FY25E APAT estimates.

Earning call KTAs

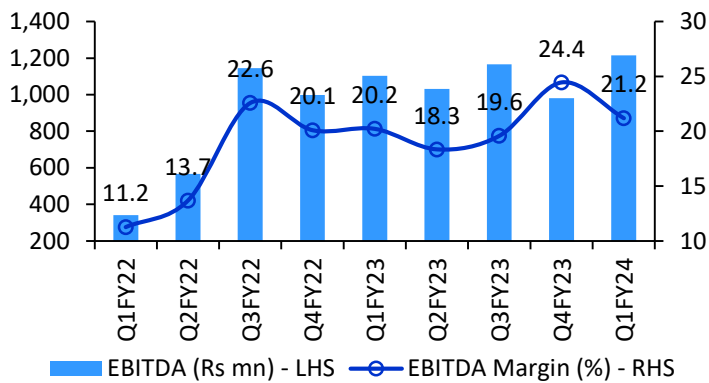
- Despite challenging demand scenario, Sapphire reported revenue growth (consol) of 19.8% YoY in Q1FY24. We believe that with the launch of new innovative products and increased marketing investment, Sapphire would witness improvement in revenue growth going ahead.
- KFC witnessed revenue growth of 21.2% YoY during the quarter. However, SSSG remained stagnant due to unfavorable macro conditions. The newly launched snackers at Rs 99/- which include Chicken Rolls, Longer Chicken Burger, Popcorn, Fries and Beverage options remain focused to boost revenues.
- Pizza Hut reported revenue growth of 12% YoY in Q1FY24, while SSSG declined by 9% due to increase contribution and general slowdown. Moreover, the launch of four new core pizzas has done well but fell short of the anticipated performance.
- Sri Lanka's revenue has increased by 9% in LKR terms, moreover, it grew by 27% in INR terms due to currency appreciation. However, consumer demand was impacted as a result of high inflation and taxes. Further, SSSG remained stagnant during the quarter. Currently, operating conditions have stabilized and we believe demand would start picking up by the end of FY24E.
- During the quarter, Sapphire added 35 stores (17 KFC, 16 Pizza Hut, 1 KFC, and 1 Pizza Hut in the Maldives), taking the total count to 778 stores. For Sri Lanka, Sapphire is taking a cautious approach on new store expansion for the next 12 months on account of the challenging macro environment. Further, Sapphire is targeting to double the store count of KFC and Pizza Hut over the next 3-4 years.

Exhibit 3: Revenue Trend (Rs mn)


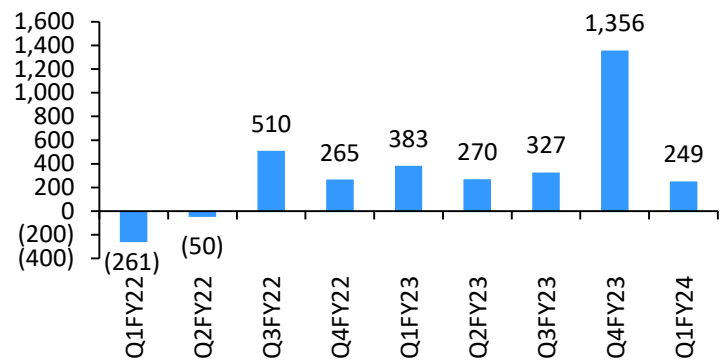
Source: Company, DART

Exhibit 4: Gross Margin Trajectory (%)


Source: Company, DART

Exhibit 5: EBITDA and EBITDA Margin Trends


Source: Company, DART

Exhibit 6: Reported PAT Trends


Source: Company, DART

Financial Performance

Profit and Loss Account

(Rs Mn)	FY22A	FY23P	FY24E	FY25E
Revenue	17,216	22,656	27,808	32,947
Total Expense	14,166	18,372	22,211	26,191
COGS	5,278	7,407	8,594	10,182
Employees Cost	2,740	2,929	3,648	4,327
Other expenses	6,148	8,036	9,969	11,681
EBIDTA	3,050	4,284	5,597	6,756
Depreciation	2,135	2,642	2,987	3,562
EBIT	915	1,642	2,610	3,194
Interest	781	869	834	876
Other Income	380	311	321	333
Exc. / E.O. items	0	0	0	0
EBT	514	1,084	2,097	2,650
Tax	54	(1,248)	544	668
RPAT	465	2,333	1,548	1,977
Minority Interest	(5)	(2)	5	5
Profit/Loss share of associates	0	0	0	0
APAT	465	2,334	1,548	1,977

Balance Sheet

(Rs Mn)	FY22A	FY23P	FY24E	FY25E
Sources of Funds				
Equity Capital	635	635	635	635
Minority Interest	(17)	(20)	(15)	(11)
Reserves & Surplus	9,436	11,924	13,477	15,459
Net Worth	10,071	12,559	14,113	16,095
Other Long term liabilities	6,606	7,820	7,868	7,922
Total Debt	612	443	443	443
Net Deferred Tax Liability	87	(1,184)	(1,184)	(1,184)
Total Capital Employed	10,754	11,798	13,356	15,342

Applications of Funds

Net Block	13,905	17,903	17,421	16,363
CWIP	320	550	550	550
Investments	0	0	0	0
Current Assets, Loans & Advances	7,415	6,267	9,192	13,346
Inventories	652	993	1,029	1,223
Receivables	141	179	210	249
Cash and Bank Balances	2,546	2,204	4,565	8,048
Loans and Advances	936	687	795	900
Other Current Assets	1,615	1,544	1,914	2,226
Less: Current Liabilities & Provisions	4,279	5,103	5,939	6,995
Payables	1,991	2,170	2,651	3,144
Other Current Liabilities	2,288	2,933	3,288	3,851
<i>sub total</i>				
Net Current Assets	3,136	1,164	3,253	6,350
Total Assets	10,754	11,798	13,356	15,342

E – Estimates

Important Ratios

Particulars	FY22A	FY23P	FY24E	FY25E
(A) Margins (%)				
Gross Profit Margin	69.3	67.3	69.1	69.1
EBIDTA Margin	17.7	18.9	20.1	20.5
EBIT Margin	5.3	7.2	9.4	9.7
Tax rate	10.5	(115.1)	25.9	25.2
Net Profit Margin	2.7	10.3	5.6	6.0
(B) As Percentage of Net Sales (%)				
COGS	30.7	32.7	30.9	30.9
Employee	15.9	12.9	13.1	13.1
Other	35.7	35.5	35.8	35.5
(C) Measure of Financial Status				
Gross Debt / Equity	0.1	0.0	0.0	0.0
Interest Coverage	0.0	0.0	0.0	0.0
Inventory days	14	16	14	14
Debtors days	3	3	3	3
Average Cost of Debt	0.0	0.0	0.0	0.0
Payable days	42	35	35	35
Working Capital days	66	19	43	70
FA T/O	1.2	1.3	1.6	2.0
(D) Measures of Investment				
AEPS (Rs)	7.3	36.7	24.4	31.1
CEPS (Rs)	40.9	78.3	71.4	87.2
DPS (Rs)	0.0	0.0	0.0	0.0
Dividend Payout (%)	0.0	0.0	0.0	0.0
BVPS (Rs)	158.5	197.7	222.1	253.3
RoANW (%)	6.2	20.6	11.6	13.1
RoACE (%)	15.1	28.4	19.0	19.9
RoAIC (%)	13.7	18.5	28.4	39.7
(E) Valuation Ratios				
CMP (Rs)	1342	1342	1342	1342
P/E	183.5	36.5	55.1	43.1
Mcap (Rs Mn)	85,248	85,248	85,248	85,248
MCap/ Sales	5.0	3.8	3.1	2.6
EV	81,789	82,828	80,447	76,944
EV/Sales	4.8	3.7	2.9	2.3
EV/EBITDA	26.8	19.3	14.4	11.4
P/BV	8.5	6.8	6.0	5.3
Dividend Yield (%)	0.0	0.0	0.0	0.0
(F) Growth Rate (%)				
Revenue	68.8	31.6	22.7	18.5
EBITDA	145.2	40.4	30.6	20.7
EBIT	(208.0)	79.5	58.9	22.4
PBT	(152.1)	110.9	93.5	26.4
APAT	(147.2)	402.3	(33.7)	27.7
EPS	(147.2)	402.3	(33.7)	27.7

E – Estimates

Cash Flow

Particulars	FY22A	FY23P	FY24E	FY25E
Profit before tax	514	1,084	2,097	2,650
Depreciation & w.o.	2,135	2,642	2,987	3,562
Net Interest Exp	0	0	0	0
Direct taxes paid	(86)	(21)	(544)	(668)
Change in Working Capital	592	(669)	340	458
Non Cash	794	783	5	5
(A) CF from Operating Activities	3,949	3,818	4,885	6,007
Capex {(Inc.)/ Dec. in Fixed Assets n WIP}	(2,844)	(3,825)	(2,504)	(2,504)
Free Cash Flow	1,105	(6)	2,381	3,503
(Inc.)/ Dec. in Investments	(1,184)	910	(20)	(20)
Other	0	0	0	0
(B) CF from Investing Activities	(4,028)	(2,915)	(2,524)	(2,524)
Issue of Equity/ Preference	108	0	0	0
Inc./(Dec.) in Debt	(1,047)	(1,084)	0	0
Interest exp net	0	0	0	0
Dividend Paid (Incl. Tax)	0	0	0	0
Other	3,064	(161)	0	0
(C) CF from Financing	2,125	(1,245)	0	0
Net Change in Cash	2,046	(342)	2,361	3,483
Opening Cash balances	500	2,546	2,204	4,565
Closing Cash balances	2,546	2,204	4,565	8,048

E – Estimates

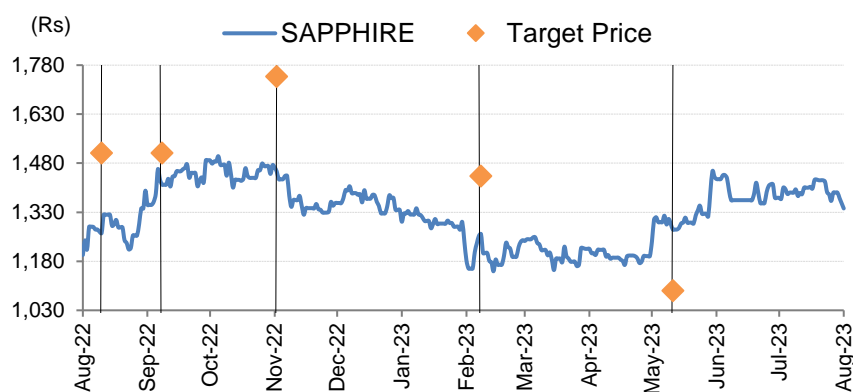
Notes

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
Aug-22	Buy	1,511	1,266
Sep-22	Buy	1,511	1,415
Nov-22	Buy	1,745	1,455
Feb-23	Accumulate	1,440	1,263
May-23	SELL	1,090	1,277

*Price as on recommendation date

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