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# Zomato: Out to Deliver


JM Financial Institutional Securities Limited

# Info Edge | BUY

## Zomato: Out to deliver

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**Global food-tech has crossed the peak of inflated expectations in the hype cycle of its evolution. Investments in this space declined 28% in 2016, after reaching a peak of USD 5bn in 2015. India is no different with a 56% drop in investments, resulting in significant consolidation. This should discourage the 'spray-and-pray' strategy of investors, going forward. We view this situation as healthy, as it will allow capital to flow to the stronger scale players. Zomato and Swiggy have emerged as clear leaders in the food ordering space in India. We find Zomato's asset light model (no delivery fleet) more sustainable. Also, Zomato's captive user and restaurant base gives it an edge in food ordering. Valuations of listed players, after correcting for the past two years, have started to inch up again. Zomato's valuation in its previous funding round may now appear optically high in that backdrop. However, its market leadership in a large (USD 15bn) underpenetrated Indian food delivery market justifies the premium valuations, in our view.**

- **Global food-tech—past the inflection point:** Online food and grocery is the largest e-commerce category globally with a c.USD 350bn market size. It is also the least penetrated segment (>5% in the US). This has spawned 4,700+ food-tech start-ups globally. Food ordering, with 69% funding share has emerged as the largest segment. This has helped expand the food delivery market—share of online food ordering globally has grown from 8% in 2011 to 30%+ in 2016, as per McKinsey. However, the initial frenzy appears to have subsided, reflected in the 28% decline in food-tech investments in 2016. Early entrants (Just Eat in UK) that have gained scale are consolidating market share. Higher stickiness of customers (c.80% customer retention in food tech) is also benefiting incumbents.
- **Indian perspective—taking a leaf from global peers:** Evolution of food-tech in India is closely following the footsteps of global peers. Restaurant discovery platform (e.g., Zomato) is the dominant segment and has preceded the recent emergence of food ordering (Zomato order, Swiggy). Online penetration is also low. Industry estimates peg the current GMV of online food ordering in India at USD 300mn versus a potential size of USD 15bn. Favourable demography and rising smartphone penetration are the obvious drivers. Not surprisingly, India has seen 1,000+ start-ups in the food ordering space alone. However, India has also witnessed consolidation recently with weaker players closing down or getting acquired. This slowed down PE funding in the space as well (-56% in 2016), in line with global trends. We believe the consolidation is healthy for the segment and should restore rationality, after the discount-led share gain strategy.
- **We prefer Zomato over Swiggy:** India's food tech market has turned into a two-player race—Zomato versus Swiggy. Zomato's leadership in the restaurant listing space allows it to control both demand (80mn unique users) and supply—40% restaurants on its platform are exclusive. This is already reflecting in numbers. Zomato's food ordering revenues grew 7x in FY17 with monthly order volume reaching 2.1mn. While Swiggy's delivery has helped it improve customer experience and gain share, we prefer Zomato's strategy of relying on third-party delivery. Our checks suggest unit economics in own delivery is neither favourable nor is likely to improve with scale. Zomato's asset light model is more geared towards scale benefits and hence more sustainable, in our view.

| Recommendation and Price Target | |
|---|---|
| Current Reco. | BUY |
| Previous Reco. | NR |
| Current Price Target (12M) | 1,010 |
| Upside/(Downside) | 17.3% |
| Previous Price Target | 1,010 |
| Change | 0.0% |

| Key Data – INFOE IN | |
|---|---|
| Current Market Price | INR 861 |
| Market cap (bn) | INR 104.4/US$1.6 |
| Free Float | 52% |
| Shares in issue (mn) | 116.9 |
| Diluted share (mn) | 120.9 |
| 3-mon avg daily val (mn) | INR 75.2/US$0.1 |
| 52-week range | 1,025/731 |
| Sensex/Nifty | 30,583/9,512 |
| INR/US$ | 64.1 |

| Price Performance | | | |
|---|---|---|---|
| % | 1M | 6M | 12M |
| Absolute | 2.4 | -2.7 | 15.7 |
| Relative* | -1.4 | -16.3 | -2.9 |

* To the BSE Sensex

| Financial Summary | | | | | (INR mn) |
|---|---|---|---|---|---|
| Y/E March | FY15A | FY16A | FY17E | FY18E | FY19E |
| Net Sales | 6,113 | 7,235 | 8,284 | 9,729 | 11,722 |
| Sales Growth (%) | 20.8 | 18.3 | 14.5 | 17.4 | 20.5 |
| EBITDA | 1,814 | 1,580 | 2,635 | 3,129 | 3,702 |
| EBITDA Margin (%) | 29.7 | 21.8 | 31.8 | 32.2 | 31.6 |
| Adjusted Net Profit | 1,939 | 1,416 | 2,677 | 2,629 | 3,065 |
| Diluted EPS (Rs.) | 16.1 | 11.7 | 22.1 | 21.7 | 25.3 |
| Diluted EPS Growth (%) | 37.1 | -27.4 | 89.1 | -1.8 | 16.6 |
| ROIC (%) | 0.0 | 147.4 | 114.9 | 147.5 | 174.0 |
| ROE (%) | 16.0 | 8.3 | 14.3 | 12.6 | 13.3 |
| P/E (x) | 53.4 | 73.5 | 38.9 | 39.6 | 34.0 |
| P/B (x) | 6.1 | 5.9 | 5.3 | 4.8 | 4.3 |
| EV/EBITDA (x) | 48.9 | 57.5 | 34.1 | 28.0 | 23.1 |
| Dividend Yield (%) | 0.3 | 0.3 | 0.5 | 0.5 | 0.5 |

Source: Company data, JM Financial. Note: Valuations as of 16/May/2017

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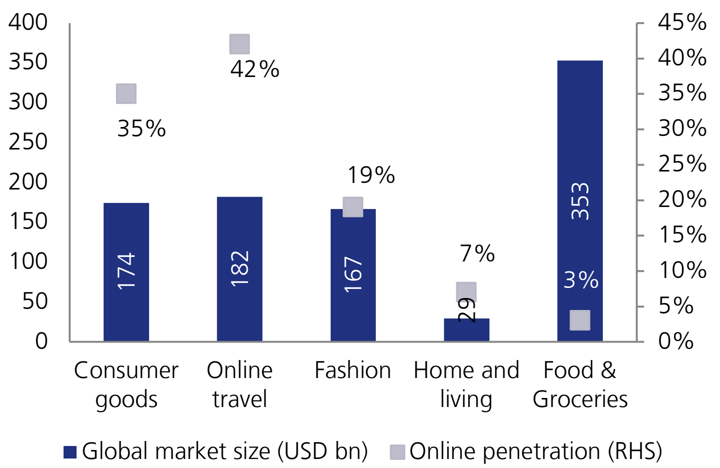
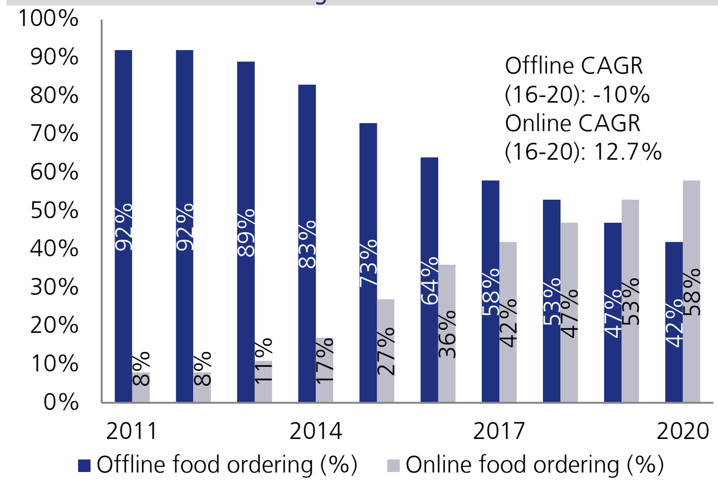
# Focus Charts

Exhibit 1. eCommerce segments: Size and penetration



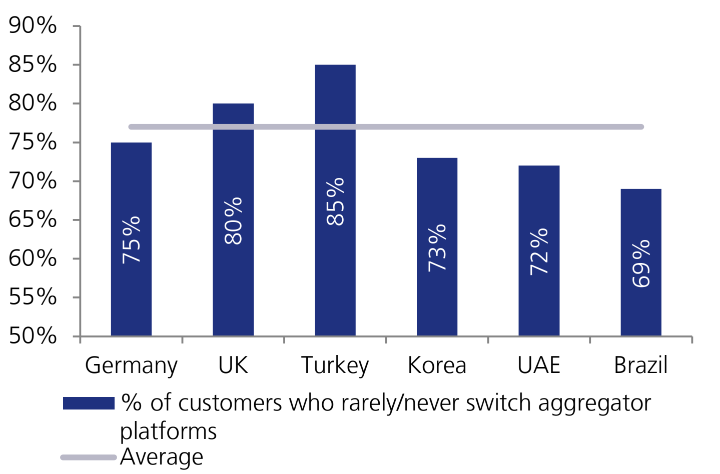

Source: Media Reports, JM Financial

Exhibit 2. Global food ordering trend



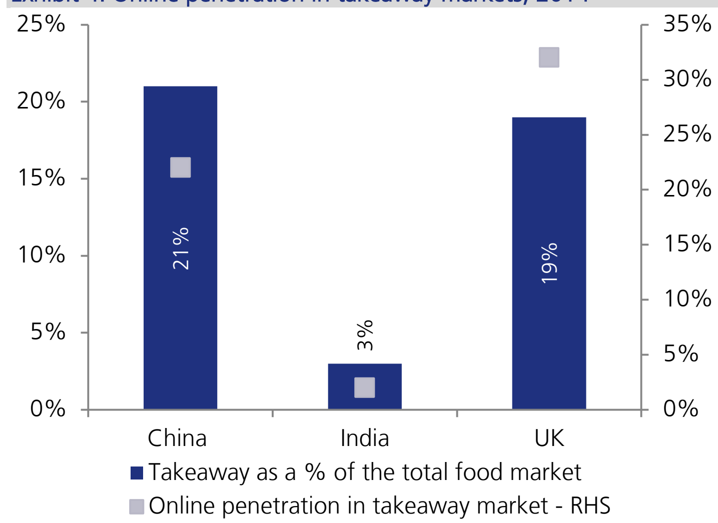

Source: McKinsey, JM Financial

Exhibit 3. Customer retention rate in select countries



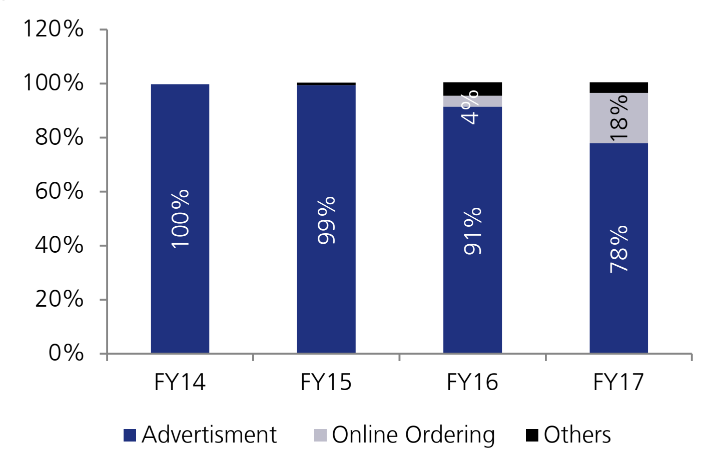

Source: McKinsey, JM Financial

Exhibit 4. Online penetration in takeaway markets, 2014




Source: Euromonitor, JM Financial

Exhibit 5. Revenue distribution by services: Zomato




Source: Company, JM Financial

Exhibit 6. Google trends: Leading food-tech players

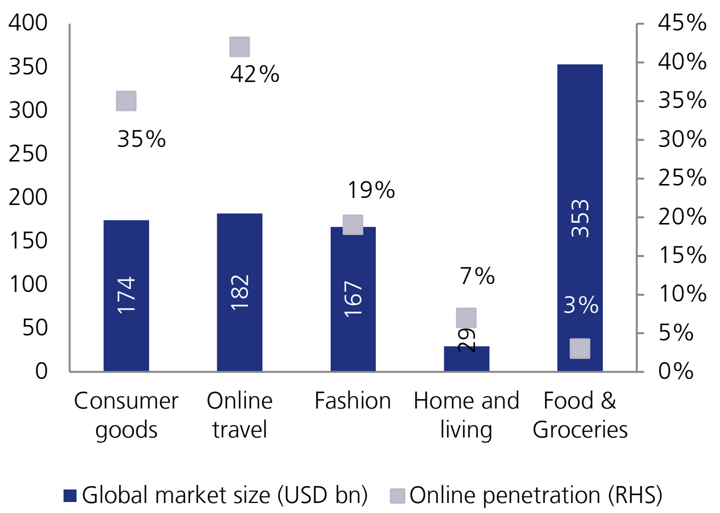

Source: Google Trends, JM Financial

# Lessons from international markets

### Online ordering and delivery: Past the inflection point

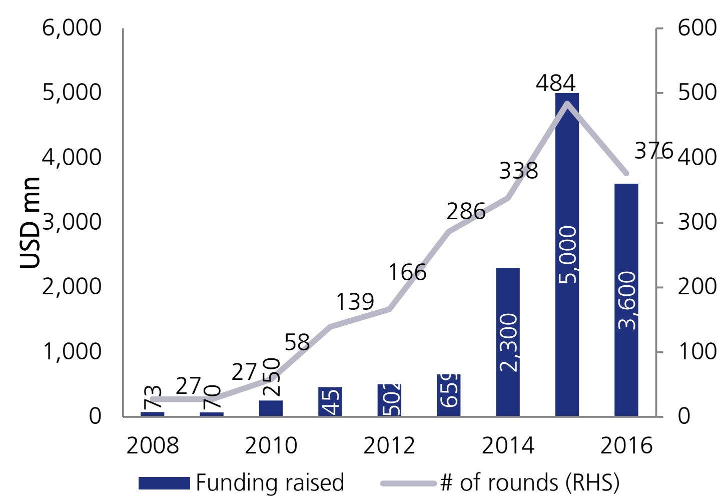
Online food and grocery is a c.USD 350bn market, the largest e-commerce category globally. Food consumption also remains predominantly offline with less than 5% online penetration in the US. Not surprisingly, the food-tech space caught the investors' attention a few years ago. This has spawned 4,700+ food-tech start-ups globally. While food restaurant discovery platforms have existed for over a decade, the recent investments were made largely in the food ordering segment. Over 2,700 food ordering start-ups have been launched, attracting c.USD 9bn of PE funding (c.70% of overall funding in food-tech). This is not only expanding the overall market, but also accelerating the shift from offline to online ordering. Mckinsey, a global consulting firm, estimates that the share of online orders in the global food delivery market increased from 8% in 2011 to 42% in 2016 (Exhibit 11). Even for Dominos (UK), which pioneered the offline food ordering, the share of online ordering has increased 30 percentage points, implying the recent nature of this shift (Exhibit 12).

Exhibit 7. A large and underpenetrated online food market…




Source: Media reports, JM Financial

Exhibit 8. …has attracted significant PE investments in this space

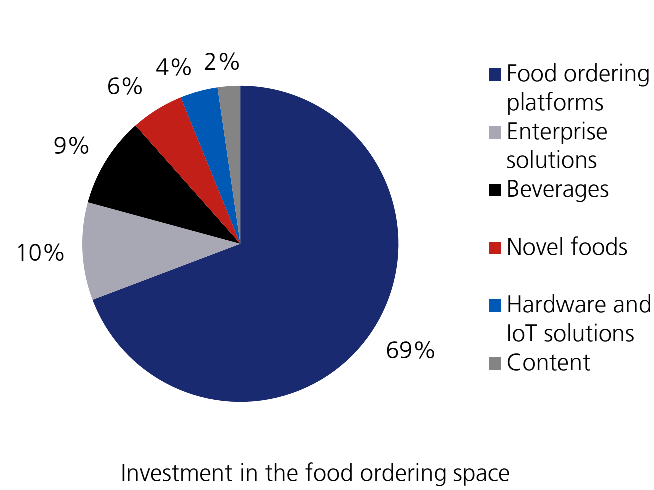



Source: Tracxn, JM Financial

However, the rush to launch and fund another food-tech upstart has abated. After peaking in 2015, the number of seed investments in food-tech declined 25% in 2016. This has been fuelled by high failure rate. For instance, of the c.4,700 food-tech companies founded, less than 2% have survived till the late stage of funding.

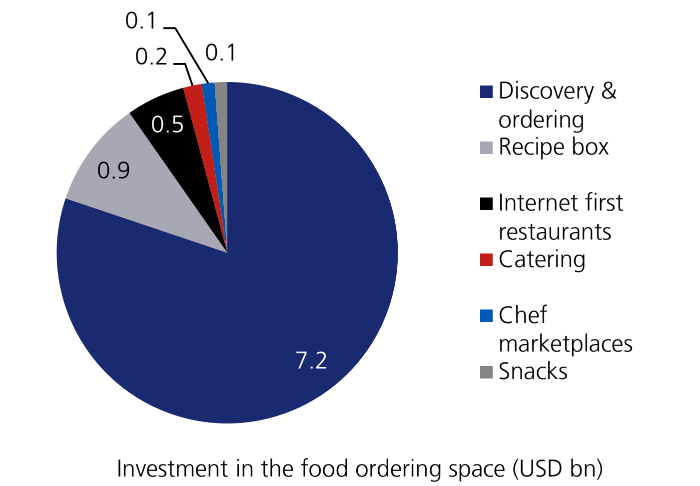
We believe consolidation in the industry is welcome, as it will weed out me-too and irrational players without a sustainable business model. It also means that more funds will be available for stronger players. This will likely create a virtuous cycle for the larger established players, further increasing the gap with weaker ones.

### Exhibit 9. Food ordering has attracted highest investor funding …



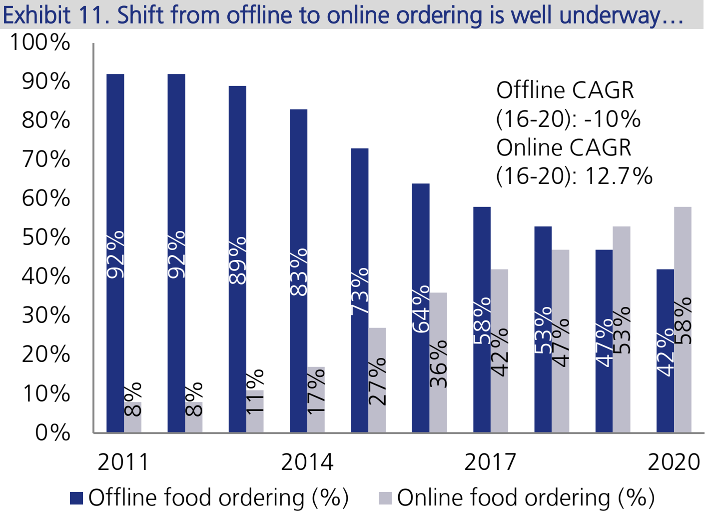

Source: Tracxn, JM Financial

### Exhibit 10. …with restaurant aggregators getting the highest share



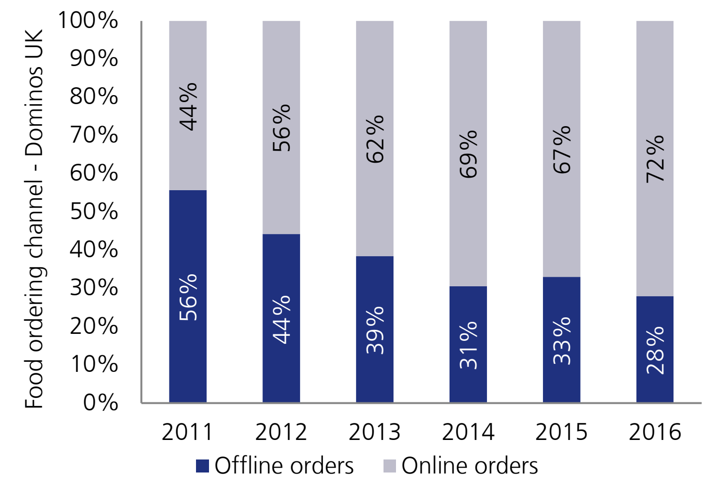

Source: Tracxn, JM Financial

### Exhibit 11. Shift from offline to online ordering is well underway…




Source: Mckinsey, JM Financial

### Exhibit 12. …reflected in Domino's shrinking offline order share




Source: Company, JM Financial

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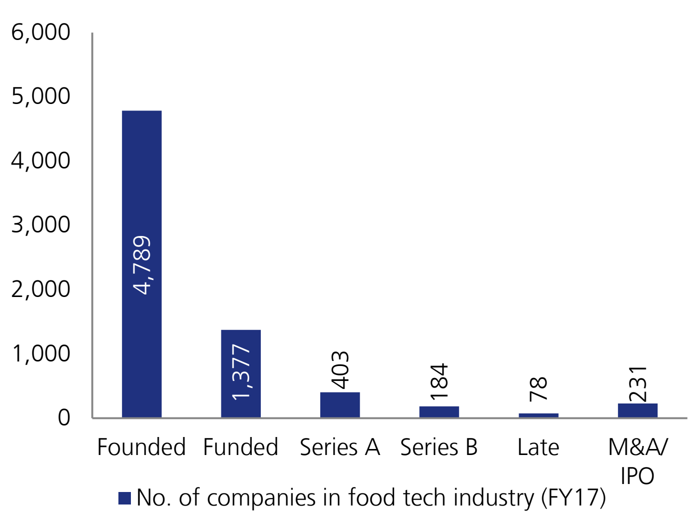
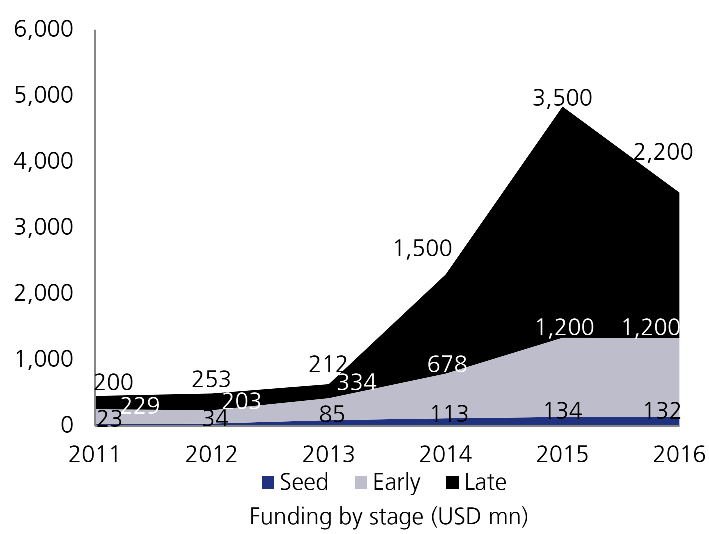



Source: Tracxn, JM Financial

### Exhibit 14. …now appears to have abated



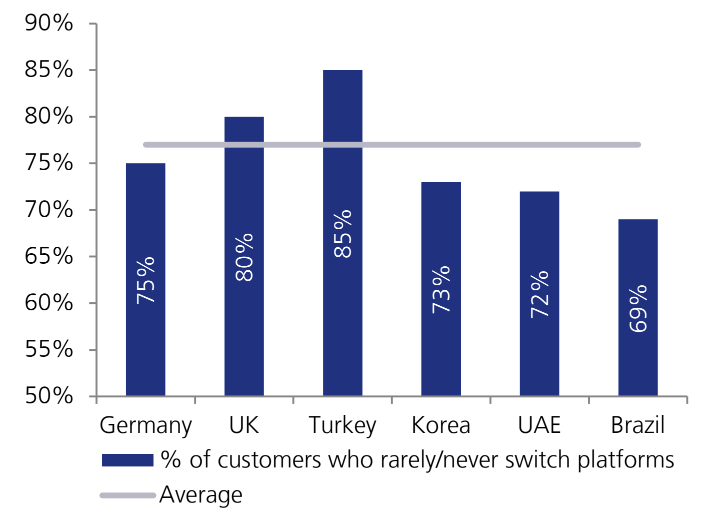

Source: Tracxn, JM Financial

### Advantage incumbents: Networking effect and consumer stickiness at play

Like any other internet platform, online food delivery platforms also exhibit the networking effect—more the number of restaurants on the platform, more users it attracts. In addition, user retention rates tend to be high in the online food segment. McKinsey estimates that around 80% of customers, who sign-up, rarely or never leave for another platform (Exhibit 15). This not only puts the early entrants at a vantage position, but reduces the customer retention cost for these players as well. For example, Just Eat, one of the early entrants in the UK food market (2001) still remains the dominant player in the country. While ruling out the threat of a new entrant would be remiss, these factors do raise the entry barriers for newer players.

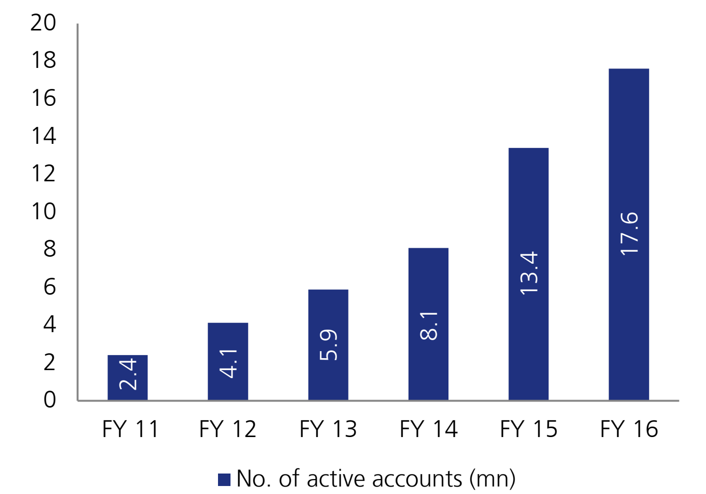
Around 80% of the customers, who sign-up for a platform, never or rarely switch for another

Exhibit 15. High retention rate gives advantage to the early entrants and leaders in the segment




Source: McKinsey, JM Financial

Exhibit 16. Early start by Just Eat has helped it retain the market leadership in the UK market



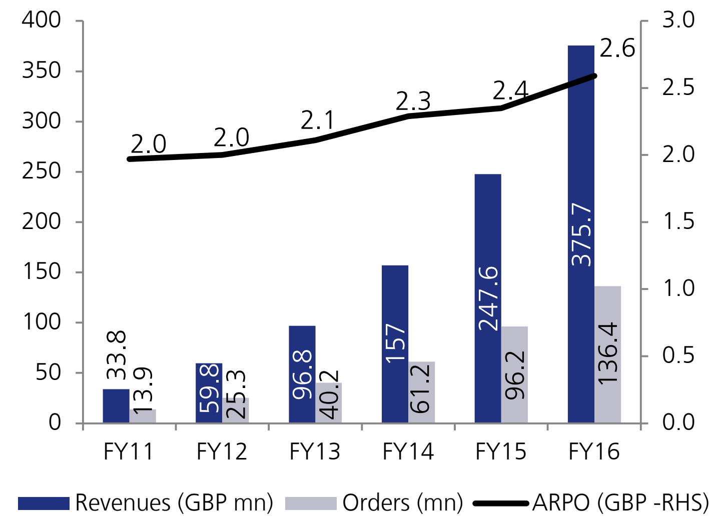

Source: Just Eat, JM Financial

### Scale key to survive even though hyper local nature of delivery restricts scale benefits

Hyper local nature of food delivery limits the economies of scale, especially for players involved in delivery themselves. While we believe unit economics for delivery may not improve proportionately with the scale, larger players are able to leverage their high volumes for a greater commission. Thus, they have been able to increase the average revenue per order (Exhibits 17 and 18). Also, scale allows other operating costs such as technology costs to be spread over a larger base. However, the benefits of scale are more visible for players, who do not deliver themselves. For instance, GrubHub, due to its recent acquisitions of food-delivery players, now delivers c.15% of the orders itself. Hence, GrubHub's reduction of other operating expenses with scale has been offset by rising delivery and operation costs (Exhibit 20). Just Eat - which has largely grown organically - on the other hand delivers only c.2% of its orders. Given the almost zero marginal cost of customer acquisitions for such a model, Just Eat's operating expenses as a percentage of revenue has dropped from c.80% in 2013 to c.66% in 2016 (Exhibit 19).

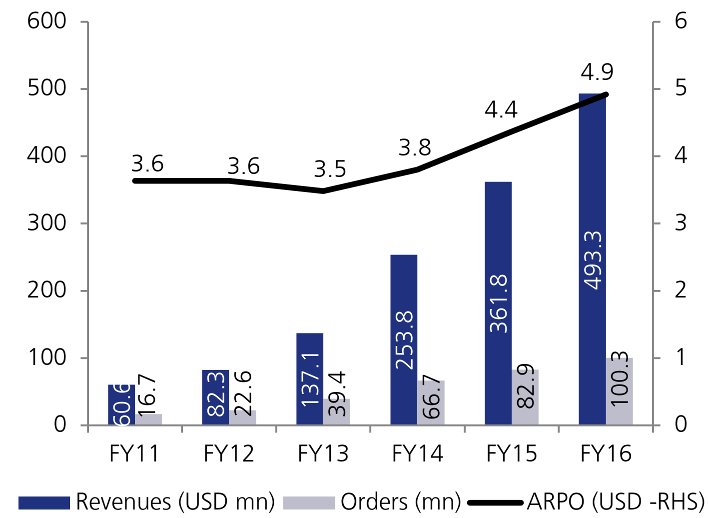
Just Eat delivers only c.2% of its orders itself versus 15% for GrubHub. This translates into relatively lower scale benefits for GrubHub

Exhibit 17. Scale helps players negotiate better takeaway rates…



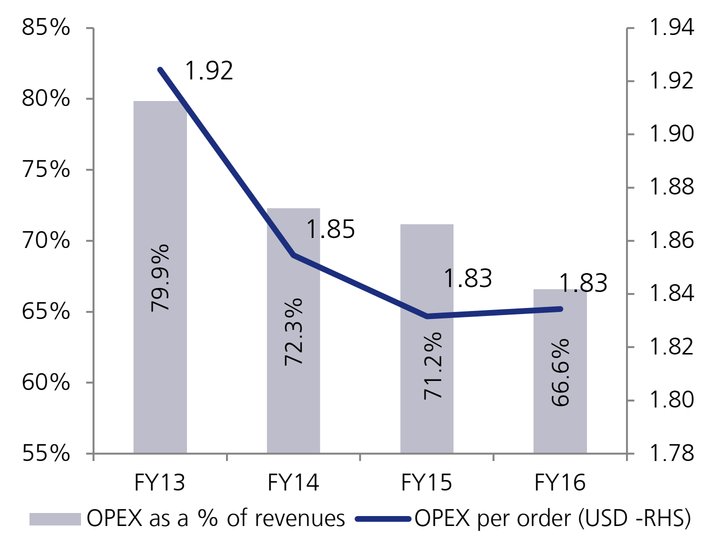

Note: KPIs for Just Eat; Source: Just Eat, JM Financial

Exhibit 18. …with restaurants as they bring higher orders for them



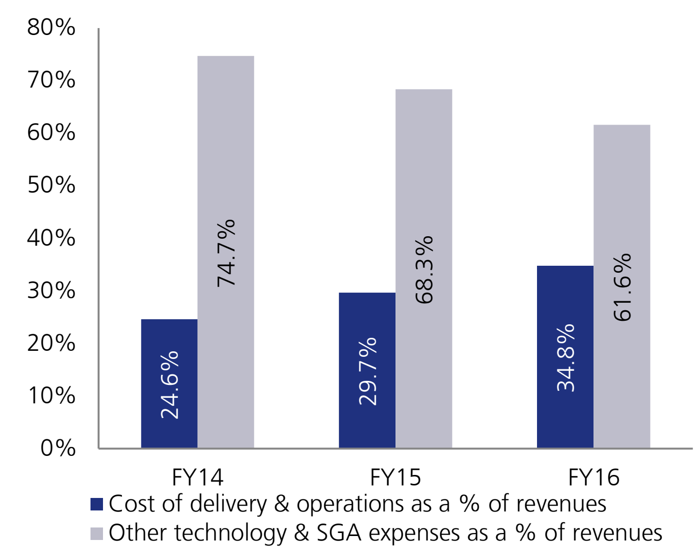

Note: KPIs for GrubHub; Source: GrubHub, JM Financial

Exhibit 19. Scale benefits for Just Eat are more visible…




Source: Just Eat, JM Financial

Exhibit 20. …vis-à-vis GrubHub due to absence of delivery cost




Source: GrubHub, JM Financial

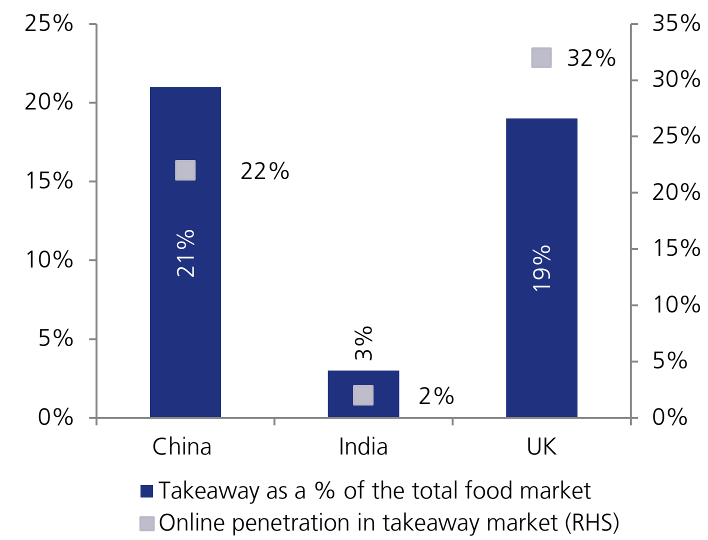
# Indian food tech: Taking a leaf from global peers

## Ingredients for growth in place

India's potential food ordering market is c.50x of the current GMV

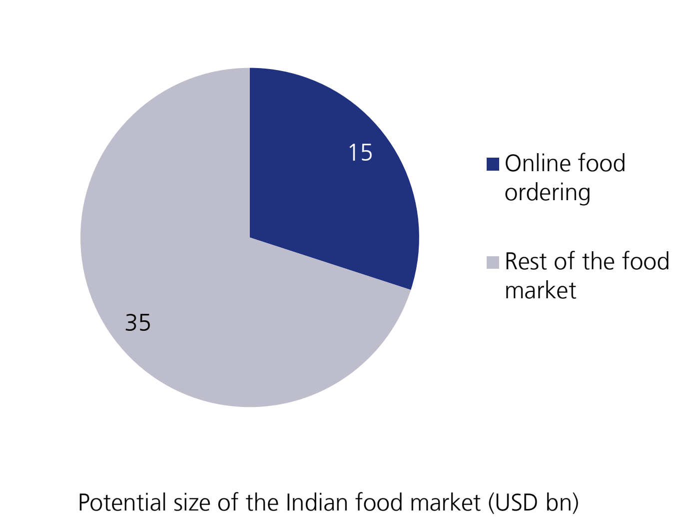
Evolution of food-tech in India is closely following the footsteps of global peers. Restaurant discovery platform (e.g., Zomato) is the dominant segment and has preceded the recent emergence of food ordering (Zomato order, Swiggy). The online penetration is also low. Gross merchandise value (GMV) of India's online food delivery market is estimated to be USD 300mn for 2016, growing at more than 100% annually. Industry estimates peg the potential online food ordering market at USD 15bn (50x of current size), implying significant headroom for growth (Exhibit 22). The wide difference in the current and potential market opportunity also indicates that shift from offline to online food ordering in India is significantly behind other developed markets. As per Euromonitor, a market research firm, out of India's total restaurant and delivery market, takeaway share was a mere 3% compared to China's 21% and the UK's 19%. Furthermore, the online share in the takeaway market is only 2% versus China's 22% and the UK's 32% (Exhibit 21). Not surprisingly, India has seen the highest number of food ordering start-ups globally (Exhibit 23).

Exhibit 21. Online penetration in takeaway markets



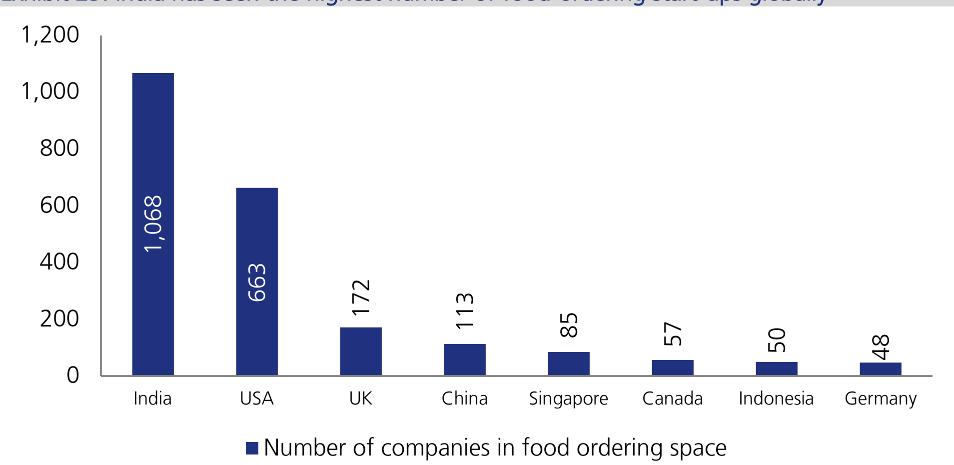

Source: Euromonitor, JM Financial

Exhibit 22. Breakup of estimated total food market in India




Source: IBEF, JM Financial

Exhibit 23. India has seen the highest number of food-ordering start-ups globally



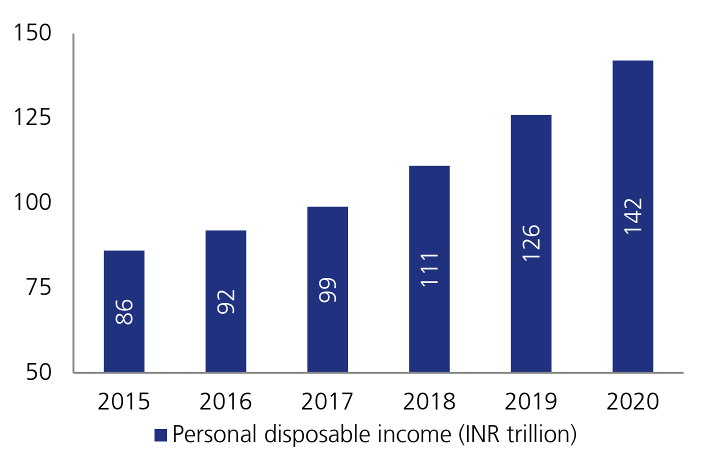

Source: Tracxn, JM Financial

Unlike developed markets, where the online shift is the key driver, we believe India's food-tech market will be driven by: a) an increase in the food takeaway market itself; and b) the shift from offline to online ordering.

### a) Increase in food-takeaway (or prepared food) market

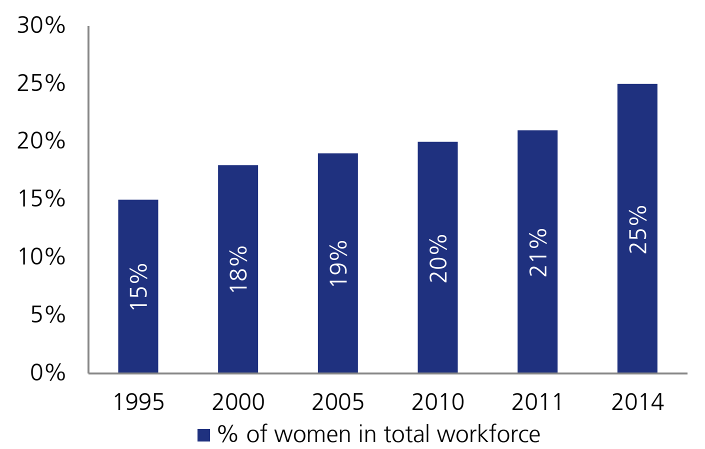
Among the major economies, the percentage of people eating out in India is one of the least (Exhibit 21). We believe this is likely to change as rising disposable income and increasing participation of women in the workforce will increase the preference for prepared meals (Exhibits 24 and 25). This will also be supported by urbanisation, a young working population (median age in India is 27 years) and more number of nuclear families.

Exhibit 24. Rising disposable income coupled with…



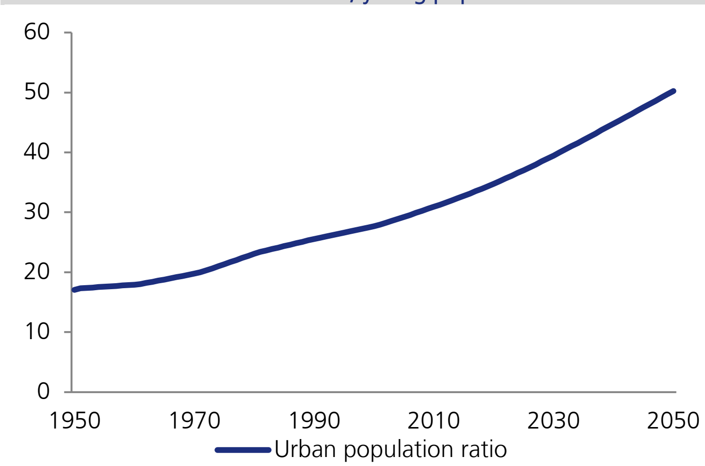

Source: KPMG, JM Financial

Exhibit 25. …higher working women to help food takeaway market



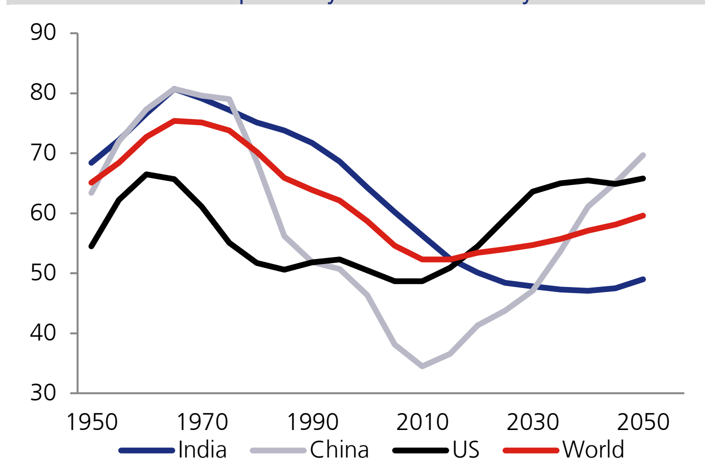

Source: KPMG, JM Financial

Exhibit 26. Increased urbanisation, young population and …




Source: United Nations, JM Financial

Exhibit 27. …lower dependency ratio are other key factors

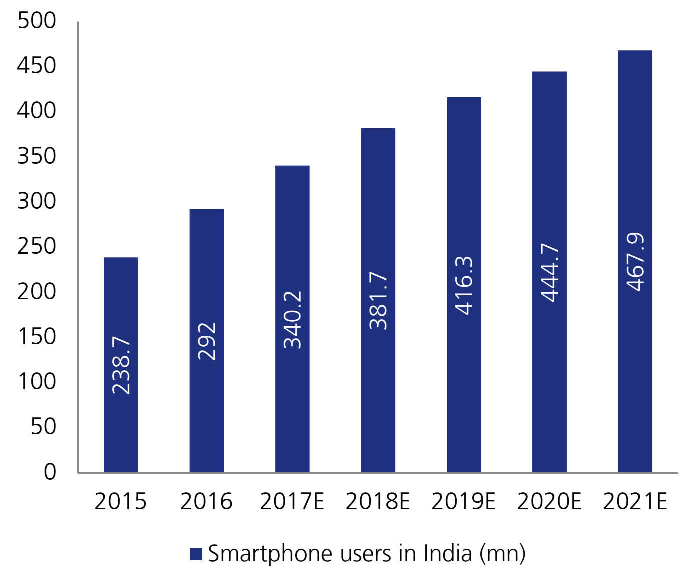



Note: dependency ratio: (<15 & 65+)/(15-64); Source: United Nations, JM Financial

### b) Shift to online ordering

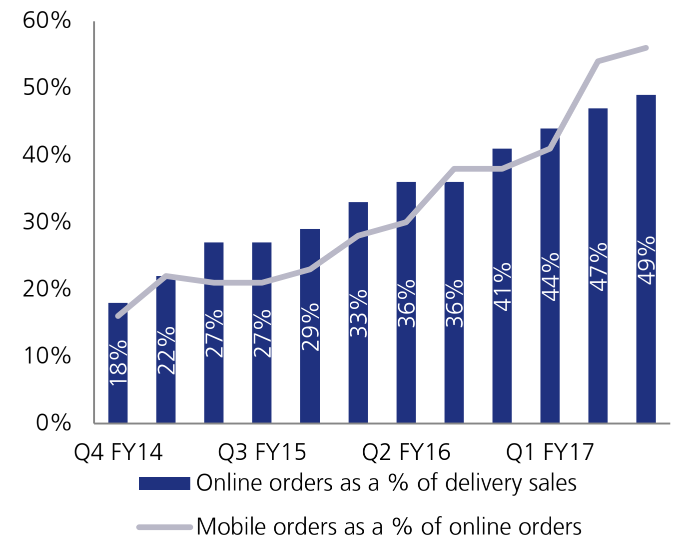
We believe India is likely to leapfrog the offline food ordering stage. A young more technology savvy population has coincided with the onset of smartphones and emergence of food delivery players. This is reflected in Dominos India's rising proportion of online orders; the company's percentage of online delivery order has surged from c.18% in Q4FY14 to nearly 50% in Q3FY17 (Exhibit 29), driven largely by mobile orders.

Exhibit 28. India's smartphone generation should help leapfrog…




Source: Media Reports, JM Financial

Exhibit 29. …the offline food ordering stage, which is already reflecting in Dominos' order trends

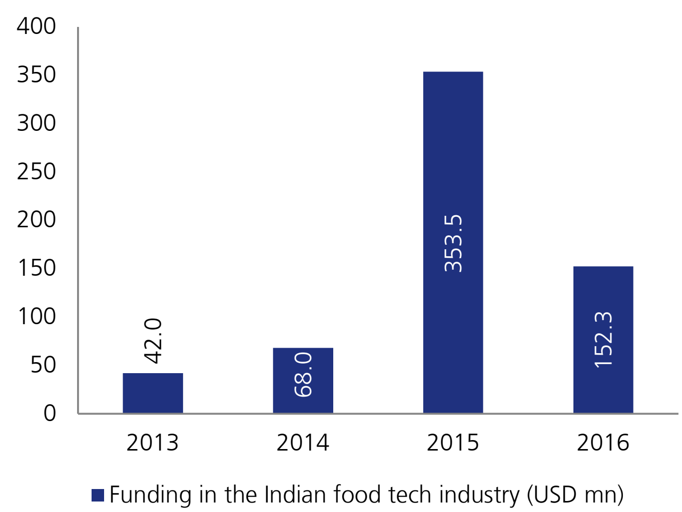



Source: Company, JM Financial

### Competitive landscape—turning into a two-player market

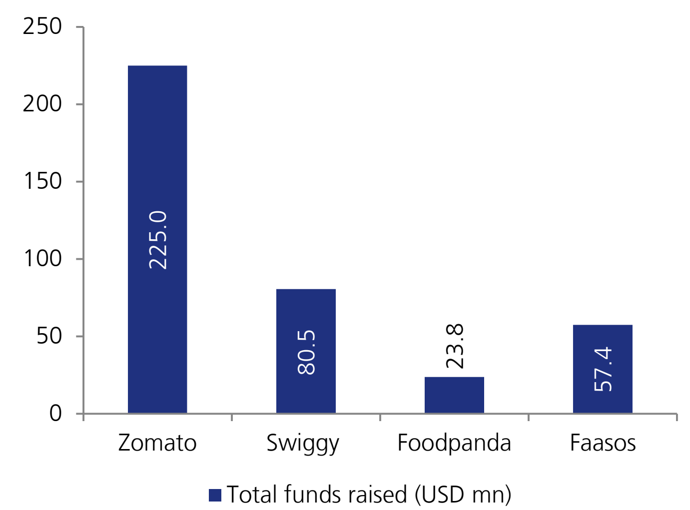
Like its global counterparts, investment in India's food-tech market also peaked out in 2015. 2016 saw a 56% drop in total investments in India's food-tech space prompting the much-needed consolidation (Exhibit 32). Like other eCommerce segments in India—e.g., cab hailing (Uber and Ola), eCommerce (Amazon and Flipkart)—food ordering is also turning out to be a two-player market. Zomato and Swiggy have emerged out to be the two-leading players in the Indian food ordering space. Also, food ordering happens to be a city-wise market than national. Our channel checks suggest that Zomato is a clear leader in major cities such as Mumbai and New Delhi whereas Swiggy is the market leader in Hyderabad and Bengaluru.

Exhibit 30. Funding in food-tech in India declined 56% YoY in 2016




Source: Media reports, JM Financial

Exhibit 31. Zomato and Swiggy have received the highest funding



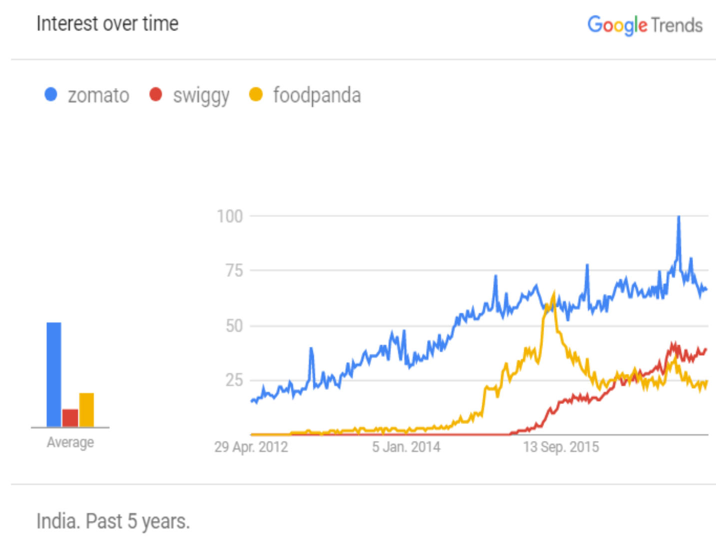

Source: Companies, Media reports, JM Financial

### Exhibit 32. India food-tech market has also seen consolidation…

| Start-up | Launched In | Acquired By |
|---|---|---|
| Foodpanda | 2012 | DeliveryHero |
| Drink King | 2015 | GrowFit |
| FYNE Superfood | 2014 | Sattviko |
| Tinyowl | 2014 | Roadrunnr |
| Sangeetha Aahar | 2012 | Jiyo Natural |
| EatOnGo | 2015 | InnerChef |
| FlavorLabs | 2014 | InnerChef |
| Place of Origin | Unknown | Craftsvilla |
| The First Meal | Unknown | Hello Curry |

Source: Inc42, JM Financial

### Exhibit 33. …precipitated by the fall of Foodpanda

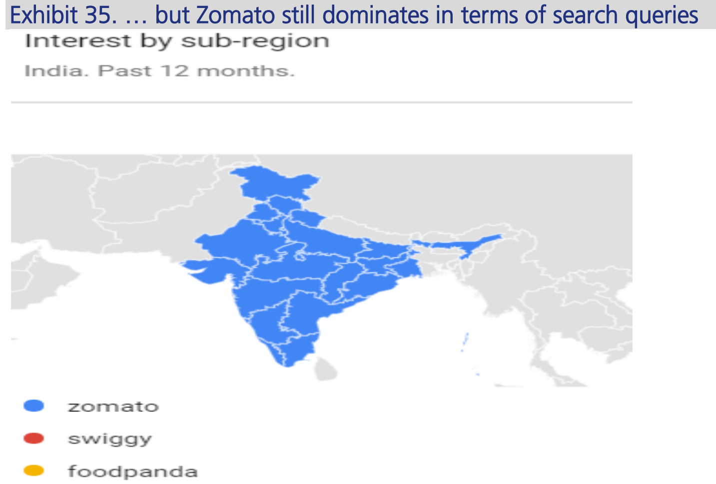



Source: Google Trends, JM Financial

### Exhibit 34. Swiggy is gradually closing the gap with Zomato…

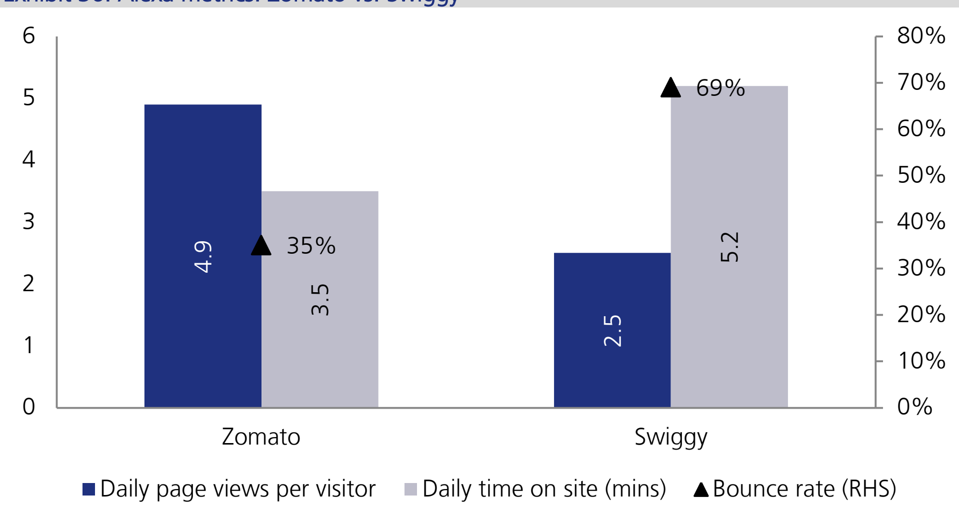

Source: Google Trends, JM Financial

### Exhibit 35. … but Zomato still dominates in terms of search queries




Source: Google Trends, JM Financial

### Exhibit 36. Alexa metrics: Zomato vs. Swiggy




Note: Data as of April'17; Source: Alexa, JM Financial

Swiggy's relatively better user experience has been reflected in increased time spent on its platform compared to Zomato

## Food delivery: Which model is better?

Unlike other segments, however, the two leading players—Zomato and Swiggy—have distinctly different business models. While Swiggy controls the entire logistics of food delivery, Zomato depends on restaurant and third-party logistics players.

"…there isn't any food delivery company in the world, which owns its last mile logistics fleet, operates at scale, and is profitable" Deepinder Goyal, Zomato

While we admit that controlling logistics allows one to manage the customer experience, we are not convinced about the economic viability of this model. Exhibit 37 compares the unit economics of three prevalent models in the market: a) delivery by restaurant (used largely by aggregators such as Zomato); b) delivery by third-party logistics players such as Grab; and c) own delivery fleet (used by Swiggy). Note that the own-delivery economics is for Mumbai and is based on our channel checks/market survey. The average delivery cost/order in Mumbai is approximately INR 100. That implies that even for a higher take rate of 12%, the average order value for the company to break-even at contribution margin level should be INR 833. The average order value for most players in India is currently less than INR 500.

As we have seen in case of GrubHub, scale does not necessarily benefit the logistics cost for food delivery players because of its hyper-local nature. We, therefore, believe Zomato's strategy of outsourcing logistics is more sustainable, even if it comes at the cost of a marginally lower customer experience.

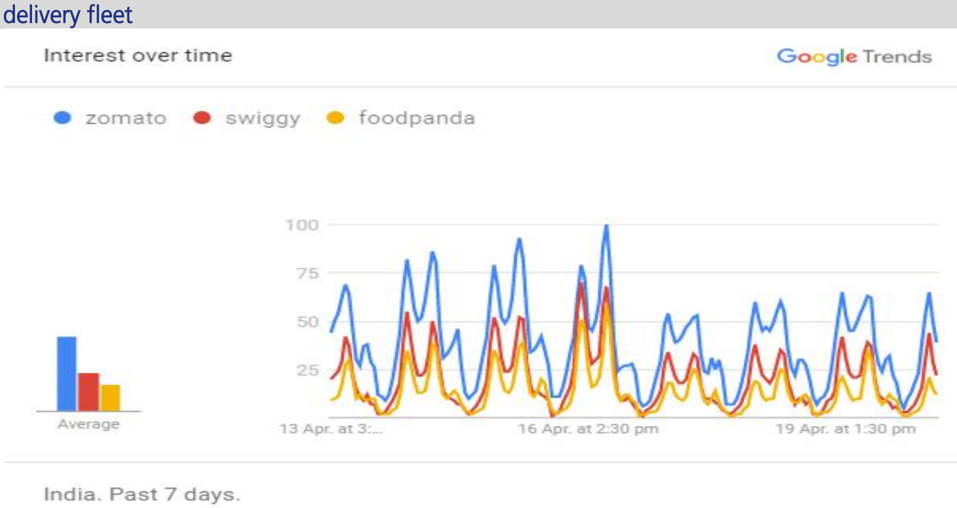
Exhibit 37. Unit economics of food-tech players

| | Restaurants delivers for Zomato | Zomato's delivery partners deliver | Own-delivery fleet - unit economics |
|---|---|---|---|
| | Type A (i) | Type A (ii) | Type B |
| Average order value (AOV) | 480 | 375 | 500 |
| Take rate (Commission) | 8.2% | 8.2% | 12% |
| Delivery fee | NA | 10% | NA |
| Gross revenue | 39.4 | 68.3 | 60 |
| Delivery cost | NA | NA | 100 |
| Delivery fee paid to partners | 0 | 50 | NA |
| Processing/support/operations cost | 18.4 | 27.4 | NA |
| Net contribution per order | 21.0 | -9.2 | -40.0 |

Source: Company, JM Financial

We estimate that for the own-delivery fleet model, average order value required to break-even in Mumbai would be INR 833. Also note that AOV for Swiggy pan-India is roughly around INR 250

Exhibit 38. Uneven order trends across the day and week makes it difficult to optimize own delivery fleet




Source: Google trends, JM Financial

Orders usually peak during the lunch and dinner time on weekdays and surge over the weekend. A variable delivery staff and cost is therefore best suitable to handle such large variations in the order.

# Zomato

### Sensing and seizing opportunities: Online food ordering

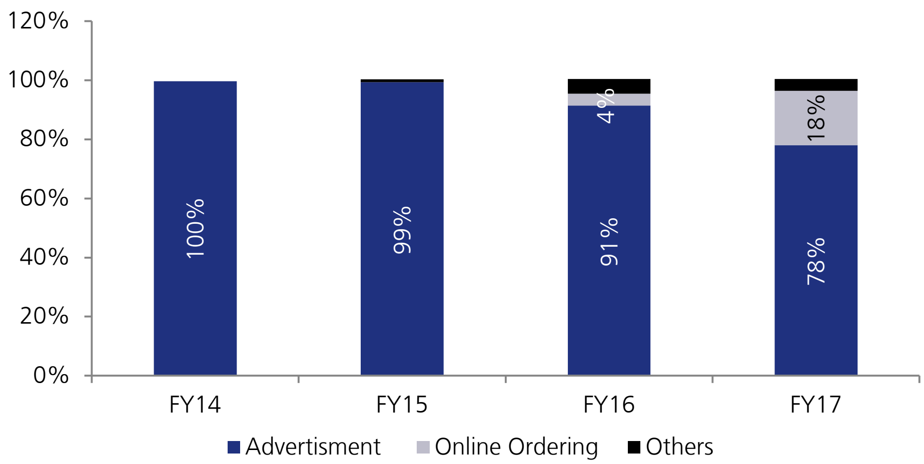
Only 2% of Zomato's unique monthly users order currently

Zomato entered the food delivery market only in 2015. However, Zomato's leadership as a restaurant aggregator gives it a unique advantage over competitors even in the ordering space. As per the company, it has c.10x the traffic compared to all competitors put together. The fact that only 2% of its monthly unique users order online gives it a large under-penetrated captive user base to leverage on. Also, being early into this space, the platform was able to get on board many restaurants with an exclusivity clause. About 40% of the restaurants listed on Zomato are exclusive to it.

Of the total restaurants on Zomato's platform, 40% are exclusive to it

This has already started to reflect in numbers. Despite a late start, Zomato's food ordering revenues grew 7x in 2017 to USD 9mn. The company has already reached a monthly order volume run-rate of 2.1mn by Mar'17.

Exhibit 39. Food ordering contributed 36% of Zomato's FY17's incremental revenues




Source: Company, JM Financial

### The journey north: Scalability pertinent

Zomato's model is geared to take advantage of economies of scale

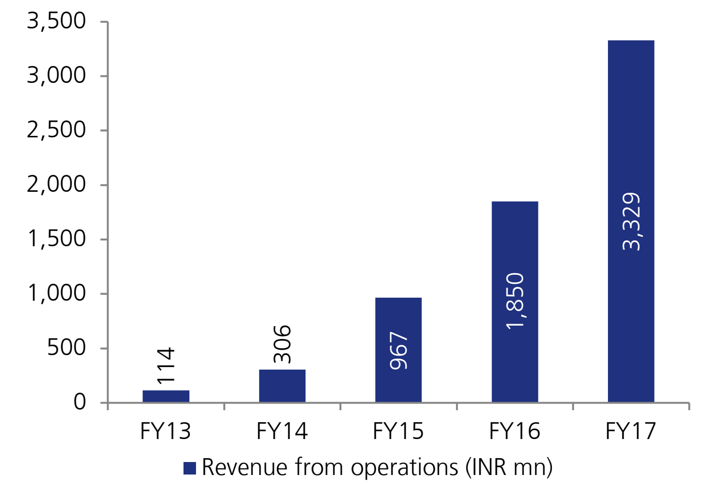
Unlike players, who own logistics of food delivery, Zomato's asset light model is more geared to take advantages of economies of scale. In our opinion, the benefits of scale have started to set in for Zomato. The company was able to drive its revenues consistently over the years, despite its reduction in sales promotion overheads (Exhibit 40).

We also believe that as the number of orders through platforms grows, Zomato could negotiate a higher takeaway margin from restaurants. Restaurateurs would be more likely to do so, as these platforms drive a larger portion of their revenue. For instance, close to 60% (75% in some cases) of the delivery revenues of some of the restaurants are driven by Zomato. The above hypothesis was also validated, when one of the respondents in our market survey revealed that the platform increased its commission margins as the number of orders through them surged.

Info-edge backed platform reported an 80% growth in revenues, despite an 81% decrease in cash burn for FY17

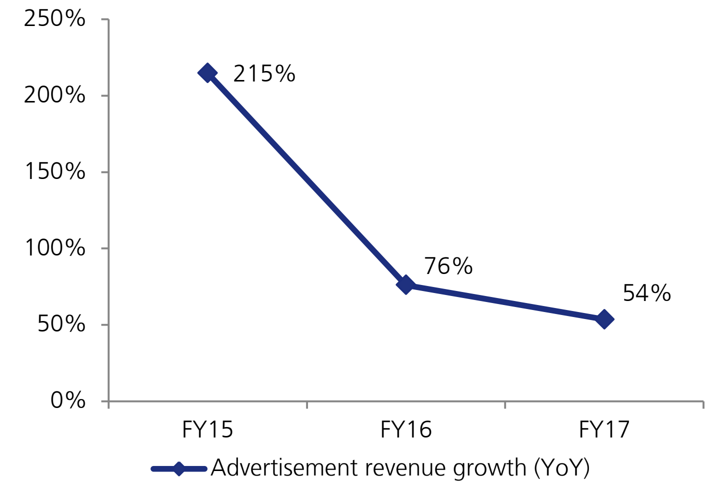
Furthermore, the company's sustained revenue growth (80% YoY), especially in the food ordering segment, despite an 81% decrease in annual operating burn (USD 12mn—FY17 vs. USD 64mn—FY16), reflects increased user retention and frequency that tags along with scale. The average monthly cash burn for Dec`16-Mar`17 was south of USD 250k compared to USD 4.2mn during March last fiscal.

Exhibit 40. Revenue from operations: Zomato




Source: Company, JM Financial

Exhibit 41. Ad revenue growth over the years: Zomato



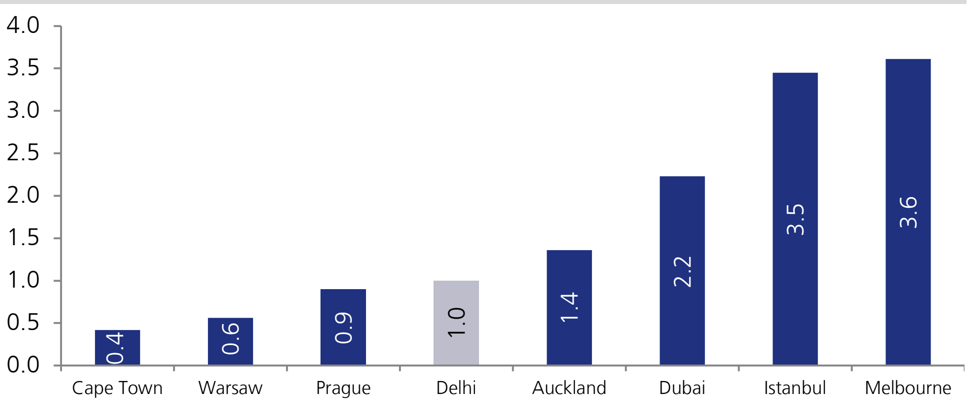

Source: Company, JM Financial

### Focused opportunity selection and flexible execution

Demand for online food delivery is concentrated in certain markets

Zomato decided to pull from certain local and international markets. This was again driven from the fact that the demand was concentrated in certain cities and it was pertinent to consolidate its position, where it is a market leader. For instance, Delhi as a market alone represents 25% of the total Indian market, as per the company. However, when compared to cities such as Dubai and Melbourne, the Indian capital is not half their market sizes. Hence, where to play is also pertinent together with how to play. Also, unit economics does not favour Zomato, when it is not using a restaurant's delivery service as a substantial cost is paid for delivery outsourcing. Again, in smaller cities restaurants do not have the delivery bandwidth nor consumers have high average order value.

Exhibit 42. Relative market sizes: Zomato




Source: Company, JM Financial

## Valuation: Out of trough?

Sharp decline in global investments in the food-tech space globally in 2016 has reflected in the valuations of listed players as well. Price-to-sales (P/S) multiples of the leading listed food-tech players (Yelp, GrubHub, Just Eat) corrected by 27-62% over 2015-16. Valuations have, however, started to inch back up. P/S multiples for these players are up 11-23% YTD in 2017. We expect the trends to sustain as market consolidation has weeded out irrational players. The same should be true for Indian players as well.

Zomato's previous funding round valued the company at c.USD 1bn, implying a P/S of 20x on FY17 basis. Though it appeared high at that time when compared to the global benchmarks, the valuation then did not include the food ordering business, in our view. Zomato's market leadership, strong growth, and India's large and under-penetrated market justify the premium valuations, in our view.

Global M&A transactions valued the restaurant aggregators at P/S ratio of 18-32x, in-line with Zomato's valuation in its previous funding round

Exhibit 43. P/S trend for leading food-tech players


Source: Bloomberg, JM Financial

Exhibit 44. Zomato's multiples are in-line with M&A multiples for similar restaurant aggregator platforms

| Acquirer | Target | Target's Revenue | Revenue growth | Acquisition Price | P/S multiple |
|---|---|---|---|---|---|
| Just Eat | Menulog | USD 20.8m | 80% | USD 687m | 18.35 |
| Delivery Hero | Yemeksepeti | USD 12.0m | 50% | USD 589m | 32.72 |

Source: Media reports, JM Financial

Exhibit 45. Relative valuation table

| | | | | P/E | | | EV/EBITDA | | | EV/Sales | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Name | Ticker | MCap (USD m) | EV (USD m) | FY1 | FY2 | FY3 | FY1 | FY2 | FY3 | FY1 | FY2 | FY3 |
| India - Internet | | | | | | | | | | | | |
| Infoedge | INFOE IN Equity | 1,618 | 1,461 | 110.8x | 61.8x | 45.7x | 103.1x | 45.5x | 29.7x | 7.9x | 6.3x | 5.0x |
| Just Dial | JUST IN Equity | 554 | 541 | 30.6x | 28.0x | 22.3x | 30.8x | 25.5x | 21.0x | 4.8x | 4.2x | 3.7x |
| Intrasoft | ITECH IN Equity | 86 | 81 | 35.7x | 20.9x | 12.8x | 25.9x | 14.7x | 9.0x | 0.6x | 0.4x | 0.3x |
| Infibeam | INFIBEAM IN Equity | 837 | 757 | 117.1x | 72.2x | 57.2x | 74.1x | 51.7x | 41.6x | 11.1x | 8.5x | 6.0x |
| Global | | | | | | | | | | | | |
| Leading Food Tech | | | | | | | | | | | | |
| Just Eat | JE/LN Equity | 5,106 | 60 | 3461.3x | 2495.7x | 1991.4x | 23.7x | 17.7x | 14.2x | 7.7x | 6.4x | 5.5x |
| GrubHub | GRUB US Equity | 3,871 | 55 | 40.4x | 32.6x | 27.0x | 19.2x | 15.2x | 12.9x | 5.4x | 4.4x | 3.7x |
| Takeaway.com | TKWY NA Equity | 1,402 | 18 | -66.7x | 169.1x | 41.1x | -126.2x | 70.5x | 22.6x | 7.2x | 5.5x | 4.4x |
| Yelp | YELP US EQUITY | 2,313 | 29 | 31.4x | 23.5x | 20.4x | 12.7x | 9.6x | 7.3x | 2.1x | 1.8x | 1.5x |
| Rocket Internet | TRIP US EQUITY | 3,541 | 31 | -24.8x | -74.6x | 37.6x | -54.4x | 923.9x | 40.2x | 8.4x | 13.4x | 11.4x |

Source: Bloomberg, Prices as of 15th May 2017, JM Financial

# Key risks

### a) Competitive risk

Competition is inevitable and happens to be one of the key risks. Nascent industry with no clear leader coupled with associated tailwinds has attracted best of the players to venture into the fast growing online food delivery space. The recent entry of Google and Uber further validates this point. Moreover, existing restaurant chains are also realising the growth opportunities that come with the structural shift and developing their independent platforms for food ordering.

However, we believe that after the early consolidation in the industry, only the serious players with viable business models survived and they have further consolidated their position in the industry. We believe the new entrants will find it difficult to uproot the already established players such as Zomato in the industry. China's food-tech industry and dominance of local players there proves a case in point. Also, entry of UberEats concerns Swiggy more than anyone due to similarity in their business model of operating delivery fleets.

Furthermore, the Indian food-tech industry is significantly large for a player to dominate and hence not a winner takes all market. It could easily accommodate 2-3 large players in the sector and help them grow healthily. Also, the entry of new and existing large players will only help the market to grow in size and increase the overall pie. As of now, the major business is driven by metro cities and a large number of Tier-I and Tier-II cities are untapped.

We believe the Indian food ordering business is significantly large for a single player to dominate

### b) New commission rates leads to higher restaurants churn

As the company scales and helps in generating better revenues for its restaurant partners, it is imminent that it will not stick to existing commission rates. However, the rise in commission rates might lead to a significant number of restaurant churn.

We believe that the above is not likely for a number of reasons. Firstly, already a number of restaurants depend on Zomato for major portion of their orders. Thus, the company can leverage the same to its advantage by charging higher commission rates. Secondly, the restaurants' business models help them enjoy high margins. Thus, it is unlikely that these partners would risk losing out on significant orders for nominal loss on margins. Thirdly, Zomato is a market leader, when it comes to restaurant listing and discovery service. The company provides all-round visibility for such restaurants and thus they would not risk losing out to other restaurant chains in this highly competitive industry.

### c) Consumer behaviour

A change in consumer preference causing them to order less or prefer ordering through telephone might adversely impact the company's expectation of future earnings. Zomato on its order platforms also provides an option to reach out to the restaurants through telephone, wherein the company loses on the commission revenues. Also, increase in consumer preference for Dine-Out rather than Ordering-In will further hamper the company's growth. However, we see the above is unlikely to happen as consumers get cash-rich and time-poor.

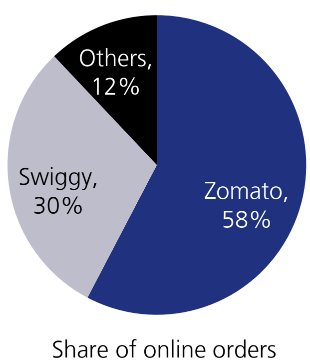
# Appendix 1: Market survey

We recently conducted a market survey of 30 restaurants across Mumbai and Delhi to better analyse and understand the demand patterns and preference of restaurants among the food ordering platforms.

Zomato was the preferred choice (64%) for the restaurants we surveyed. The main reason restaurants attributed was the higher traffic/order Zomato routes to them and hence more revenues. Zomato drives majority (58%) of the online orders for the restaurants surveyed, even where Swiggy was present. It also charges lower commission compared to its competitors, thus driving higher revenues and profit for restaurants. Furthermore, the delivery-only platforms such as Grab and Delhivery help them with the deliveries. Zomato is also more efficient and timely in its payment to restaurants, which restaurants like.

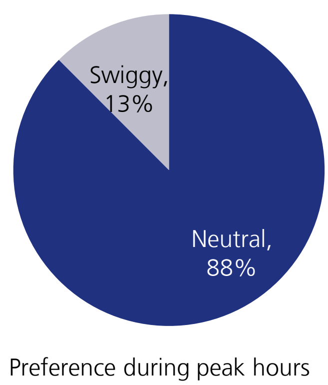
A substantial portion of respondents were neutral towards all their online partners for order fulfilment during peak hours. Although the commissions charged by these platforms differed, the total cost to the restaurant was same, including delivery expenses. That said, c.13% of the restaurants preferred to fulfil Swiggy's orders first, primarily because of services such as "Swiggy Assure" in which the delivery personnel collects the orders from the restaurant in guaranteed time.

Exhibit 46. Zomato dominates in terms of online orders



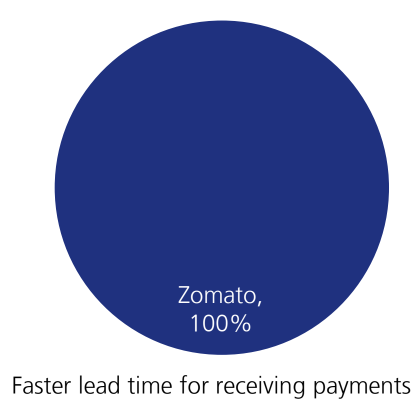

Source: n=30, JM Financial

Exhibit 47. 88% respondents are neutral towards food ordering platforms w.r.t. preference for order fulfilment in peak hours



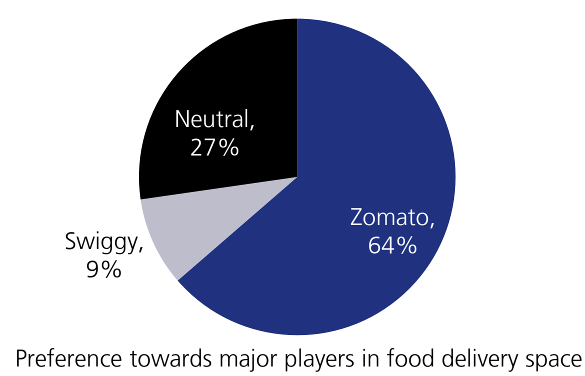

Source: n=30, JM Financial

Exhibit 48. Consensus among respondents that Zomato has lower lead time when it comes to receiving payments from these platforms




Source: n=30, JM Financial

Exhibit 49. 64% of the respondents relatively speaking value their partnership with Zomato more

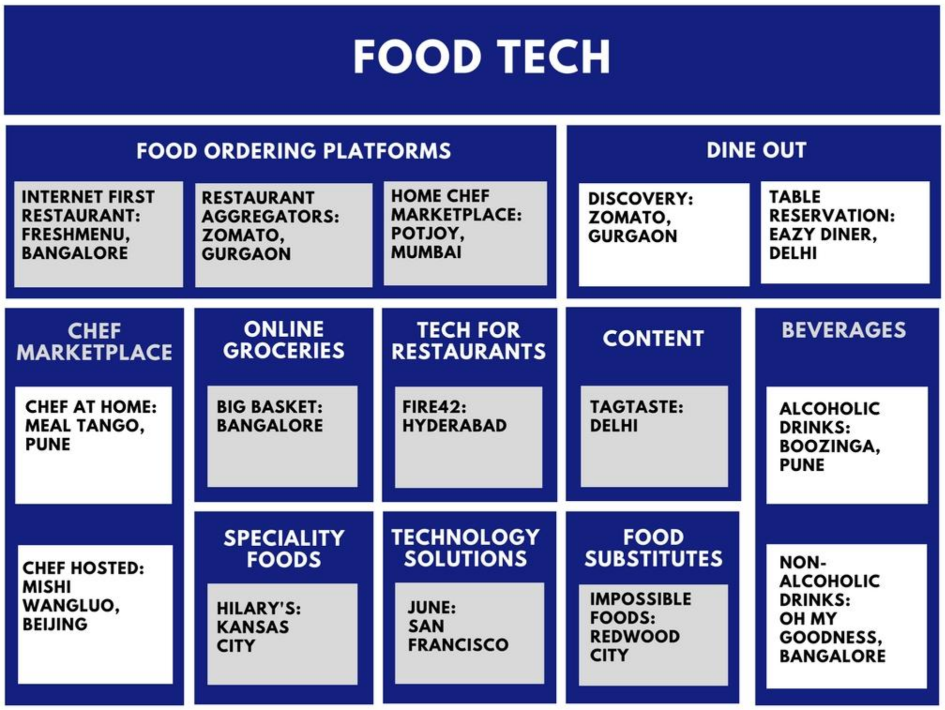



Source: n=30, JM Financial

## Appendix 2: Food-tech industry—a primer

The global food-tech ecosystem consists of companies that help discover restaurants, book tables online, order and deliver food as well as provide enterprise software solutions for the restaurant for managing online orders, etc. In food-tech, food ordering is the largest segment with nearly every one out of three start-ups being an online ordering platform. Not surprisingly, the online restaurant aggregators have attracted highest funding in the sector.

Exhibit 50. Global food-tech landscape




Source: Tracxn, JM Financial

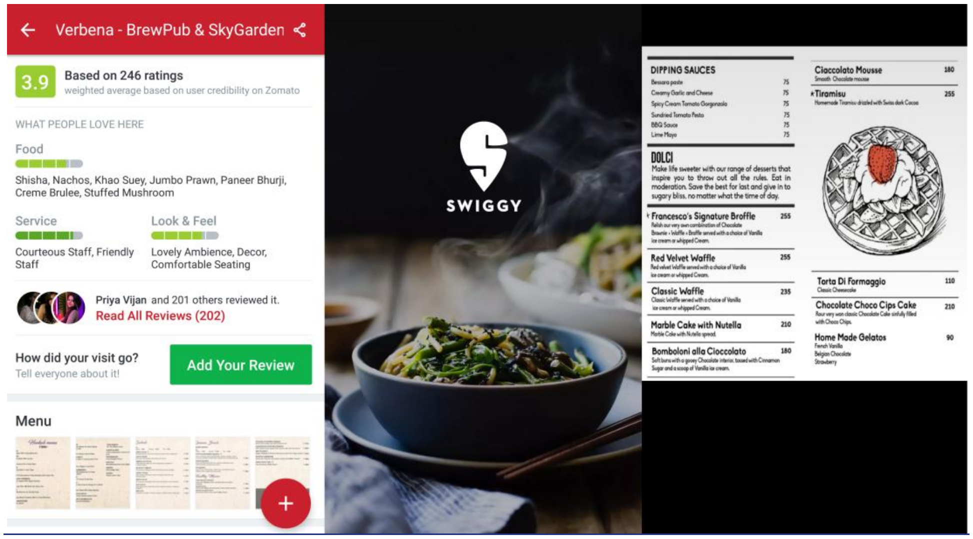
The food ordering segment predominantly consists of:

a) Aggregators: These offer customers access to multiple restaurants on a single digital platform. Start-ups such as Just Eat in the UK and Zomato in India have been following marketplace business model, wherein they play the role of aggregators for consumer and restaurants without taking control of logistics.

b) New Delivery: These platforms allow customers to view as well as order food through a single website or app. These platforms also help extend the delivery to even those restaurants that would otherwise not deliver, thus expanding the market. These start-ups (e.g., Swiggy), however, have to bear the cost of transportation and delivery fleet. This makes their business model less flexible. Furthermore, hyperlocal delivery and uneven distribution of food orders makes the economies of scale difficult to achieve, in our view. For example, orders peak towards lunch and dinner, whereas it is more or less stagnant throughout the day. Also, a substantial part of the business is on Fridays and weekends.

While food ordering and delivery, pioneered by Dominos, have existed for a while globally, the shift from offline to online food ordering has lagged other eCommerce categories. We attribute this to the existence of offline (telephone) ordering, consumers' proclivity to order from their select favourite restaurants and reluctance to experiment new ones online. However, this is changing fast as food-tech players enhance their offerings. Notably, the addition of customer reviews, improved UI/UX, offers and discounts along with increasing smartphone penetration are driving the shift (Exhibit 51).

### Exhibit 51. Improved UI/UX




Source: JM Financial

### Exhibit 52. Top-10 players in food ordering segment…

| Company | City | Funding | Investor |
|---|---|---|---|
| Ele.me | Shanghai | USD 2.34B | Sequoia, JD.com |
| Delivery Hero | Berlin | USD 1.37B | General Atlantic |
| Deliveroo | London | USD 474M | Accel Partners |
| HelloFresh | Berlin | USD 367M | Insight Ventures |
| Foodpanda | Berlin | USD 318M | Goldman Sachs |
| Baidu Waimai | Beijing | USD 250M | Hina Group |
| Zomato | Gurgaon | USD 225M | Info Edge, Sequoia |
| Blue Apron | NY | USD 194M | Fidelity |
| Just Eat | London | USD 129M | Greylock Partners |
| Takeaway | London | USD 118.8M | Prime Ventures |

Source: Tracxn, JM Financial

### Exhibit 53. …and the dine out segment

| Company | City | Funding | Investor |
|---|---|---|---|
| Zomato | Gurgaon | USD 225M | Info Edge, Sequoia |
| Ricebook | Beijing | USD 53.5M | IDG Capital Partners |
| Kzhuo | Beijing | USD 30M | Tiantu Capital |
| Ness | Los Altos | USD 20M | American Express |
| MangoPlate | Seoul | USD 7.2M | Qualcomm |
| Burpple | Singapore | USD 6.75M | Neoteny Labs |
| Chefs Feed | San Francisco | USD 6M | Subtraction Capital |
| Luka | NY | USD 4.54M | Y Combinator |
| Retty | Tokyo | USD 4.4M | Mizuho Capital |
| Foodspotting | San Francisco | USD 3.75M | 500 Startups, Felicis |

Source: Tracxn, JM Financial

### 100% takeaway outlets

**Absence of major real estate cost lowers barriers to entry for such businesses**

With GMV of INR 1bn, the 100% takeaway market in India has witnessed a 14% growth with total number of transactions clocking 2.1 million in 2015. One of the primary reasons for such takeaways flourishing is the need for affordable independent foodservice outlets by young urban population. From a business perspective, 100% takeaway outlets check all the boxes. Firstly, the absence of seating space in exorbitantly priced urban hubs eliminates a major cost for the outlet. As per a Grant Thornton report, real estate is the second-largest cost after raw materials and accounts for 15-20% of the revenues. Also, increased technology usage and development of third-party platforms help them to reach out and deliver to a larger audience.

Online ordering platforms benefit a huge deal from the above development due to increased demand for online food ordering and increased demand for advertisement slots due to higher competition. Also, delivery only platforms such as Grab and Delhivery also experience demand from such takeaway outlets, as they help them reach out to locations the outlets could not otherwise. Furthermore, total dependency for orders from these platforms gives them the leverage to charge higher commission from such outlets.

# Appendix 3: Zomato overview

Zomato is one of the leading food-tech players in India. As of 2016, the company has presence in 23 cities across the globe with clear market leadership in India and the UAE. Zomato started off as a platform for online discovery of restaurants and generated revenue through its classified business. More recently, the company has forayed into the growing its online food delivery business through the ordering platform "Zomato Order".

The restaurant search and discovery platform was first launched in 2008 under the name www.foodiebay.com. Over the years, the company has raised c.USD 225mn in funding, including the last Series G round of USD 60mn, led by Singapore-based Temasek Holdings. Info Edge (India) Limited is the largest investor in the company with c.47% stake (Exhibit 54).

Exhibit 54. Zomato funding and valuation till date

| Date | Fund raise | Valuation (USD mn) | Investors | INFOE's investment (USD mn) | INFOE's stake |
|---|---|---|---|---|---|
| 10-Aug | 1 | | Info Edge | 47 | |
| 11-Sep | 3 | | Info Edge | 182 | |
| 12-Sep | 2.5 | | Info Edge | 310 | 48.50% |
| 13-Jan | 10 | | Info Edge | 860 | 57.90% |
| 13-Nov | 37 | 161 | Sequoia/Info Edge | 1,430 | 50.10% |
| 14-Nov | 60 | 660 | Vy Capital/Info Edge/Sequoia | 3,272 | 50.10% |
| 15-Apr | 50 | 700 | Vy Capital/Info Edge/Sequoia | 4,830 | 50.10% |
| 15-Sep | 60 | 1000 | Temasek/Vy Capital | 4,838 | 47.00% |

Source: JM Financial

Apart from its restaurant discovery service, the company now offers multiple services under its name. Its offerings include white-label platform that helps restaurants create their own customised application, which features Zomato's support and analytics. It also has a table reservation service by the name Zomato Book. More recently, it has entered the food ordering business under the banner Zomato Orders. It aims to help consumers by offering frictionless ordering experience with large variety of options. Users can browse menus and track their deliveries in real time. The logistics in the process are fuelled by third-party affiliates. Zomato's applications are available on Windows, Android and iOS.

In terms of geography, India and the UAE stand to be the largest markets for the company. Its restaurant search and discovery service is available across 23 cities worldwide. Zomato Order is, however, available only it is major markets in India and the UAE. The company provides food ordering service in 13 cities of India and three cities of the UAE.

Also, as per our findings from the market survey, we believe that Zomato has been actively pursuing the creation of a large user base of consumers and at the same time increasing online orders for the listed restaurants by means of providing discounts on behalf of the restaurants that are advertising on it. This has multiple implications. Firstly, most of the advertised results on the platform are discounted and this pushes consumers into ordering online. Secondly, higher number of orders for restaurants helps them perceive that advertising drove higher sales for them, whereas a significant part was played by the discount provided. Hence, this results in restaurants purchasing advertising slots regularly. Lastly, one would argue that revenue from advertisements is offset by the discounts provided, but the larger picture lies in the benefits of scale. Once a dependency is created on the platform for sales, restaurants are charged a higher commission, which further helps improve the overall profitability for Zomato.

# Financial Tables (Consolidated)

## Income Statement (INR mn)

| Y/E March | FY15A | FY16A | FY17E | FY18E | FY19E |
|---|---|---|---|---|---|
| Net Sales | 6,113 | 7,235 | 8,284 | 9,729 | 11,722 |
| Sales Growth | 20.8% | 18.3% | 14.5% | 17.4% | 20.5% |
| Other Operating Income | 0 | 0 | 0 | 0 | 0 |
| **Total Revenue** | **6,113** | **7,235** | **8,284** | **9,729** | **11,722** |
| Cost of Goods Sold/Op. Exp | 2,518 | 3,205 | 3,609 | 4,100 | 4,902 |
| Personnel Cost | 0 | 0 | 0 | 0 | 0 |
| Other Expenses | 1,781 | 2,450 | 2,040 | 2,500 | 3,118 |
| **EBITDA** | **1,814** | **1,580** | **2,635** | **3,129** | **3,702** |
| EBITDA Margin | 29.7% | 21.8% | 31.8% | 32.2% | 31.6% |
| EBITDA Growth | 8.7% | -12.9% | 66.8% | 18.8% | 18.3% |
| Depn. & Amort. | 173 | 210 | 258 | 302 | 363 |
| EBIT | 1,640 | 1,370 | 2,376 | 2,828 | 3,339 |
| Other Income | 1,035 | 711 | 903 | 929 | 1,039 |
| Finance Cost | 0 | 0 | 0 | 0 | 0 |
| PBT before Excep. & Forex | 2,675 | 2,082 | 3,280 | 3,756 | 4,378 |
| Excep. & Forex Inc./Loss(-) | 0 | 0 | 0 | 0 | 0 |
| PBT | 2,675 | 2,082 | 3,280 | 3,756 | 4,378 |
| Taxes | 736 | 666 | 602 | 1,127 | 1,313 |
| Extraordinary Inc./Loss(-) | -293 | 115 | -403 | 0 | 0 |
| Assoc. Profit/Min. Int.(-) | 0 | 0 | 0 | 0 | 0 |
| Reported Net Profit | 1,647 | 1,530 | 2,274 | 2,629 | 3,065 |
| **Adjusted Net Profit** | **1,939** | **1,416** | **2,677** | **2,629** | **3,065** |
| Net Margin | 31.7% | 19.6% | 32.3% | 27.0% | 26.1% |
| Diluted Share Cap. (mn) | 120.2 | 120.9 | 120.9 | 120.9 | 120.9 |
| **Diluted EPS (Rs.)** | **16.1** | **11.7** | **22.1** | **21.7** | **25.3** |
| Diluted EPS Growth | 37.1% | -27.4% | 89.1% | -1.8% | 16.6% |
| Total Dividend + Tax | 410 | 426 | 573 | 573 | 645 |
| Dividend Per Share (Rs) | 3.0 | 3.0 | 4.0 | 4.0 | 4.5 |

Source: Company, JM Financial

## Balance Sheet (INR mn)

| Y/E March | FY15A | FY16A | FY17E | FY18E | FY19E |
|---|---|---|---|---|---|
| Shareholders' Fund | 16,624 | 17,640 | 19,797 | 21,853 | 24,273 |
| Share Capital | 1,202 | 1,209 | 1,211 | 1,211 | 1,211 |
| Reserves & Surplus | 15,422 | 16,431 | 18,585 | 20,642 | 23,061 |
| Preference Share Capital | 0 | 0 | 0 | 0 | 0 |
| Minority Interest | 0 | 0 | 0 | 0 | 0 |
| Total Loans | 3 | 4 | 5 | 5 | 5 |
| Def. Tax Liab. / Assets (-) | -64 | -60 | -88 | -88 | -88 |
| **Total - Equity & Liab.** | **16,563** | **17,584** | **19,713** | **21,770** | **24,189** |
| Net Fixed Assets | 935 | 1,020 | 1,052 | 1,145 | 1,302 |
| Gross Fixed Assets | 1,615 | 1,860 | 1,935 | 2,329 | 2,850 |
| Intangible Assets | 0 | 0 | 0 | 0 | 0 |
| Less: Depn. & Amort. | 680 | 840 | 883 | 1,184 | 1,548 |
| Capital WIP | 0 | 0 | 0 | 0 | 0 |
| Investments | 5,410 | 5,736 | 7,516 | 7,516 | 7,516 |
| Current Assets | 12,947 | 13,705 | 14,650 | 17,164 | 20,186 |
| Inventories | 0 | 0 | 0 | 0 | 0 |
| Sundry Debtors | 98 | 118 | 91 | 133 | 193 |
| Cash & Bank Balances | 11,981 | 9,879 | 10,937 | 13,005 | 15,411 |
| Loans & Advances | 0 | 0 | 0 | 0 | 0 |
| Other Current Assets | 869 | 3,707 | 3,622 | 4,026 | 4,582 |
| Current Liab. & Prov. | 2,729 | 2,877 | 3,505 | 4,055 | 4,815 |
| Current Liabilities | 0 | 0 | 0 | 0 | 0 |
| Provisions & Others | 2,729 | 2,877 | 3,505 | 4,055 | 4,815 |
| Net Current Assets | 10,219 | 10,828 | 11,145 | 13,109 | 15,371 |
| **Total - Assets** | **16,563** | **17,584** | **19,713** | **21,770** | **24,189** |

Source: Company, JM Financial

## Cash Flow Statement (INR mn)

| Y/E March | FY15A | FY16A | FY17E | FY18E | FY19E |
|---|---|---|---|---|---|
| Profit before Tax | 2,675 | 2,082 | 3,280 | 3,756 | 4,378 |
| Depn. & Amort. | 173 | 210 | 258 | 302 | 363 |
| Net Interest Exp. / Inc. (-) | -1,327 | -597 | -1,307 | -929 | -1,039 |
| Inc (-) / Dec in WCap. | -99 | -1,202 | 436 | 105 | 144 |
| Others | 0 | 0 | 0 | 0 | 0 |
| Taxes Paid | -736 | -662 | -631 | -1,127 | -1,313 |
| **Operating Cash Flow** | **686** | **-169** | **2,037** | **2,107** | **2,532** |
| Capex | -157 | -295 | -290 | -394 | -521 |
| Free Cash Flow | 529 | -464 | 1,747 | 1,713 | 2,011 |
| Inc (-) / Dec in Investments | -1,788 | -326 | -1,780 | 0 | 0 |
| Others | 1,044 | -797 | 1,207 | 929 | 1,039 |
| **Investing Cash Flow** | **-901** | **-1,419** | **-863** | **534** | **518** |
| Inc / Dec (-) in Capital | 110 | 7 | 2 | 0 | 0 |
| Dividend + Tax thereon | 7,245 | -521 | -119 | -573 | -645 |
| Inc / Dec (-) in Loans | -2 | 1 | 1 | 0 | 0 |
| Others | 0 | 0 | 0 | 0 | 0 |
| **Financing Cash Flow** | **7,354** | **-513** | **-116** | **-573** | **-645** |
| **Inc / Dec (-) in Cash** | **7,139** | **-2,101** | **1,058** | **2,068** | **2,405** |
| Opening Cash Balance | 4,842 | 11,981 | 9,879 | 10,937 | 13,005 |
| Closing Cash Balance | 11,981 | 9,879 | 10,937 | 13,005 | 15,411 |

Source: Company, JM Financial

## Dupont Analysis

| Y/E March | FY15A | FY16A | FY17E | FY18E | FY19E |
|---|---|---|---|---|---|
| Net Margin | 31.7% | 19.6% | 32.3% | 27.0% | 26.1% |
| Asset Turnover (x) | 0.5 | 0.4 | 0.4 | 0.5 | 0.5 |
| Leverage Factor (x) | 1.0 | 1.0 | 1.0 | 1.0 | 1.0 |
| RoE | 16.0% | 8.3% | 14.3% | 12.6% | 13.3% |

## Key Ratios

| Y/E March | FY15A | FY16A | FY17E | FY18E | FY19E |
|---|---|---|---|---|---|
| BV/Share (Rs.) | 142.3 | 145.4 | 161.7 | 178.5 | 198.1 |
| ROIC | 0.0% | 147.4% | 114.9% | 147.5% | 174.0% |
| ROE | 16.0% | 8.3% | 14.3% | 12.6% | 13.3% |
| Net Debt/Equity (x) | -0.7 | -0.6 | -0.6 | -0.6 | -0.6 |
| P/E (x) | 53.4 | 73.5 | 38.9 | 39.6 | 34.0 |
| P/B (x) | 6.1 | 5.9 | 5.3 | 4.8 | 4.3 |
| EV/EBITDA (x) | 48.9 | 57.5 | 34.1 | 28.0 | 23.1 |
| EV/Sales (x) | 14.5 | 12.6 | 10.8 | 9.0 | 7.3 |
| Debtor days | 6 | 6 | 4 | 5 | 6 |
| Inventory days | 0 | 0 | 0 | 0 | 0 |
| Creditor days | 0 | 0 | 0 | 0 | 0 |

Source: Company, JM Financial

# APPENDIX I

## JM Financial Institutional Securities Limited

Corporate Identity Number: U65192MH1995PLC092522
Member of BSE Ltd. and National Stock Exchange of India Ltd. and Metropolitan Stock Exchange of India Ltd.
SEBI Registration Nos.: BSE - INZ010012532, NSE - INZ230012536 and MSEI - INZ260012539, Research Analyst – INH000000610
Registered Office: 7th Floor, Cnergy, Appasaheb Marathe Marg, Prabhadevi, Mumbai 400 025, India.
Board: +9122 6630 3030 | Fax: +91 22 6630 3488 | Email: jmfinancial.research@jmfl.com | www.jmfl.com
Compliance Officer: Mr. Sunny Shah | Tel: +91 22 6630 3383 | Email: sunny.shah@jmfl.com

| Definition of ratings | |
|---|---|
| Rating | Meaning |
| Buy | Total expected returns of more than 15%. Total expected return includes dividend yields. |
| Hold | Price expected to move in the range of 10% downside to 15% upside from the current market price. |
| Sell | Price expected to move downwards by more than 10% |

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