1ST APRIL 2022

5 MINUTE STOCK IDEA

BY SMART SYNC INVESTMENT ADVISORY SERVICES

RESTAURANT BRANDS ASIA

WHAT WE LIKE

FASTEST GROWING QSR BRAND IN INDIA
Burger King has been the fastest growing QSR chain in India. Before Covid put brakes on the industry in FY21, **Burger King grew its store count at a CAGR of 85% for the period FY15-20.** In the same period, outlets of all the major QSR brands like Domino's Subway, McDonald's & KFC had a CAGR of <10%.

AGGRESSIVE GROWTH TARGETS AS PART OF FRANCHISE AGREEMENT

- **Master franchisee** of Burger Kings
- **Exclusive rights** to operate in India until 2039
- Aggressive target of scaling up 300 stores **to 700 stores by FY26**
- **Royalty rate capped** at 5% until 2039
- **Max Debt to Equity Ratio allowed is 2:1**

ENCOURAGING TRACK RECORD

- **High Sales growth with 65% gross margins.**
- **Cluster based approach** (6-7 outlets in one ring leads to efficient logistics)
- Target to **improve gross margin by 300 bps** in the next 2-3 years **through BK Café expansion** (higher margin business) & Economies of Scale
- **Well defined restaurant architecture** helps in setting up new stores quickly.

NEW INITIATIVES

BK Café

- To open 75 stores in 2-3 years
- Gross margin 80%
- Low capex and payback of 3-6 months Vs 5-6 years in case of Burger Kings stores

Burger King App & Delivery Based Revenue

- 2.5 million downloads already
- Helps in loyal customer base
- Cost of delivery through App is higher than aggregator-through delivery
- Dine In Delivery to moderate to 70:30 going forward.
- Drive-through stores and high speed locations

Entry into fast-growing Indonesian Market

- Store count to increase from 176 to 350 in the next 5 years
- Fund it through a QIP

FAST GROWTH DESPITE MEASURED STRATEGY
"I have got opportunities at the two, three sites in Guwahati which will be 3 lakhs, 4 lakhs kind of ADS sites but are not jumping and going into Guwahati until I build that Kolkata base and then kind of go out from there and build out their outline cities so it is a very disciplined approach"
- Rajeev Varma on the Q3FY22 Investor Concall

WHAT WE DON'T LIKE

RAPID GROWTH IN NEW STORES MAY DENT METRICS
ADS, SSSG & Brand contribution margins are the key metrics to measure the performance of any QSR. **However, when you are in a hyper expansionary mode,** all these metrics become difficult to track as new stores take time to mature and produce the desired levels of results. **Moreover, BK's growth target is so steep that it hardly leaves any room for any error.**

THREAT FROM CLOUD KITCHENS FOCUSED ON DELIVERY ONLY MODEL
Food aggregators are now becoming an indispensable part of the QSR industry. **With that, the growing number of cloud kitchens is also a cause of worry in the long run for BK and the rest of the branded QSR industry.**
Cloud Kitchens require far less capital to set up and much lower working capital to run compared to what BK needs. **On top of that, the aggregators have personalized data of crores of customers at their disposal which they can use to disrupt the branded QSR market.**

COST PRESSURES IN AN INFLATIONARY ENVIRONMENT
If inflation is here to stay for long, there is no denying the fact that it will lead to high prices for almost all of their raw material inputs. As BK has a strong durable brand, one can expect some of it to be passed on to the consumers. **However, it is fair to assume margin pressures in a prolonged inflationary scenario.**

ACQUIRING BURGER KING INDONESIA
BK India has diluted 11% of their holding in order to fund its acquisition of BK Indonesia. The aggressive target of reaching 330 stores is a challenge too. **It remains to be seen how they are able to achieve this ambitious target while chasing similar targets in India at the same time.**

STRETCHED VALUATION
At roughly 5500 Cr market cap, BK is trading at 6 times TTM Sales. **We at SSS believe that this number is good if the growth momentum continues in FY23.**
However, a few quarters of stagnation can lead to a significant de-rating.