Research

Deadly bite

Covid-19 to devour half of dine-in revenues this fiscal

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Heartburn getting worse

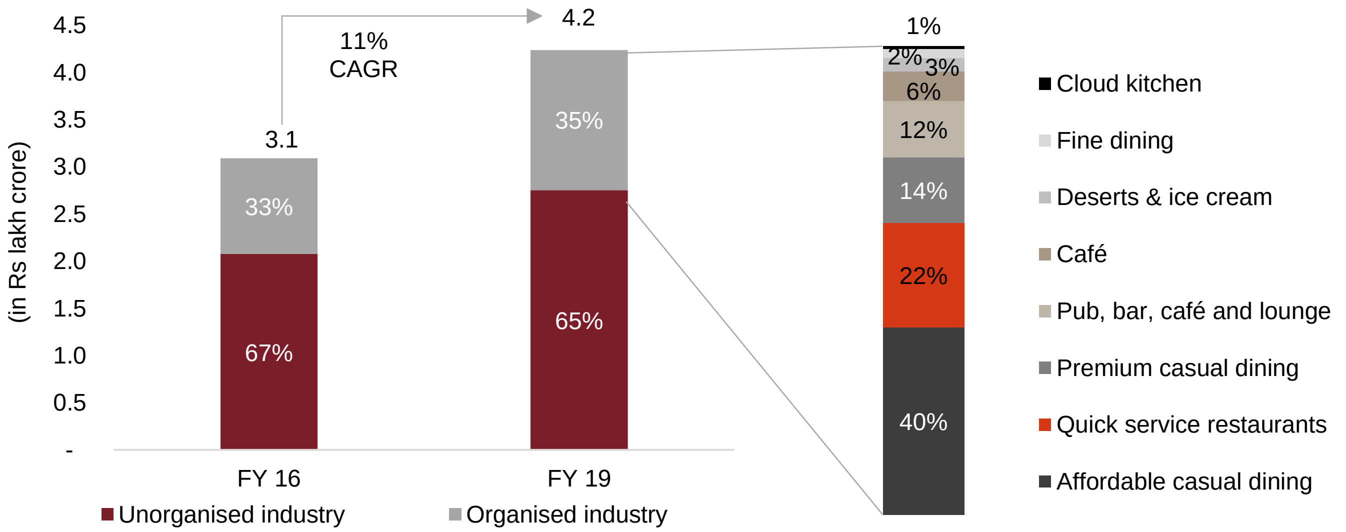
The Rs 1.5 lakh crore organised restaurant business will take at least a year after the lockdown is lifted to recover from the Covid-19 pandemic, a CRISIL Research estimate shows.

That's because, diners are unlikely to get back to relishing their favourite Paneer Tikka Masala or Tsing Hoi Chicken or Neapolitan Lasagna at a restaurant in a hurry after the lockdown is lifted.

Consequently, the organised dine-in segment's revenue may be chopped 40-50% this fiscal.

The reasons for the heartburn aren't difficult to fathom. For starters, dine-in and public entertainment venues in cities such as Mumbai, Delhi National Capital Region (NCR) and Bengaluru have been shut since March 13-14, before the nationwide lockdown came into effect on March 25.

India's restaurant industry as of fiscal 2019



Source: Industry sources, CRISIL Research

The online delivery option is only available in a few cities and that too at low service levels. While Mumbai, Delhi NCR, Bengaluru, Kolkata, Pune and Bhubaneswar have operational online deliveries, these are not available in Hyderabad, Ahmedabad, Visakhapatnam, Indore and Lucknow because of safety guidelines and restrictions by state bodies, unavailability of workforce and non-operational kitchens.

According to industry interactions, only 20% of the restaurants listed on online delivery platforms – including casual dining, quick service restaurants and cloud kitchens – are open for delivery currently. And these are operating at just 40% of normal sales volumes.

The total organised restaurant sector volume has dipped 90% during the lockdown.

What's worse, service pick-up is expected to be slow and delayed, especially in the dine-in segment.

Mumbai and Delhi NCR, which account for nearly 50% of the total organised restaurant market, are both in the red zone. As on May 11, the two cities accounted for over 30% of the total Covid-19 cases in the country. Given this, restrictions on public movement and gatherings are likely to be extended; and hence, restrictions on dine-in restaurants will likely continue or operations may be allowed at low service levels.

Online delivery operations in various cities

Cities	Zomato	Swiggy	Cities	Zomato	Swiggy
Delhi NCR	✓	✓	Bhopal	✓	✗
Mumbai	✓	✓	Coimbatore	✓	✓
Kolkata	✓	✓	Nagpur	✓	✓
Chennai	✓	✓	Surat	✓	✓
Hyderabad	✗	✗	Lucknow	✗	✗
Bengaluru	✓	✓	Kochi	✓	✓
Pune	✓	✓	Kozhikode	✓	✓
Ahmedabad	✗	✗	Bhubaneswar	✓	✓
Visakhapatnam	✗	✗	Agra	✗	✗
Indore	✗	✗			

Note: Data as of May 11, 2020. Orange tick indicates10-50 listings, Green tick: Low service level delivery, Red cross: No delivery. Source: App website, CRISIL Research

Suppliers and delivery partners to feel the heat…

The resulting decline in revenue will impact everyone, from horticulture farmers and dairy producers to food processors and from suppliers to logistics and delivery partners.

On the supplier side, we expect unorganised food producers, many of whom have a high exposure to the restaurants sector, to be hit the hardest given that bulk demand will decline sharply over the coming year.

Perishable goods are already witnessing high wastage owing to the fall in institutional demand. Besides, the reduced earnings of horticulture farmers and declining availability of agri-inputs will also impact the next produce cycle.

Delivery partners are also getting scalded. Online orders for restaurants have shrunk 50-70% during the lockdown, though these could improve in the long run with customers refraining from dining out. With their frontline delivery staff facing a high exposure risk, the platforms will have to ensure their safety for business continuity and consumer confidence.

…job losses on the plate, too

Low utilisation levels are likely to prompt the industry to reduce fixed costs through outlet closure, and job and salary cuts.

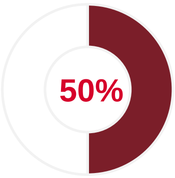
As per our interactions, the organised restaurant business employs ~40 lakh kitchen and restaurant workers.

The dine-in segment accounts for 75% of the business within the organised sector, while online delivery/takeaway accounts for the rest.

With the financial health of restaurants impacted, the spectre of significant job losses appears all too real.

Unpalatable options and revival recipes

Our analysis of the organised dine-in segment's revenue being chopped in nearly half this fiscal takes into account the nationwide restrictions on hospitality and restaurant dine-in facilities across all zones till end of May. It also assumes services will resume sometime in June but only at low service levels since demand for dine-in will be very limited in the first month post-lockdown.



The organised sector in Mumbai and Delhi NCR is nearly 50% of the total organised restaurant market. Both cities are in the red zone.

40-50% Organised dine-in segment's revenue expected to shrink by 40-50% this fiscal#

The decline in revenue is based on the assumption that restaurant services would resume by mid-June 2020, and likely level of clientele after the lockdown ends

CRISIL Research expects restaurants to operate at 25-30% of their monthly service levels during the first 45 days post lifting of the lockdown due to muted demand and social distancing norms. The industry will likely take a year to resume normal service levels.

This will severely impact the financial health of restaurants since it is a risky business with high operating leverage. According to our estimates, fixed costs account for 30-35% of the income in the restaurant business. Given a 40-50% decline in revenue, we estimate profit margin will turn negative at current cost structure.

As a result, the organised restaurant segment will witness heavy losses, closures, salary cuts and layoffs, affecting lakhs of workers.

The impact will be more in the unorganised segment because of higher revenue volatility and limited financial support.

To manage liquidity constraints and cash flows, many restaurants are currently seeking concessions on rental value or deferral of rent payments.

A raft of challenges loom

Decline in revenue	Difficult financing scenario	Imminent fixed-cost reduction	Covid-19: Cost of change
No dine-in means, severe impact on revenue and cash inflows for restaurants Even online / delivery segment is facing the heat.	Business uncertainty, decline in revenues and profits, high fixed cost structure and lower asset ownership for collaterals will make fund-raising tough	Limited source of funds and drastic fall in revenues will spawn cost-cutting measures such as outlet closures, salary cuts and layoffs.	The crisis also demands change in business operations and adoption of new norms post Covid-19 – the cost of this will be added burden

Of the set of companies assessed by CRISIL Research using Quantix, CRISIL's integrated data and analytics platform, nearly 60% of the organised players have a current ratio less than 1.

The restaurant industry typically carries less inventory, resulting in lower current assets. However, with the decline in revenue, meeting the current liabilities through sales will be a burden.

More than 50% of the players in the industry have stressed balance sheets with negative networth or debt equity ratio of more than 2 times. Around 30% of the set analysed also have low interest coverage ratio (ICR), at less than 2 times. With declining revenue and increase in working capital requirements, these players will find it difficult to raise debt from banks.

Even with low gearing, the industry will face issues in raising debt, given revenue volatility, lower or negative profitability, and low asset ownership. Indebted players will be under pressure to shut unprofitable outlets to save cost and raise funds.

Larger ones with low debt may be able to raise money owing to factors such as private investment and promoter support, brand recognition, customer loyalty, and strong market presence. However, even they face high uncertainty in terms of a return to business as usual.

That’s not all. The operational challenges post the lockdown will also lead to changes in the business model. For instance, volumes are likely to dip since customers will turn cautious on discretionary spends. Also, social distancing norms will lead to lower operational levels with fewer tables, reduced working hours and improved ventilation systems.

With consumers emphasising on greater hygiene in both restaurants and the supply chain, cost will increase. Contact-less dining will also need to be facilitated, such as enabling ordering from a customer’s phone instead of a menu card. With the dine-ins facing stiff competition from the delivery segment, restauranteurs will have to retune their strategies since consumers are less likely to queue up for a table.

The industry is undertaking several measures to tide over the crisis and adapt to the new normal. For instance, the dine-in segment is looking at new offerings such as do-it-yourself meal boxes with ingredients and recipes, and focusing on healthy products and safe deliveries. They are also changing menus to suit demand – comfort food, quick and combo meals are fresh additions.

Players are also wooing customers by offering discount vouchers to bolster cash flows during the lockdown.

For now, dine-in remains closed, with the restaurant industry awaiting further guidelines from the government on resuming business. Any extension of the restrictions on dine-in in key regions to June will aggravate the restaurant industry’s woes, and stretch the time to recovery.

Decline in revenue and lower profitability to impact financial health of restaurant industry

RANGE FOR GEARING RATIO (D/E)	BREAK-UP OF INDUSTRY FOR D/E RANGE	SHARE IN TOTAL SAMPLE DEBT
NEGATIVE	20%	30%
0.01 - 0.50	40%	22%
0.51 - 1.00	5%	19%
1.01 - 2.00	12%	9%
2.01 - 5.00	15%	17%
>5.01	8%	4%

RANGE FOR ICR	BREAK-UP OF INDUSTRY FOR ICR RANGE
<=0.0	15%
0.01 – 1.00	3.5%
1.01 – 2.00	11.5%
2.01 – 5.00	39%
>5.01	31%

RANGE FOR CURRENT RATIO	BREAK-UP OF INDUSTRY FOR CURRENT RATIO RANGE
<=0.5	15%
0.01 – 1.00	45%
1.01 – 2.00	30%
>2.01	10%

RANGE FOR DEBT/ PBDIT	BREAK-UP OF INDUSTRY FOR DEBT/ PBDIT RANGE
<=0.0	8%
0.01 – 1.00	20%
1.01 – 2.00	19%
2.01 – 5.00	35%
>5.01	19%

Note: Based on sample set calculations for 25 companies in the organised sector, with total debt of Rs 610 crore for fiscal 2019.

Source: CRISIL Quantix, CRISIL Research

About CRISIL Limited

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