

Sapphire Foods

Weak SSSG impacts profitability

Sapphire's Q4FY23 performance was operationally weak, largely led by moderating SSSG. While the India revenue grew by 23%, led by store addition, SSSG was weak for both KFC (+2%) and PH (-4%) on account of a tough demand environment. The impact on operating margins was more profound (more so for the weaker franchise like PH) as weak SSSG led to negative opev. KFC/ PH ROM fell 110bps/ 530bps QoQ to 19/8.6%. Notwithstanding near-term weakness, the management has maintained its medium-term guidance of 5-7% SSSG growth and doubling store count (over 3-4 years). In the near term, we expect pressure on margins for QSR companies to sustain due to decelerating discretionary spending. We maintain our EPS estimates and value Sapphire at 50x P/E on Jun'25 EPS to arrive at a TP of INR 1,000. Maintain REDUCE.

- Revenue growth supported by store addition as SSSG moderates:** Consolidated revenue grew by 13% YoY (19% HSIE) to INR 5.6bn. India revenue grew by 23% (HSIE 26%), which was supported by 30% store addition as SSSG was weak. KFC/PH revenue grew by 24/18% YoY while SSSG weakened to 2/-4% due to demand softness. ADS declined by 4/9% YoY (down 7/14% QoQ) for KFC/PH. Transaction growth remained positive for PH while KFC saw a decline, as per the management. Dine-line continued to do well for KFC, whereas PH saw broad-based growth across both channels. Recovery in Sri Lanka sustained with revenue growing by 10% in CC (down 27% in INR due to currency impact). Notwithstanding near-term pressure, management remains optimistic of 5-7% SSSG growth in the medium to long term. However, given the deceleration seen in discretionary demand, we bake in SSSG of 2/9/5% for KFC and 1/9/6% for PH over FY24-26. We estimate consolidated revenue will grow at 19% CAGR over FY23-26E.
- No change in store opening guidance:** Sapphire opened 16/78 KFC and 12/67 PH stores in Q4/FY23. Despite the near-term weakness, management has reiterated its guidance of doubling store count over the next 3-4 years. We are building 220 KFC and 120 PH store addition over FY24-26.
- Margin pressure as SSSG weakens:** Gross margin saw sequential improvement on a consolidated level as well as brand level on softening RM basket. However, with weak SSSG growth, the consolidated ROM/EBITDA margin contracted by 230bps/260bps YoY. While KFC ROM expanded by 10bps (down 110bps QoQ), the contraction was steep for the weaker PH brand which saw a decline of 290bps YoY (530bps QoQ).
- Call and BS/CF takeaways:** (1) Management believes current demand pressure is only in the near term. (2) Yum stepped up innovation and marketing spending in April in order to support demand. (3) If at all softness extends, management shall recalibrate store expansion plans. (4) In KFC, a 3.5% price hiked in April'23. (5) Sri Lanka's operating conditions have improved. Expect to reach 20% RoM in the next 12-15 months. (6) Deferred tax credit of INR 1.2bn boosted PAT in Q4. (7) In FY23, FCF stood at INR - 23mn vs INR 1bn YoY.

Quarterly/annual financial summary

(INR mn)	Q4FY23	Q4FY22	YoY (%)	Q3FY23	QoQ (%)	FY22	FY23	FY24E	FY25E	FY26E
Net Sales	5,604	4,968	12.8	5,961	(6.0)	17,216	22,656	27,276	33,260	38,612
EBITDA	981	998	(1.7)	1,167	(15.9)	3,050	4,284	4,977	6,173	7,236
APAT	1,355	265	411.3	327	314.4	460	2,332	889	1,158	1,545
EPS (INR)	21.32	4.17	411.3	5.15	314.4	7.2	36.7	14.0	18.2	24.3
P/E (x)						162.8	32.1	84.2	64.6	48.5
EV / EBITDA						40.3	27.6	24.2	18.1	14.8
RoCE (%)						6.2	20.5	8.1	8.2	9.3

Source: Company, HSIE Research

REDUCE

CMP (as on 12 May 23) INR 1,277

Target Price INR 1,000

NIFTY 18,315

KEY CHANGES	OLD	NEW
Rating	REDUCE	REDUCE
Price Target	INR 1,000	INR 1,000
EPS %	FY24E	FY25E
	0%	0%

KEY STOCK DATA

Bloomberg code	SAPPHIRE IN
No. of Shares (mn)	64
MCap (INR bn) / (\$ mn)	81/992
6m avg traded value (INR mn)	255
52 Week high / low	INR 1,574/909

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	6.0	(6.6)	22.8
Relative (%)	3.8	(7.0)	5.6

SHAREHOLDING PATTERN (%)

	Dec-22	Mar-23
Promoters	44.90	44.90
FIs & Local MFs	24.95	27.44
FPIs	16.54	15.50
Public & Others	13.61	12.16
Pledged Shares	0.00	0.00

Source : BSE

Pledged shares as % of total shares

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Disclosure:

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