Jubilant FoodWorks' Q2 and H1 FY21 Earnings Conference Call Transcript November 12, 2020

Management Speakers : Mr. Shyam S Bhartia, Chairman
Mr. Hari S Bhartia, Co-Chairman
Mr. Pratik Pota, CEO
Mr. Prakash C. Bisht, CFO

Moderator: Ladies and gentlemen, good day and welcome to the Jubilant FoodWorks' Q2 & H1 FY21 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded.

I would now like to hand the conference over to Mr. Siddharth Rangnekar from CDR India. Thank you and over to you, sir.

Siddharth Rangnekar: Thank you, and welcome to Jubilant FoodWorks' Q2 and H1 FY21 Earnings Conference Call for Investors and Analysts. We are joined today by senior members of the management team, including Mr. Shyam Bhartia – Chairman of Jubilant FoodWorks, Mr. Hari Bhartia – Co-Chairman of Jubilant FoodWorks, Mr. Pratik Pota – CEO of Jubilant FoodWorks and Mr. Prakash Bisht – CFO of Jubilant FoodWorks.

We will commence with key thoughts from Mr. Bhartia. Thereafter, we will have Mr. Pota sharing updates on JFL's progress and the strategic perspectives on growth. After the opening remarks from the management, the forum will be opened for question and answers.

A cautionary note, some of the statements made on today's call could be forward-looking in nature, and the actual results could vary from these statements. A detailed statement in this regard is available in Jubilant FoodWorks' Q2 and H1 FY21 results release and earnings presentation, both of which are available on the Company's website under the Investor Relations section.

I would now like to invite Mr. Bhartia to share his views with you. Thank you, and over to you, sir.

Hari Bhartia: Good evening, everyone. Thank you for joining us on the call today. I hope everyone is staying safe and healthy.

While visibility for the near-term demand has improved sequentially, we remain cautious from the broader economic impact of the global pandemic in the coming period. We, on our part, continue to navigate the COVID-19 pandemic situation and try to serve our customers, our communities with convenience, affordable, safe food and service experience.

I am pleased to report that the Company's second quarter results delivered a continuation of and, in many respects, an acceleration of the key themes we outlined on our previous call:

Firstly, our effort was to secure the quickest path to recovery. Despite tremendous headwinds from COVID-19, the Company secured the quickest path to recovery by adapting the business to new realities. This was done while according highest priority to health and safety of our customers and employees. I am glad to share that, as of today, we have reopened almost 100% of our store network across the country. And as you have seen in October, we have recorded near 100% sales recovery compared to last year.

Secondly, we have continued to leverage this opportunity to strengthen our operating model. During this crisis, we took significant steps to strengthen our business, increase our financial flexibility and optimize our cost structure. Notably, pursuant to our decision to close 105 unprofitable Domino's stores, we had effected their closure in H1 FY21, that is 5 stores in Q1 and 100 stores in Q2. As you are aware, these stores were part of margin improvement program during the pre-COVID period. However, we remain on track to open more than 100 new Domino's stores in the most viable store format as a result our network will be of similar size as last year. We plan to make our stores portfolio to become more profitable by the end of this year.

Thirdly, we have continued to leverage investments in our digital assets. Our continuous investment in our in-house tech platform has helped us to respond fast to our new requirements of business. The app downloads during Q2 at 6.3 million were the highest ever for the Company. Online orders for delivery sales have risen to 99%, thereby reducing cost and improving efficiency.

Fourthly, we have continued to innovate during this tough period. As you know, we launched the new Drive-and-Pick functionality, which will obviously allow our customers to avail of takeaway orders conveniently from within the safety of their vehicles and without stepping into the Domino's store. We have also launched a 'Pasta Pizza Party', with the launch of Pasta Pizzas and our new range of Pastas. Pratik will elaborate more on these.

Lastly, I must say, we continue our efforts on delivering superior performance. As a synergetic combination from revenue recovery and stringent cost control, despite host of challenges, the Company has delivered a superior performance, with improvement in earnings and substantial improvement in margins, year-on-year.

With the current business momentum, we are confident that the business will continue to improve to achieve near normalcy by the exit of FY21.

During the opening of COVID, we had curtailed our store opening plans. During Q2 FY21, we restarted our efforts and now have removed all stops, and you will see more store openings quarter-on-quarter in newer and more optimized format for all of our brands.

Considering all the requisite interventions affected by us in light of the changes in operating environment, I fully expect that when we emerge from the pandemic, we will be even more agile, responsive and efficient. We are continuing to invest significantly to further enhance our digital strength in maintaining a continuous dialogue with our consumers with relevant advertisements and promotional campaigns and in allied growth areas.

Now, I would request our CEO, Pratik Pota, to continue this discussion by sharing his perspectives.

Pratik Pota: Thank you, Mr. Bhartia. Good evening, and thank you for joining the Q2 earnings call today.

In the face of continuing COVID related headwinds, I am happy to report that we showed true resilience and mettle to deliver a strong all-round performance during the quarter. We executed a clear strategy and playbook to navigate this challenging environment during the quarter. We implemented a new set of safety and COVID containment SOPs in our stores and commissaries, which has allowed us to offer continued and uninterrupted service to our customers safely and consistently.

We reopened most of our stores across cities, with a few stores that were not opened being in corporate parks or in specific locations that have restrictions. We brought a strong focus on delivery and takeaway channels to mitigate the pressure on dine-in. In delivery, we removed the threshold of a minimum order value requirement that we believe will help grow orders and will allow us to tap into both a new set of emerging customers and also into new occasions. The takeaway channel continued to see strong momentum, and we made the user experience more smooth and more intuitive. We also launched the new drive-and-pick functionality, which will allow our customers to avail of our takeaway order conveniently from within the safety of their vehicle and which will simulate the drive-through experience. Dine-in remains muted as expected, though there was an encouraging recovery sequentially.

Our continued focus on digital helped us during the quarter. Our sharp focus on performance marketing helped drive app downloads to a record number of 6.3 million during the quarter. We also introduced a number of features on our app that helped improve the user experience and drive convergence.

We stepped up our marketing investments in Q2 with an aggressive presence on IPL through a promotion, followed by the launch of the ‘Pasta Pizza Party’. We had strong visibility both on television and on digital, and we had a dominant share of voice on television during the quarter.

We also maintained a tight focus on keeping costs under control. We made good progress on containing our fuel, energy and maintenance costs. We also did well to control our manpower costs in our stores. As a result, we were able to partly mitigate the impact of revenue deleverage on our financials. We also continue to invest in our future growth drivers. Hong's Kitchen business showed an encouraging recovery, and we now have five stores of Hong's Kitchen operational across Delhi NCR. Our range of RTC products ChefBoss that we launched last quarter is now available on leading e-commerce platform. While it's early days yet, we are encouraged to see the consumer trials and good reviews on these marketplaces.

Coming to the Q2 Results:

Operational revenue was Rs. 8,055 million, an increase of 111.8% sequentially. Our overall system sales recovery, for Domino's, was 82.3% when compared to the same period last year. Within this, the delivery and takeaway channels did well and grew by 5.8% and 49.8%, respectively. The dine-in channel continued to underperform and recovered 17.5% of system sales revenues compared to same time last year. Within this recovery, our larger metro towns of Mumbai, Delhi NCR and Bangalore showed a slower recovery as compared to other smaller towns. A total of 159 towns recovered their sales fully by September and showed a growth as compared to last year.

EBITDA for Q2 came in at Rs. 2,147 million at 26.7% of revenues, an improvement of 290 basis points year-on-year. The margin improvement was on the back of soft dairy prices, along with several specific cost optimization initiatives that were undertaken during the quarter. Profit after tax of Rs. 769 million increased by 1.3% versus last year. PAT margins at 9.5% were up by 180 basis points year-on-year.

The Company's cash position further strengthened during the quarter. Total cash and cash equivalents, bank deposits and investments increased from Rs. 6,401 million by end of Q1 to Rs. 8,278 million as we ended Q2. We opened 10 Domino's stores this quarter and entered into two new towns. Our new store count for the year so far, therefore, stands at 34 for Domino's. We also opened one new store each for Hong's Kitchen and Dunkin' Donuts. As committed during the last earnings call, we are on track for opening more than 100 Domino's stores during this year. In the international part of our business, we saw sustained recovery in both Sri Lanka and Bangladesh, led by online delivery sales.

Moving from the last quarter, with a more recent optimal performance, we saw a strong recovery continue in the month despite, if you recall, lapping a strong month from last year, which had both Dussehra and Diwali as part of the base. We had an overall revenue recovery of 96.2% with the channel wise recovery being similar to the preceding year's trend.

In summary, I would like to say that we are pleased with the performance last quarter in the face of continued operational challenges in a difficult demand environment. Notwithstanding the changing and uncertain nature of the COVID pandemic, we believe that the worst is well behind us and feel extremely confident about the future.

I would like to end by calling out the tremendous work done by all of our employees across the country. Their determination, resolve, their persistence and untiring efforts in the face of difficult circumstances has been truly humbling, and it has helped us serve our customers unceasingly and to recover faster. We owe our employees and our team members and their families a huge debt of gratitude.

With that, I will hand the call back to the moderator for Q&A session. Thank you.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the questions-and-answer session. The first question is from the line of Abneesh Roy from Edelweiss Securities. Please go ahead.

Abneesh Roy: Congratulations on the margin expansion. My first question is on the fusion product. So, you have come out with the Pasta Pizza. So earlier, you had tried another fusion product, Burger Pizza, which did not exactly go as per expectation. So my question is, what were the learnings from there in terms of pricing, product formulation, branding, which you will do differently and what is the confidence level this time versus Burger Pizza?

Pratik Pota: Actually, it's an interesting question that you asked. So, I would like to contrast Pasta Pizza and Burger Pizza, they are fairly different. I think the key difference is that the Pasta Pizza product as a format is a pizza itself. It's pasta on a pizza, there is no format innovation. The pizza is similar to any other pizza that we are known for. It is the introduction of pasta as a topping that makes it unique. The learnings from the Burger Pizza, indeed from all our innovations, is something that we always take on board, and we incorporate them in our launch planning. And I think the critical ones are ensuring that we do a lot of consumer inciting around the proposition, make sure we test the product, make sure we have operational readiness trials done. Those learnings are ongoing learnings. And we indeed tick those boxes before we launch Pasta Pizza, despite the challenges linked to having the launch happen in the middle of a pandemic. And I think the early response on Pasta Pizza that we have seen in terms of trial, in terms of repeats, in terms of customer feedback and NPS Scores, the feedback on social media, all of these has been extremely encouraging.

Abneesh Roy: My second question is on the store closures. So, such sharp quick closure of stores, especially when things are coming back so quickly. In terms of cost also, if you see, cost dynamics are also structurally lower versus what it was pre-COVID. And gross margin almost 250 to 300 bps expansion. My question is, what was the hurry to close 100 stores? And second, now most of the new stores, will it be adjacent to the existing store? I am asking this also because you have exited from six cities in Domino's. So, shouldn't you exit a city after the new stores are opened, so if you could address that part?

Pratik Pota: So, I think the important point is to go back to what we discussed on the call last time, which is that these 100 stores or 105 in total were stores where we saw no line of sight to profitability, despite a lower cost structure, both in terms of food cost and therefore high gross margins and in terms of lower operating costs, including lower rents. The reason for that fundamentally was, most of these stores were largely dine-in oriented stores, or stores in locations where we did not see traffic come back. So, when it was abundantly clear that there was no line of sight to profitability, then it made sense to exit from these stores quickly. I think it's important to also, in the same breath, say that our commitment is to open at least one store per store that we shut down. And therefore, we attempt to end this year with the same network size as we had when we entered this year. And as Mr. Bhartia said in his opening remarks that we are removing all possible barriers to store expansion. I think the important thing is to open stores that are efficient, that are optimized to serve under the new demand pattern and to serve customers across all channels, delivery, carry-out and indeed stores optimized for dine-in.

Coming back to your question about where the new stores will be, yes, we have exited some towns but we intend to come back in these towns, we also intend to open many more in new towns in the balance of the year. So, the new stores that we open will be in some cases same micro markets, where we were present earlier and where we shut the stores down. But in some cases, it will be more optimized for the new channel demand, the new demand pattern that we have seen by channel to sort of take advantage of the growth of delivery and takeaway. So, I think to summarize the key things, these stores were not going to be profitable in the next couple of years based on our modeling, and therefore, it made sense to shut them down ASAP, number one. Number two, we will be opening at least one store for every store that we shut down. Number three, these stores will be put both in towns that we are present there and also in new towns. So, we are a growth brand and a growth business. And based on the revenue recovery that we have seen last quarter and in October and the way our cost structures have been controlled, we feel extremely confident about the future. And our agenda is to open more stores, not to shut more stores.

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

Percy Panthaki: My first question is on your gross margins. So, in the last several years, your gross margins have gravitated towards the 75% kind of mark and last two quarters have been higher than that. So, would you say that the 78% kind of gross margin is the new normal going ahead?

Pratik Pota: I think it's important to understand the reasons why our gross margins have expanded in this quarter compared to, like you rightly said, the historical trend line, which was a little lower. I think there are three of four drivers of the gross margin expansion. The first one is a fairly soft commodity cost environment in dairy. Unlike last year, when we saw huge pressure on dairy prices, milk and cheese prices, last quarter, and indeed the year so far has been a lot softer, and that obviously helps us grow gross margins to an extent, number one.

Number two, I think compared to same time last year, if you remember the period of a year ago, there was intense competition and I think there was a lot of discounting on aggregator platforms. I think this year, the discounting has been lower. And indeed, our own discounts, therefore, have been calibrated accordingly. And in fact, lower discount also helped us expand the gross margin.

The third thing and very important work that the team has done is in controlling wastage through a lot better forecasting, a lot more vigil in the stores and, therefore, that's made us more efficient in the stores.

And the fourth reason, of course, is delivery charges. The fact that we introduced delivery charges towards the end of last quarter and Q2 was the first full quarter when we got delivery charges play out.

So, these are the four reasons that helped our gross margins expand. And if you go down the list, I think it's very clear that some of these are sustainable and some of these will correct as the price cycle plays out.

Percy Panthaki: Let me ask the same question in another way. This delivery charge that you have taken or rather introduced, would you consider that as part of your normal annual price increases or is that over and above that?

Pratik Pota: I think it's important to look at this from a consumer lens. I will say two things, charging for delivery is part of the operating protocol for the entire delivery ecosystem, whether it is food, whether it is grocery, whether it is any other service. We were the only outlier, the only exception to this rule which we have now corrected and we have introduced delivery charges, which are towards recovering partly the cost of delivery and providing the convenience at the customers' doorstep. So that's the first point.

The second point is that we recognized and we know that ensuring that we are in the right space in terms of value for money is critical. We are in the QSR space, our strategy is to expand and grow the market and grow the category amongst a set of very, very value conscious consumers. So, between the delivery charge introductions and anything else that we may do, we have to make sure that we keep value for money as an equation front and center. And we do nothing that damages that equilibrium.

Percy Panthaki: On your store opening trajectory, could you give us some idea how many stores you would target to open in FY22?

Pratik Pota: That's a little early right now. We are right now focused on FY21, the number we talked about for this year, as you know, is over 100 stores. But it would be fair to say that the momentum would accelerate for next year as we exit this year.

Moderator: The next question is from the line of Latika Chopra from JP Morgan. Please go ahead.

Latika Chopra: My first question was on revenue trends and the comments that you plan to achieve normalcy by the end of FY21. Now this quarter, though, you would have a base impact, with festivals being in the base. But at the same time, we had IPL which was not there in the base. So how should we read the growth trends? And what do you mean by normalcy by exit FY21? Do we expect the Company to recover back to normalized SSG growth levels or we are talking about absolute sales being same as last year levels? As there was IPL this year and then the base had Diwali? So just in that context.

Pratik Pota: The way we are seeing this is that IPL certainly had an upside similar to our delivery sales and for the entire category. There was also Diwali base sitting in last year's numbers. If we spread the numbers and do the math, we still believe that coming close to 100% recovery in October, I think it's very, very good momentum. And remember, the overhang of COVID continues, that's not gone away. And one of our channels has been underperforming for obvious reasons. That got a little better in October, in terms of the numbers, but still well below what it should be pulling at. So, all things put together, I think, October performance is very, very encouraging. I think the way to see this is to look at the trend line month-on-month. See, channel-by-channel, look at the numbers for each channel and see how both at system level and like-for-like levels, how the numbers have moved up. So, all the numbers that we modeled internally tell us that this is very, very encouraging. And this is ahead of what we have seen in the category in general.

Coming to the second part of your question. Yes, I think the way we are seeing normalcy is that we would see actual growth happen year-on-year and the COVID overhang to sort of become almost a non-issue. That we believe would happen towards Q4 or the exit of this year.

Latika Chopra: And as the markets open up, I just wanted to get a sense on how are you seeing the momentum on new customer additions, frequency of consumption from existing consumers as more food options become available? Any color on some of these underlying trends and how are they behaving?

Pratik Pota: There are two or three points to keep in mind here. I think the first large point and the contextual point that you all know is that, in India, the category frequency and the category penetration remain low. Structurally, we have always been a dine-in driven market, and even consumption within that, is actually low. Number three, we have been a highly fragmented market with a multiplicity of choice and very often driven by discounts and deals. I think a lot of these variables are changing. The market is becoming a lot more organized. I think there is a greater acceptance of food coming home, and there is going to be a shrinkage of marginal brands with questionable antecedence and questionable credentials. So, all of these trends, if you add them up together, it will mean three or four things. It will mean growth in the organized sector, faster growth. It will mean growth and faster growth of credible trusted brands. It will mean a faster growth in the delivery channel. It will mean faster growth on the back of online and technology.

Now all of these trends will do two things: (a), it is to grow the category, of course; and (b), it will play to us and for the brand. So, even as the market opens up, even as consumers now have more choice, we believe structurally the way that the market will shift, will be playing to our strengths.

Moderator: The next question is from the line of Chirag Shah from CLSA. Please go ahead.

Chirag Shah: The highest ever app downloads that you have seen of 6.3 million is very, very impressive. So of course, the lockdown is one of the incentives for the consumer to download the app. But beyond that, what are the efforts and promotion that the Company has done to give an incentive for the consumer to download? And at what stage do we start data analytics once the app is downloaded? And does the download mean that the consumer would have tried his first order on the app?

Pratik Pota: Thankyou Chirag, I agree, I think we were very encouraged to see the sharp increase in app downloads. And we were gratified because that was very clearly a conscious strategy on our part. What drove this? I think two or three things.

The first one is a very clear focus on performance marketing, which helped drive our consumers to download the app with a specific call to action and the increase of our spends on performance marketing by almost 80% versus same time last year. That was a very clear strategy to drive app downloads, number one.

Number two, our app through the last quarter and the last five months, has always been advantaged vis-à-vis other ordering platforms in terms of promotions and in terms of experience. So, in Q2, specifically, during IPL, we had a 50% Back-To-Cricket offer, which we ran exclusively on our own assets, our own apps. So, that was an incentive for customers to come in and download and order from our app. The Pasta Pizza launch was previewed first on our app for a fortnight before opening up to other platforms. So those are two reasons.

Third reason, we believe, is the fact that for Domino's users, the most intuitive and the most smooth and most seamless experience actually comes from our app. Because once you order on our app, your choices will be remembered, you can customize your pizzas. So, the time to transact, the time to complete the order is the shortest on our app. And customers began to see that and we saw that happen, and that's what actually drove our app downloads.

Our data tracking, to your point begins immediately once the app is downloaded, we prompt and encourage customers to place their first order. Once they place their first order, we, of course, get the feedback and customer satisfaction scores and then we prompt repurchase as well. So, there's a very clear customer engagement strategy which follows an app download. And our CRM strategy plays a very, very big role in complementing our app download strategy.

Chirag Shah: Understood. And my second question is on the store closures. Have we reorganized the delivery to service larger areas wherever you have closed stores or it doesn't make sense considering the increase in delivery cost that it entails?

Pratik Pota: Just to go back to my earlier response to Abneesh, I think a lot of the stores that we closed were actually dine-in stores. Obviously, in that case, this question is not relevant. But in cases where we had delivery stores closed as well, what we did do is reorganize the deliver area to make sure that those customers were serviced from a proximate store in the neighborhood, wherever we could do that without compromising the customer experience.

Moderator: The next question is from the line of Avi Mehta from Macquarie. Please go ahead.

Avi Mehta: Two questions. One, continuing on the store closure bit. Now, you have maintained that you would look to at least maintain the store count. How would you change the portfolio now? Would it be a change or in what form, location by size if you could kind of share your thoughts on that, please?

Pratik Pota: As we said on the call last time, and given the changing nature of the channel-wise demand, the stores that we open this year will be a little different from the stores that we had in the past and especially the stores that we have closed, in a couple of ways. I think the first is that they will be a lot more optimized for delivery and carryout. They will not be dine-in dependent alone, they will be smaller stores, more compact, typically of a 700 to 800 square feet size, that will allow us to deliver to neighborhood very, very quickly, and allow us to also give a good easy takeaway experience. Given the size and given their objective, they will be located close to neighborhood in high streets, in residential areas, typically, they will not be in malls for the larger part and they will certainly not be in the food courts. So, in that sense, for the larger part, the new stores will be a little different from the ones that we are closing. The only exception that we would make is when we enter a new town where we believe that there will still be a demand for dine-in, the store might be a little larger and with slightly more dine-in covered to allow the experience to be had by consumers in that new town. But even then, the store would be between 1,200 to 1,300 square feet, it will not be much more than that. So, yes, to summarize, smaller, more efficient stores, optimized for delivery, carryout in existing towns with some space for dine-in in new markets.

Avi Mehta: And second just a book keeping bit about discounting. How has that trend kind of behaved? Have you seen an increase in the festive period or does it continue to be below historical levels? That's all from my side.

Pratik Pota: So, if I do the trend line on discounting, sequentially, of course, there has been an increase because in Q1, I think everyone was looking to just drive continuity of business rather than discounting. So there has been that increase sequentially. But on a year-on-year basis, there has been a softening of the discounts, both for us and for the category in general.

Going forward, unless there is some irrational behavior which comes again, we believe that the worst of aggregator-led discounting is behind us, and we see a lot more rational discounting regime continue in the quarters to come. Also, I think it's important to recognize that consumers have become a little less discount and deal seeking and a little bit more value and quality seeking. That will also help moderate the discounting behavior.

Moderator: The next question is from the line of Vivek Maheshwari from Jefferies. Please go ahead.

Vivek Maheshwari: Just two questions. Firstly, I know it's an apple to mango comparison, but let's say, as things have started picking up, we have seen a pullback in packaged foods. Now Jubilant or Domino's for that matter is at a very interesting juncture. So, one side is the delivery and the takeaways and the other side is dine-in. As things pick up, customers get more experimentative, in that context how do you think about that, is there a possibility that you have had a huge advantage in the last few months of being the most trusted brand, as consumers start, let's say, looking out for options, is there a possibility that some part of the benefit goes away and gets to the competition, do you think that is something which is possible?

Pratik Pota: I would sort of go back to my answer that I gave earlier, and the things are as follows. I think our category still in India is small and nascent and has ample room to grow both in terms of penetration and in terms of frequency. We have seen, in the last six months, adoption of delivery as a channel, as a service increase across multiple categories, including in food. What has been very encouraging in our case, in our category has been the adoption of delivery in the smaller towns. So, delivery growth has been much stronger in smaller towns compared to the larger towns. Such behavior change, as we know is a one-way street, once the behavior changes it endures. We also know that dine-in has a role to play. The occasion that dine-in caters to, the moment and the occasion and the celebration the dine-in caters to of providing an experience that occasion will remain relevant for time to come. It got a little muted right now because of COVID. But once that goes down or goes away, dine-in will come right back. To all of this, consumers will navigate increasingly so by hygiene, safety, trust quality, whether it's dine-in, whether it's takeaway, whether it's a delivery. They will also navigate by quality of service and quality of products. All of these are our strengths. So as the market opens up, as, I think, more choices get available, I think the market will grow, number one. Number two, the contours of the market growth and the change will play to our strength. So, it doesn't deter us at all. And in all our modeling, we are not seeing that play out. We're not worried about a competitive headwind coming our way.

Vivek Maheshwari: Got it. Sure. And on the other expenses bit, how should we think about this line item because on a Y-o-Y basis, I mean, Q-o-Q may not help much. But the Y-o-Y comparisons, when I look at, it is still quite below. Of course, part of this will be variable. But if I look at from a second half perspective, how should I think about whether in terms of percentage of revenues or on an absolute basis how do you think about that line item?

Prakash Bisht: Yes, so Vivek, as you have seen in the first two quarters. And particularly in this quarter, you have seen that we have maintained and we have controlled the fixed cost. Of course, this line item has partly variable cost and partly fixed cost. So far, we have maintained this cost line item. So, to the extent it is variable, of course, it will go up. But I think the right way to see it is in terms of percentage to sales. So far, we have been able to manage the percentage of sale. We do not foresee too much change happening there. Of course, in the first two quarters we had rent concessions, the savings of the rent concessions have gone into this line item. In the next two quarters, whether we will be able to maintain the same pace of concession, that's a thing that we will discover in the next two quarters. Barring that, we believe that this is not going to go too much higher or lower in terms of percentage to sale. I think that is the right way to see it.

Vivek Maheshwari: Okay. From the second quarter level?

Prakash Bisht: Yes. So maybe to the extent of rent you must see and the rest of the things, you should see that we will try to cover the expenses in-line with this, because to the extent variable will move with the variable, fixed costs we have controlled so far, we will continue to control them. Rent concessions, we will see how it will spell out in Q3 and Q4.

Pratik Pota: If I can add to that, I think in the other expenses line, there were three drivers of productivity, as Prakashji said. One was rent, clearly. The other one was productivity in specific cost lines in our stores, whether it was energy, fuel, housekeeping, etc. And there was obviously the saving on account of some lower G&A, travel, etc., because of, again, obvious reasons. We will also offset the hit in this line, on account of two things. One is that, of course, expenses linked to COVID and the incremental cost of sanitization, etc., which hit us. That's one hit. Along with that, our increased marketing spends. This was an IPL quarter, and therefore, we had to increase our marketing spends as well. So those are the pluses and the minuses. Some of these will sustain over time, the costs or advantages, some will get mitigated. So that's the way we are seeing this play out. As COVID costs go away, as marketing expenses normalize, rents also will go away. So, some of that will get neutralized.

Moderator: The next question is from the line of Resham Jain from DSP Mutual Fund. Please go ahead.

Resham Jain: Just two questions. So, first is on the loyalty feature which we have added into the app, if you can just share your thoughts around that? And any global experience if you can share related to royalty feature, how it will help the overall performance going forward.

Pratik Pota: So Resham, loyalty is something that we are still piloting, it's in a pilot stage right now, in a couple of markets. So, it's early days to talk about our own experience with loyalty. That's still relatively recent. And also, there is a little bit of noise because of COVID. If I pull back and address your larger questions about loyalty and what role it could play, I think we believe that loyalty has an important role to play in driving frequency, driving stickiness and driving occasions. And that's something we intend to do, therefore, explore and push in the times to come. We are fortunate that we have access to the global learning from Domino's, the Domino's ecosystem, both in the U.S., in Australia and other parts of the world. And you can be sure that we keep benchmarking them and learning from them and assimilating and incorporating the best of what they have done and their learning into our program design. So, that work is going on. But it's early days to report an update on loyalty yet.

Resham Jain: Okay. My second question is on Hong's Kitchen and Dunkin' Donuts. After the downsizing of Dunkin' and now with five stores of Hong's Kitchen, where are we in the journey, are we confident enough now with whatever different formats or the products which we have launched over there to take it to the next level? Or do you think that it is still couple of years before ramping it up significantly?

Pratik Pota: Dunkin' has seen a slower recovery than Domino's, which, I think, is natural and to be expected, and that's the way we modeled it, given its larger dependence on dine-in and given its format of the product and the portfolio. That said, and we have called it out last time as well, we believe that the future of Dunkin' lies in having smaller stores, more compact stores, in few place kiosk-like stores, which have beverages, which have donuts and which have simple food. And whenever we opened such stores, we have been encouraged by the results we are seeing there. If I take away the COVID wave, we believe that Dunkin' has a path to scale with a model like that. But of course, it will be tested at scale once COVID becomes less of a factor.

On Hong's Kitchen, as I called out in my opening remarks as well, very encouraging recovery post COVID of the business. We have now got five stores in Delhi NCR, we intend to go to 15 stores as we exit this year. We were encouraged by the response to our value range that we launched earlier this year. We are encouraged to see customer feedback, both on the product, on the packaging and our service. And we believe that the space that we are trying to explore and sort of blow up, which is that of Chinese QSR, affordable great tasting Chinese food served across channels, I think backed by a credible brand. I think that space, we believe we can exploit and leverage and build the brand in. So, I think good early results, very encouraged and we intend to scale it up in Delhi NCR in the balance of the year.

Moderator: The next question is from the line of Aditya Soman from Goldman Sachs. Please go ahead.

Aditya Soman: Congratulations on some good sequential improvement. However, I mean, were the overall sales still underwhelming given that, if you look at in a global context where Domino's is seeing high-teens sort of growth, we have seen even on the delivery side about mid-teens in October. And this is taking into consideration that we had close to a 10% sort of effective price increase because of the delivery fee and the app growth has been about 73% year-on-year. So, would that mean that for a downloaded app, the number of orders has effectively halved?

Pratik Pota: I would not call the revenue performance underwhelming, and I would not do a like-for-like comparison between India and other markets without incorporating and looking at the other factors as well, in terms of the COVID case load, in terms of working hours in which stores are allowed to operate or not, in terms of contribution of various channels between delivery, dine-in, takeaway across various markets. I think the way to look at this is to say that despite the continued headwinds on COVID, in Q2, and as we all know, even as the lockdown was revoked and unlock happened, the COVID cases continued to increase and the fear factor around that continued to increase. So, there was continued customer fear, anxiety, reluctance. In the face of that, we have come back to nearly the same revenues as last year in the month of October despite having a significant channel mix towards dine-in in the way. And again, all that we have seen gives us conviction that this momentum will sustain and we will start building back revenues, working around the dine-in handicap through delivery and takeaways. And of course, a big driver of that has been our digital assets, has been our digital strategy, has been our digital app download number, that has been our focus on continued marketing. We are the only brand that has maintained salience and marketing presence, brand presence across both the quarters nonstop. First, we were setting focus solely on safety and then, of course, more on safety plus food, and then on promotions and innovations. So systematically, we have built back the growth drivers, and that led us to come back to almost the same revenues as last year.

Aditya Soman: No, absolutely. I understand your perspective, Pratik. And about the second question, where you have got sort of your total app downloads has gone up to, say, 44 million from 25 million. But we are not seeing the same level of increase in total orders, and we have also seen a price increase. So, would that mean that the number of orders per consumer who has downloaded the app gone down significantly?

Pratik Pota: Actually, on the contrary, the contribution of our orders on our own assets and the order growth on our own assets has been highest ever, has been very, very encouraging. So, I would not call that out. I think, if anything, the fact that we have driven our apps singularly and driven the app download and driven customers to come to our app through promotional probe, through differential propositions, that has what has helped us drive order growth and delivery. So, if you double click on the given numbers, and we don't share the data publicly, the reality is that our app has shown a very, very healthy increase in orders.

Aditya Soman: Fair enough. And just a couple of bookkeeping questions, I mean, one is on CAPEX per new store. And second is, what would be the impact on SSG of the store closures, especially where you have closed in, say the delivery stores?

Prakash Bisht: Yes. So, overall CAPEX for the year, we see in the range of Rs. 200 crore because, of course, we are opening 100 stores and we are opening stores for other brands, and there will be, of course, some maintenance CAPEX and other spends. And with regard to the SSG on the closed stores, because most of the time these stores were any way closed during the year also, they were not operating. So as such, and most of the stores, as Pratik had explained, they were dine-in stores, they were in malls and they were in food courts, so their SSG impact is very difficult to explain because the dine-in segment itself is subdued at this point of time. So that even if they were opened, that would have been very, very minimal.

Aditya Soman: No, but earlier with larger stores, our store CAPEX was about, Rs. 1 crore to Rs. 1.1 crore, right? So why is the CAPEX almost 2x now?

Prakash Bisht: No, Aditya, so it's 100 stores, plus, of course, there are stores for other brands plus, there will be other reimaging and maintenance CAPEX. The number that I am giving you is a rough cut in the range.

Moderator: The next question is from the line of Kishan Gupta from CD Equisearch. Please go ahead.

Kishan Gupta: Basically, I want to understand what sort of sales cannibalization happens when you open new stores in places where you have no small presence like Mumbai, Pune, New Delhi, Bangalore and Chennai?

Pratik Pota: So, what we have seen consistently when we have fortressed our markets and opened stores in the neighborhood of existing stores is that our service levels improved significantly, we deliver to our customers much faster. And that, in turn, helps improve customer satisfaction and this in turn drives reorders and repeats much faster. So, our existing stores, the mother stores, sees a temporary drop in revenue, but then it comes back to the original revenue levels quickly within a year's time but with a much better customer experience, and therefore, typically a higher frequency over time. And the new stores end up servicing some of the old areas better but also creates typically new market which it caters to. So, the 1 plus 1 is better than 2, typically, that's how the fortressing strategy works.

Kishan Gupta: So basically, as you talked about this, what do you think is the store potential for cities like Mumbai where you have already almost over 100 stores?

Pratik Pota: So, whether it is Mumbai or whether it is any other market across the country, we are excited by the opportunity that lies ahead. We believe that there is tremendous opportunity and tremendous sales worth to add stores. Both in markets like the one you described and also in markets which are smaller, where we have one store, where we can add one more, where we have two, so we can add maybe one or two more. And of course, in 300, 400, 500 towns, we don't have a store right now. So, I think what excites us, when we look at Domino's in India and indeed in Sri Lanka and Bangladesh as well, is a sheer run way we have to add more stores. And hence, our strategy of really ensuring that we remove all bottlenecks and all the barriers to store expansion.

Kishan Gupta: But if I see your store count, it is more concentrated in these cities. So, 50% or more than 50% of our stores would be in these six cities basically?

Pratik Pota: That's right. And as we go forward, not only are we fortressing these markets but we will also be entering a large number of new markets as well. So, if I look at the store opening strategy, we will make sure that we strengthen our presence and fortress our presence in markets like Mumbai, markets like Bangalore, Delhi NCR, etc. We will ensure we have more stores and more distribution and access points in smaller towns, in the Tier 2, Tier 3 towns, where we may have one or two or three stores. And then we also have a strategy of entering towns where we have no stores right now. So, while you are right, historically, our bias has been more towards the larger markets, increasingly you will find us to be a store network that is present deeply in large markets like Mumbai, but also present across a large number of markets distributed as well.

Moderator: We take the last question from the line of Manoj Menon from ICICI Securities. Please go ahead.

Manoj Menon: Just a couple of questions on cost, actually. One, given that now the delivery charges are pretty much part of the template, the gross margins band from around 74% - 76%, does it now move to structurally a higher number, it could be 76% - 79%? Just from a band point of view for the medium term?

Prakash Bisht: I think it's difficult to put the numbers. As Pratik explained it in the earlier part of the call that the improvement in gross margin is a product of at least the favorable commodity prices, we see less pressure on discounting in the delivery charges and the efficiencies that we have brought in. Of course, out of these four, commodity prices are not in our hand. Discount to a limited extent, it's in our hands, but though Pratik already mentioned, that we believe that the aggressive discounting that we saw in the previous periods may not come back. So, out of these four components, two components are sustainable, two components are not in our control, they will move with the environment.

Manoj Menon: Understood. Just quickly on the same, when I move beyond as per the gross margins, or including gross margins actually on the COGS, could you just comment about some of the work which you have done, some of the good work which actually could result in permanent cost savings? I am not looking for a quantification, I am looking for a directional understanding.

Prakash Bisht: So, Manoj, this was mostly discussed in the earlier part of the call also. We have worked on various kinds of productivity during this period. So obviously, one of them was rent which is, obviously, disclosed in the results also, you know the number. But there are lot many other productivities that we have driven and which is reflecting in the numbers that despite many of the fixed costs in these line items, we did not allow it to affect the leverage, or no deleverage is reflecting. So, that could happen primarily because we worked on our store operating costs, we have worked meticulously on controlling the store operating cost. We have also worked around bringing the efficiencies in terms of the wastages, we have controlled, we have also controlled miscellaneous line items within the other G&A. There also we have gone structurally, and we have tried to control. So, the results that you are seeing is a combination of the productivity and some of the impact which is rent, which is mostly during this period. So, some of them are going to be sustainable because whatever structural changes we have made in terms of productivity, in our store operating cost, they will sustain. Some of them to the extent of rent concessions and all will depend on the environment. And some of these costs are variable, so they will change with the volumes. So, that's how it's going to play out.

Pratik Pota: If I can add to what Prakashji has said, I think a few things that I want to underline. The first one is much more efficient deployment of manpower in our stores. And further to what we discussed on the last call that we changed the manpower deployment model to a variable model, that led to a structural improvement in our manpower productivity, and that we believe will endure.

The second piece of good work which was done was in reducing the energy cost in our stores. And again, we called it out a couple of quarters ago that we now got energy management systems across all our stores, and the data we generate from the stores is used very effectively and very, very surgically almost to identify stores that are underperforming on actual consumption. And therefore, intervene there. So, our energy costs came down substantially during the quarter. We believe this is something that hopefully we will endure as well.

The third area where we had some very good work done was on reducing store level wastage. In Q1, all of us, I think the entire industry was caught on the wrong foot post lockdown, where we had unplanned, unforeseen wastages happened. But structurally, I think the work that the team did between operations, finance, supply chain, to improve the forecasting accuracy, to improve the vigilance in the stores in terms of ensuring that we were dosing as per standard recipes and compliant with that, all of that led to a significant improvement and reduction in store level food wastage.

The fourth area, again, where we saw improvement was in the cost of delivery and the vehicle operating costs. We used this COVID period to also intervene with a lot of reporting and technology interventions in the stores and we could scrutinize the consumption by assets, by stores much more closely. And using that data you're able to intervene and control the fuel cost as well in our stores. So, these are structural interventions. I could go on, but these are four or five big things that we did, which we believe were not coincidental because they were driven by the team, and most of these we believe would endure in the future as well.

Manoj Menon: Completely understood. Just one last thing, if I may, and this is quite straightforward, actually. Just before COVID or maybe reasonably prior to COVID actually, there was a thought to reimagine about 100-odd stores every year for a different touch and feel, and I do remember visiting one of those stores in Bangalore, maybe a year back or so. Is that in the back burner currently? What is the thought process? Because it may be a great opportunity to do a lot of this work when really no dine-ins are actually happening.

Pratik Pota: So Manoj, I think for obvious reasons, store level reimaging also took a bit of a backseat during the first four, five months of this year. But it is absolutely part of our strategy to reimage the old stores and bring them up to the required standard. And one reason why the CAPEX number is also higher, which I was referring to an earlier discussion on this call, is that we intend to reimage existing stores as well. So, it's absolutely part of our strategy, and we continue with it in balance part of the year.

Manoj Menon: Understood. So, 100-odd stores would remain, right, broadly speaking?

Pratik Pota: That's right. That's for obvious reasons, the trend line directionally that's the intention.

Manoj Menon: And the newer stores would be reimagined, if I am right?

Pratik Pota: That's right. All stores that we are opening now are in the new design, what we call the Ace design. And we have got tremendous feedback for the new design. And that's now part of our design template, not just in India, but across Bangladesh and Sri Lanka as well.

Moderator: Ladies and gentlemen, that was the last question for today. I would now like to hand the conference back to the management for their closing comments.

Pratik Pota: Thank you, everyone for joining the call today. I do hope we have been able to answer and address all the questions that you have asked to your satisfaction. Despite the ongoing challenges, the strength and resilience of our business model has led to an encouraging recovery of our business, both in quantum and in space. We are excited about the opportunities that lie ahead and are confident that we have the right strategy in place to tap into them in this emerging new world.

I wish you and your families a very Happy Diwali. And one request, please don't forget to order your favorite Domino's pizzas while you enjoy the festival with your near and dear ones.

Should you need any more clarifications, feel free to reach out to us. Thank you, and Happy Diwali once again.

Moderator: Thank you. On behalf of Jubilant FoodWorks Limited, that concludes this conference. Thank you for joining us, ladies and gentlemen. You may now disconnect your lines.

Note: This transcript has been edited for readability and does not purport to be a verbatim record of the proceedings.