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CRISIL Opinion

Organised fast food in the fast lane

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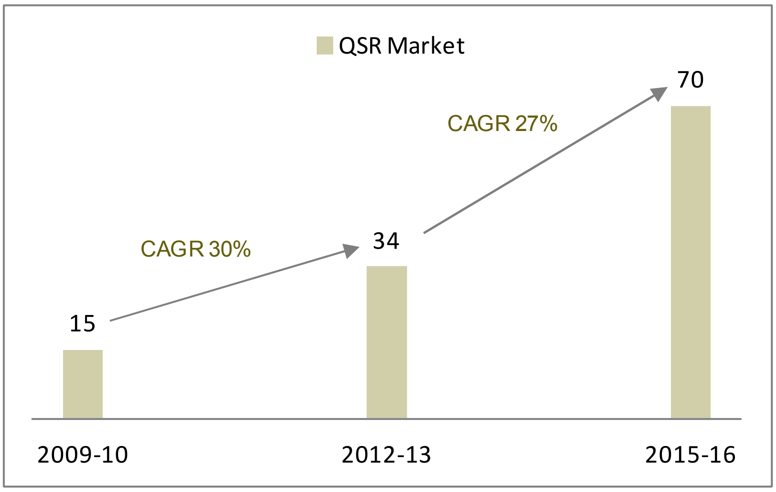
(Organised) Fast food in the fast lane

- Organised fast-food chains, also called quick service restaurants or QSRs, have bucked the economic slowdown and are growing by leaps and bounds.
- As a result, CRISIL Research estimates the QSR market will more than double to Rs 70 billion over the next three years from Rs 34 billion in 2012-13.
- And what would be the secret sauce of success? Rapid store additions in Tier II and III cities by established foreign players and increased access to outlets multiplying consumption.
- On the flip side, the downturn and increasing competition (especially in Tier I cities) will lead to much slower same-store sales growth.

Quick Service Restaurants market to grow two-fold in the next three years

The entry of McDonald's in 1996 marked the beginning of the QSR concept in India. Many global brands have followed suit since then, either through company-owned stores or the franchisee model, or a mix of both. Over the past 5-6 years, many Indian QSR brands have also mushroomed across the country, serving either foreign cuisine or adapting Indian cuisine to the fast food service format. This helped the Indian QSR market to expand rapidly to about Rs 34 billion by 2012-13. CRISIL Research expects this strong growth to continue over the next three years, as global brands expand into smaller cities. We expect the QSR market to reach a turnover of Rs 70 billion by 2015-16, growing at an average annual rate of about 27 per cent.

Growth in Indian QSR market

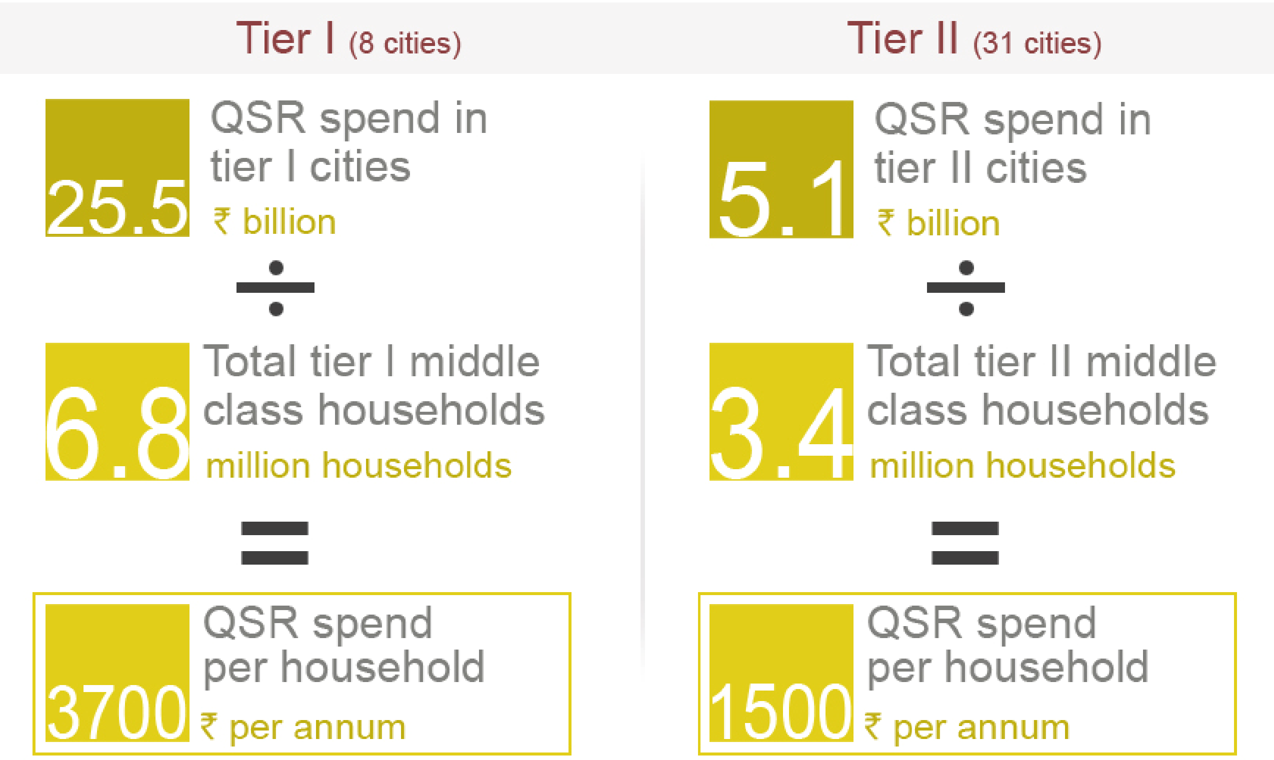


Source: CRISIL Research

Growth to be higher in tier II markets

CRISIL Research has separately analysed per-household spends on organised fast food or QSRs for the tier I and tier II markets. (Together these markets account for about 85-90 per cent of the QSR industry's revenues). Interestingly, on an average, a tier I middle class household spends about Rs 3,700 per annum for eating at QSRs. This roughly equates to about 12 pizzas per household per annum. However, the next phase of growth will revolve around tier II cities. Annual spends on QSRs by middle-class households in these areas are expected to surge by 150 per cent to Rs 3,750 per annum over the next three years. In comparison, annual spends in tier I cities are expected to increase by more than 60 per cent to about Rs 6,000 by 2015-16. The quantum jump in QSR spends in urban areas will be propelled by an increase in nuclear families and working women, steady growth in incomes, changing lifestyle and eating patterns, and more importantly, greater accessibility of QSR outlets.

QSR spend per urban middle class household in Tier I and Tier II cities



Source: CRISIL Research

Note: Middle class has been defined as households having annual income in excess of Rs 200,000.

New outlets to largely aid growth in QSR market

Growth in the Indian QSR industry is expected to be largely driven by new outlets. We expect outlet additions to continue to grow at an average annual rate of 16-18 per cent. The remaining 8-10 per cent growth is expected to come through an increase in same store sales.

Total Quick Service Retaurants growth
(27 per cent)

- New store addition (16-18 per cent).
  - Established foreign brands (Tier II and Tier III)
  - New Indian QSRs (Tier I)
- Same store sales growth (8-10 per cent)
  - Price Hike (5-6 per cent)
  - Increase in transactions (3-5 per cent)

Of the total store additions, we believe that 40-45 per cent will take place in tier II and tier III cities. Currently these markets account for just 25 per cent of total outlets. For large, established players who already have a sizeable presence in tier I cities, tier II and tier III markets are expected to account for roughly 70 per cent of store additions over the next three years. Large players have already established a strong brand and are better-placed to take advantage of the lower lease rentals and limited competition that smaller cities offer. On the other hand, new entrants and relatively new Indian QSR brands are expected to focus more on larger cities and consolidate operations in a single region before moving on to newer markets.

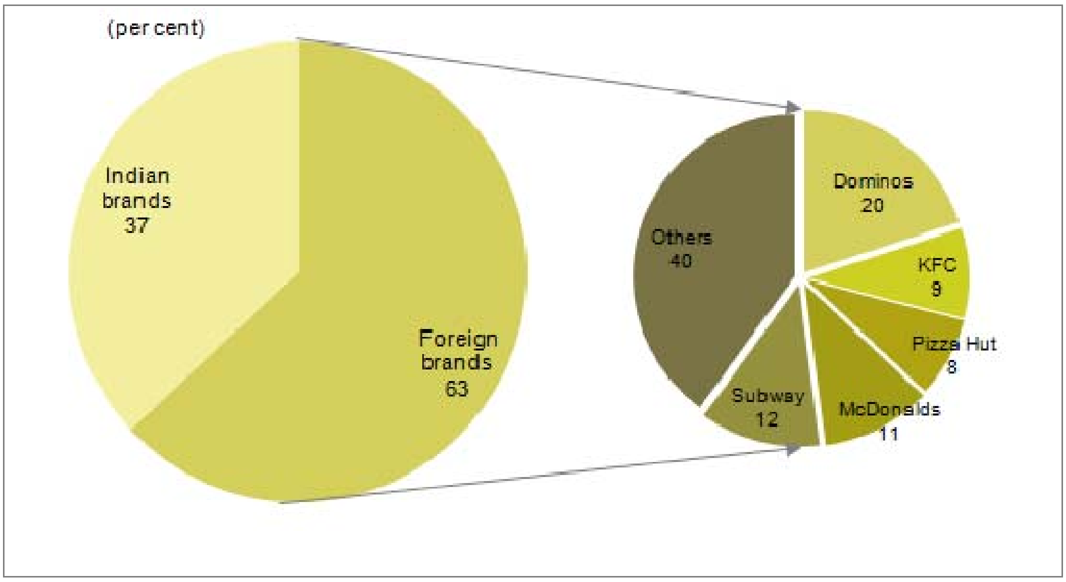
Same store sales growth to remain subdued in the near term

Same store sales, which have been growing at a robust 20-25 per cent over the past few years, are expected to slow down significantly in the near term. Two factors will cause the decline in growth: 1) An economic slowdown, which will curb discretionary spending; and 2) cannibalisation due to opening of multiple outlets in the same catchment area and a resultant increase in competition. Growth in same store sales is expected to come from a 5-6 per cent hike in prices (in line with the typical hikes made every year) and a 3-5 per cent increase in the number of transactions at existing stores. Stores set up in the last couple of years are expected to see a higher increase in transactions per outlet, as new stores usually take 2-3 years to ramp up operations.

Foreign brands dominate market

McDonald's was followed into India by other international brands such as Dominos, Subway, Pizza Hut and KFC. These brands typically operate through the franchise model, which helps them expand rapidly with minimal capital investments. These foreign players have established themselves strongly and currently dominate the Indian QSR market with an aggregate share of 63 per cent (based on the number of operational outlets).

Break-up of market share



Source: CRISIL Research

Foreign cuisine more adaptable to QSR Format

Foreign cuisines dominate the menus in quick-service restaurants. Easy adaptability to the cold storage format and the quick-to-serve nature has made them more amenable to the QSR market. Currently, pizzas, burgers and sandwiches together account for about 83 per cent of the total QSR market.

In comparison, it is more difficult to adapt Indian food, which is prepared through complex processes using several ingredients, into an assembly line production model. This is reflected in the lower market share of Indian cuisine in the QSR market. However, efforts are underway by domestic players such as JumboKing and Goli Vada Pav to successfully implement the quick-service model to domestic cuisines.

Definition of QSR market
A quick service restaurant (QSR) is characterised by fast food cuisine, minimal table service and a fixed menu. The food (or ingredients) is prepared in bulk in advance and is packaged to order. QSRs are usually part of a restaurant chain or a franchise operation, which provisions standardised ingredients and/or partially prepared foods and supplies them to each restaurant through controlled channels. It is different from fine dining, as the latter usually targets rich and upper middle class consumers. Fine dining restaurants also offer a unique ambience and upscale service. Although fine dining restaurants do not compete directly with QSR, a moderate casual dining restaurant could be a competitor. It is pertinent to note that while QSRs typically target customers within the age group of 16-35 years, a casual dining restaurant would target people across age groups. QSRs are able to compete with casual dining restaurants on the basis of factors such as consistency in quality and speed of delivery. CRISIL Research's definition of QSR does not include coffee chains such as CCD, Barista, etc.

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