

Resilient SSSg demonstrates brand strength

Collins Foods delivered a robust FY23 result, modestly exceeding our forecasts, driven by stronger SSSg and higher KFC Europe margin, and despite ongoing margin pressure from cost inflation. We are encouraged by the resilience of SSSg in recent months in an environment of tightening consumer spending. Persistent cost inflation is delaying a cyclical recovery in margins and constraining near term earnings growth. Building on an impressive FY23 result, confirmation of an acceleration in new store openings in KFC Europe will present an important catalyst to build further confidence in the long-term growth profile.

Key Points

FY23 result. NPAT (norm) of \$51.9m declined 13% on pcp, but was 7% above our forecast, driven by slightly stronger EBITDA and lower D&A expense. EBITDA (norm, post-AASB16) of \$205m declined 2% on pcp, but was 1% above our forecast. Stronger SSSg and KFC Europe margin offset weaker KFC Australia margin and higher corporate costs. Operating cash flow was broadly in line with expectations, while the final dividend was in line with pcp.

Outlook. No explicit guidance. Robust KFC SSSg across first 7 weeks of FY24 (Australia: +8.8%, Netherlands: +9.0% and Germany: +12.4%). While price and ticket remain the major drivers, we are encouraged by the resilience of transaction count (ie. volumes) in an environment of tightening consumer spending. Elevated inflation and supply chain disruption continue to impede what is normally attractive and predictable margins. We continue to view this as a timing issue and expect both a cyclical recovery, complemented by structural growth in KFC Europe through the benefit of operational scale. Confirmation of an acceleration in new store openings in KFC Europe will present an important catalyst to build further confidence in the long-term growth profile.

Forecasts. Sales increase 3%, driven by higher SSSg in FY24 (though below the level achieved through the first 7 weeks) and inclusion of the recently acquired 8 KFC stores in the Netherlands. EBITDA broadly unchanged, with higher sales offset by lower margins. The latter reflects lower margins in KFC Australia (FY24 flat on pcp) and higher margins in Europe (FY24 slightly lower than 2H23). NPAT down 11% in FY24 and 6% in FY25, driven by higher D&A and interest expense. On a pre_AASB16 basis, NPAT forecasts are down 5% and 1%, respectively.

Valuation. Our revised 12m target of \$11.16 p/sh (was \$11.49) is set at the mid-point of our DCF and earnings capitalisation valuations. Our DCF is broadly unchanged at \$13.90 p/share. Our earnings capitalisation valuation of \$8.41 p/share (was \$9.39) is based on an FY24 PER of 17x (pre-AASB16), with the decline primary driven by earnings changes. As a guide, rolling forward our earnings capitalisation valuation to FY25 lifts the valuation to \$10.98, benefitting from assumed margin improvements, and is more closely aligned with our view of fundamental value.

Recommendation

OVERWEIGHT

12-mth target price (AUD)	\$11.16
Share price @ 27-Jun-23 (AUD)	\$9.25
Forecast 12-mth capital return	20.6%
Forecast 12-mth dividend yield	2.9%
12-mth total shareholder return	23.5%

Market cap (\$m)	1,085
Enterprise value (\$m)	1,297
Shares on issue (m)	117.3
Sold short (%)	0.9
ASX Small Ords weight (%)	0.3
Median turnover/day (\$m)	3.0

James Ferrier, CFA

james.ferrier@wilsonsadvisory.com.au
Tel. +61 3 9640 3827

12-mth price performance (\$)



	1-mth	6-mth	12-mth
Abs return (%)	7.6	30.8	3.5
Rel return (%)	10.4	33.6	0.6

Financial summary (Y/E Apr, AUD)	FY22A	FY23A	FY24E	FY25E	FY26E
EBITDA norm (\$m)	209.2	205.1	220.8	253.3	281.7
NPAT norm (\$m)	59.7	51.9	49.0	65.9	80.7
EPS norm (cents)	51.2	44.5	41.7	56.2	68.8
Consensus EPS (cents)			43.8	54.6	
EV/EBITDA (x)	6.0	6.3	5.6	4.8	4.2
P/E (x)	18.1	20.8	22.2	16.5	13.5
Dividend yield (%)	2.9	2.9	2.9	3.8	4.3

Source: Company data, Wilsons estimate, Refinitiv, IRESS.
All amounts are in Australian Dollar (A\$) unless otherwise stated.

Wilsons Equity Research

Analyst(s) who owns shares in the Company: n/a Issued by Wilsons Advisory and Stockbroking Limited (Wilsons) ABN 68 010 529 665 – Australian Financial Services Licence No 238375, a participant of ASX Group and should be read in conjunction with the disclosures and disclaimer in this report. Important disclosures regarding companies that are subject of this report and an explanation of recommendations can be found at the end of this document.

Key changes		30-Nov	After	Var %
EBITDA	FY24E	222.4	220.8	-1%
norm	FY25E	252.0	253.3	1%
(\$m)	FY26E		281.7	
EPS	FY24E	47.2	41.7	-11%
norm	FY25E	60.1	56.2	-7%
(cents)	FY26E		68.8	
Price target		11.49	11.16	-3%
Rating		O/W	O/W	

Business Description

Collins Foods Limited (CKF) operates 344 KFC restaurants (as the franchisee) throughout Australia, and more recently via the acquisition of store networks in the Netherlands and Germany. Collins Foods also operates 26 Taco Bell franchises across Queensland, Victoria and WA.

Catalysts

Read-through from peer results; Success of marketing and promotional campaigns; Execution of store opening targets; Acquisitions.

P&L (\$m)	FY22A	FY23A	FY24E	FY25E	FY26E
Sales	1,185	1,349	1,494	1,584	1,679
EBITDA norm	209.2	205.1	220.8	253.3	281.7
EBIT norm	116.1	107.9	111.4	137.1	158.9
PBT norm	85.9	75.5	71.0	95.5	116.9
NPAT norm	59.7	51.9	49.0	65.9	80.7
NPAT reported	54.8	11.3	47.6	64.5	79.3
EPS norm (cents)	51.2	44.5	41.7	56.2	68.8
DPS (cents)	27.0	27.0	27.0	35.5	39.5

Growth (%)	FY22A	FY23A	FY24E	FY25E	FY26E
Sales	11.1	13.9	10.8	6.1	6.0
EBITDA norm	12.3	(2.0)	7.7	14.7	11.2
NPAT norm	25.6	(13.1)	(5.7)	34.6	22.4
EPS norm (cents)	25.6	(13.2)	(6.2)	34.6	22.4
DPS (cents)	17.4	0.0	0.0	31.5	11.3

Margins and returns (%)	FY22A	FY23A	FY24E	FY25E	FY26E
EBITDA margin	17.7	15.2	14.8	16.0	16.8
EBIT margin	9.8	8.0	7.5	8.7	9.5
PBT margin	7.3	5.6	4.8	6.0	7.0
NPAT margin	5.0	3.8	3.3	4.2	4.8
ROA	9.0	7.9	8.2	10.3	12.2
ROIC	20.5	18.1	20.0	24.5	28.1
ROE	15.2	13.5	12.2	15.4	17.5

Interims (\$m)	2H22A	1H23A	2H23A	1H24E	2H24E
Sales	650.3	614.3	734.3	686.0	807.6
EBITDA norm	114.2	95.4	109.7	106.2	114.7
EBIT norm	61.8	50.8	57.1	56.0	55.4
PBT norm	45.2	35.9	39.6	37.1	33.9
NPAT norm	30.9	24.8	27.1	25.6	23.4
NPAT reported	28.4	11.0	0.3	24.9	22.7
EPS norm (cents)	26.5	21.2	23.3	21.8	19.9
DPS (cents)	15.0	12.0	15.0	12.0	15.0

Stock specific	FY22A	FY23A	FY24E	FY25E	FY26E
KFC Aust EBITDA (\$m)	206.9	201.6	215.0	237.4	254.6
KFC Europe EBITDA (\$m)	27.6	32.8	39.5	50.8	63.1
Sizzler EBITDA (\$m)	1.7	2.9	0.4	0.0	0.0
Taco Bell EBITDA (\$m)	(0.4)	(1.5)	(0.3)	0.5	0.6
Corporate costs (\$m)	(26.6)	(30.7)	(33.8)	(35.5)	(36.5)

Investment Thesis

We remain attracted to the investment thesis for Collins Foods, notably the strength of the KFC brand (particularly in Australia), significant growth opportunities through store rollout (particularly in Europe), and strong cash conversion. In the near-term, consumer spending patterns and inflationary pressures on margins warrant investor attention.

Risks

Economic conditions and consumer sentiment and the associated impact on demand; Management of the KFC and Taco Bell brands by the franchisor; Execution of growth plans in new geographies / brands.

Balance sheet (\$m)	FY22A	FY23A	FY24E	FY25E	FY26E
Cash & equivalents	97.2	80.2	104.3	100.0	97.9
Current receivables	4.2	20.1	5.2	5.5	5.9
Current inventory	7.9	8.3	10.5	11.1	11.8
PPE	216.1	224.5	199.1	173.9	152.4
Intangibles	475.3	492.3	488.0	483.5	478.7
Other assets	482.2	544.9	551.4	554.2	557.4
Total assets	1,283	1,370	1,358	1,328	1,304
Current payables	116.5	116.5	134.4	142.6	151.1
Total debt	271.0	291.9	261.9	231.9	201.9
Other liabilities	502.0	577.5	561.7	527.0	489.1
Total liabilities	889.4	985.9	958.0	901.4	842.0
Minorities	0.0	0.0	0.0	0.0	0.0
Shareholders equity	393.5	384.5	400.4	426.8	462.1

Cash flow (\$m)	FY22A	FY23A	FY24E	FY25E	FY26E
Operating cash flow	156.3	146.2	153.8	161.8	180.1
Maintenance capex	(18.5)	(16.8)	(20.2)	(21.8)	(23.3)
Free cash flow	137.8	129.4	133.7	140.1	156.8
Growth capex	(50.5)	(58.8)	(59.5)	(64.7)	(73.3)
Acquisitions/disposals	(28.3)	(17.9)	22.8	0.0	0.0
Dividends paid	(28.6)	(29.4)	(31.7)	(38.1)	(44.0)
Other cash flow	(32.0)	(43.5)	(41.1)	(43.0)	(44.8)
Cash flow pre-financing	(1.6)	(20.3)	24.2	(5.7)	(5.4)
Funded by equity	0.0	0.0	0.0	0.0	0.0
Funded by cash/debt	(1.5)	17.0	5.8	35.7	35.4

Liquidity	FY22A	FY23A	FY24E	FY25E	FY26E
Cash conversion (%)	101.5	101.5	99.7	89.9	90.4
Net debt (\$m)	173.8	211.6	157.6	131.8	104.0
Net debt / EBITDA (x)	0.8	1.0	0.7	0.5	0.4
ND / ND + Equity (%)	30.6	35.5	28.2	23.6	18.4
EBIT / Interest expense (x)	3.8	3.3	2.8	3.3	3.8

Valuation	FY22A	FY23A	FY24E	FY25E	FY26E
EV / Sales (x)	1.1	1.0	0.8	0.8	0.7
EV / EBITDA (x)	6.0	6.3	5.6	4.8	4.2
EV / EBIT (x)	10.8	12.0	11.2	8.9	7.5
P / E (x)	18.1	20.8	22.2	16.5	13.5
P / BV (x)	2.7	2.8	2.7	2.5	2.3
FCF yield (%)	12.8	11.9	12.3	12.9	14.4
Dividend yield (%)	2.9	2.9	2.9	3.8	4.3
Payout ratio (%)	52.7	60.7	64.7	63.2	57.4
Franking (%)	100.0	100.0	100.0	100.0	100.0
Weighted shares (m)	116.6	116.7	117.3	117.3	117.3

Source: Company data, Wilsons estimate, Refinitiv, IRESS.
All amounts are in Australian Dollar (A\$) unless otherwise stated.

FY23 Result Review

Figure 1: Summary of FY23 result

Y/E Apr. AUD		FY22A	FY23A	Growth	WILSe	Var
Operating revenue	\$m	1,184.5	1,348.6	13.9%	1,353.1	(0.3%)
KFC Australia	\$m	206.9	201.6	(2.6%)	203.2	(0.8%)
KFC Europe	\$m	27.6	32.8	18.9%	27.5	19.1%
Taco Bell	\$m	(0.4)	(1.5)	275.0%	(1.4)	5.7%
Sizzler	\$m	1.7	2.9	70.6%	2.4	21.8%
Shared services / other	\$m	(26.6)	(30.7)	15.4%	(28.2)	8.8%
EBITDA norm	\$m	209.2	205.1	(2.0%)	203.5	0.8%
Margin	%	17.7%	15.2%	n/a	15.0%	n/a
EBIT norm	\$m	116.1	107.9	(7.1%)	104.4	3.3%
Margin	%	9.8%	8.0%	n/a	7.7%	n/a
Pre-tax profit	\$m	85.9	75.5	(12.1%)	70.7	6.8%
NPAT norm	\$m	59.7	51.9	(13.1%)	48.8	6.5%
NPAT reported	\$m	54.8	11.3	(79.4%)	47.4	(76.2%)
EPS norm	cents	51.2	44.5	(13.2%)	41.7	6.6%
DPS	cents	27.0	27.0	0.0%	24.5	10.2%
Operating cash flow	\$m	156.3	146.2	(6.5%)	142.8	2.4%
Net debt	\$m	173.8	211.6	21.8%	192.7	9.8%

Source: Company data & Wilsons.

Income Statement

Revenue of \$1,349m increased 13.9% on pcp and was in line with our forecast.

EBITDA (norm, post-AASB16) of \$205m declined 2% on pcp, but was 1% above our forecast. Segment results included:

- KFC Australia** EBITDA of \$202m declined 3% on pcp and was 1% below our forecast. SSSg of +5.8% exceeded our forecast of +5.2%, but this was more than offset by a weaker EBITDA margin (pre-AASB16), down 240bps on pcp and 40bps below our forecast, driven by cost inflation across labour, ingredients and energy. Digital sales reached 24% of total sales in 2H23, up from 22% in 1H23 and 17% in FY22.
- KFC Europe** EBITDA of \$32.8m increased 19% on pcp and was 19% above our forecast. SSSg of +13.9% exceeded our forecast of +11.0% and this was compounded by a stronger 2H23 EBITDA margin (pre-AASB16), up 280bps on pcp and hoh. We understand the margin improvement reflected operating leverage in the owned store network driven by higher sales, along with achievement of the CFA incentive (paid on calendar year) for operational performance across the franchise network and meeting of development targets.
- Taco Bell** EBITDA loss of \$1.5m. Management opted to impair the remaining asset value associated with Taco Bell.

NPAT (norm) of \$51.9m declined 13% on pcp, but was 7% above our forecast, driven by slightly stronger EBITDA and lower D&A expense.

NPAT (reported) included significant items associated with Taco Bell impairments and acquisitions.

A final dividend of 15cps was declared which was in line with pcp, but above our forecast of 12.5cps. This brings the total FY23 dividend to 27.0 cps fully franked.

| Cash Flow

Operating cash flow of \$146m declined 7% on pcp, but was 2% above our forecast.

| Balance Sheet

Net debt at \$212m increased 22% and was 10% above our forecast, primarily driven by funding of the acquisition of 8 KFC stores in the Netherlands. The leverage ratio (pre-AASB16) stands at 1.5x (pcp: 1.2x).

Earnings Outlook

Guidance

No explicit guidance. Key commentary and focus areas for each segment include:

KFC Australia

First seven weeks FY24 SSSg of +8.8%. Cost pressure expected to persist during FY24 with higher energy and labour costs feeding through; some lag in commodity price improvements flowing through to COGS. Targeting FY24 EBITDA to be broadly margin neutral with improvement in FY25 towards historical levels. Supply chain, energy and menu pricing initiatives to mitigate inflation. Digital and delivery channels expected to drive further growth. New restaurant development of nine to 12 restaurants expected in FY24.

KFC Europe

First seven weeks FY24 SSSg of: +9.0% (Netherlands) and +12.4% (Germany). Margin headwinds remain with significant cost increases across energy, labour and COGS; potential softening of pressures in second half FY24. Margin offsets from menu pricing, value-focused marketing, operational efficiencies, and procurement initiatives. Targeting limited margin contraction in FY24. New restaurant development of three to five restaurants expected in FY24, with pipeline building in line with CFA targets. Monitoring landscape for additional M&A opportunities, including within other European countries.

Taco Bell

First seven weeks FY24 SSSg of +2.1%. Focus on return to SSS growth through enhanced product quality, e-commerce expansion, and marketing initiatives focused on value and taste. Margin pressure expected to continue in FY24. Target to re-establish positive EBITDA at restaurant level (Pre start up and brand G&A costs: pre AASB 16). Restaurant rollout currently paused.

Changes to Our Forecasts

Sales increase 3%, driven by higher SSSg in FY24 (though below the level achieved through the first 7 weeks) and inclusion of the recently acquired 8 KFC stores in the Netherlands.

EBITDA broadly unchanged, with higher sales offset by lower margins. The latter reflects lower margins in KFC Australia (FY24 flat on pcp) and higher margins in Europe (FY24 slightly lower than 2H23).

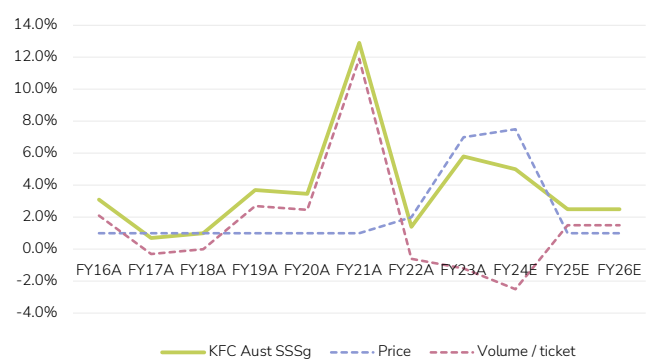
NPAT down 11% in FY24 and 6% in FY25, driven by higher D&A and interest expense. On a pre_AASB16 basis, NPAT forecasts are down 5% and 1%, respectively.

Figure 2: Summary of changes to our forecasts

Y/E Apr, AUD		FY24E			FY25E		
		Old	New	% chg	Old	New	% chg
Group sales	\$m	1,446.0	1,493.6	3.3%	1,538.9	1,584.1	2.9%
Group EBITDA	\$m	222.4	220.8	(0.7%)	252.0	253.3	0.5%
Group EBIT	\$m	117.5	111.4	(5.2%)	140.6	137.1	(2.5%)
NPAT norm	\$m	55.3	49.0	(11.4%)	70.4	65.9	(6.4%)
EPS norm	cents	47.2	41.7	(11.5%)	60.1	56.2	(6.5%)
DPS	cents	27.5	27.0	(1.8%)	35.5	35.5	0.0%

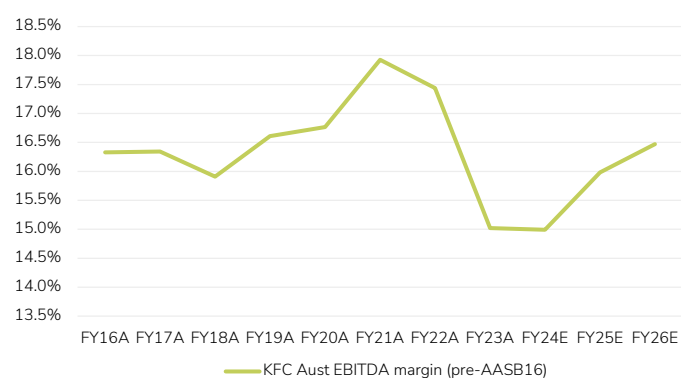
Source: Company data & Wilsons.

Figure 3: KFC Australia segment SSSg disaggregated



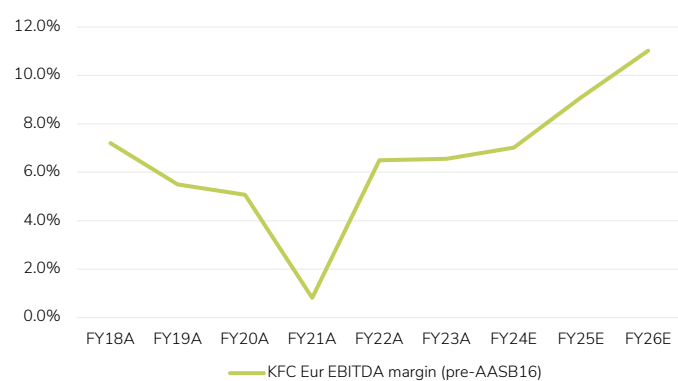
Source: Company data & Wilsons.

Figure 4: KFC Australia segment EBITDA margin



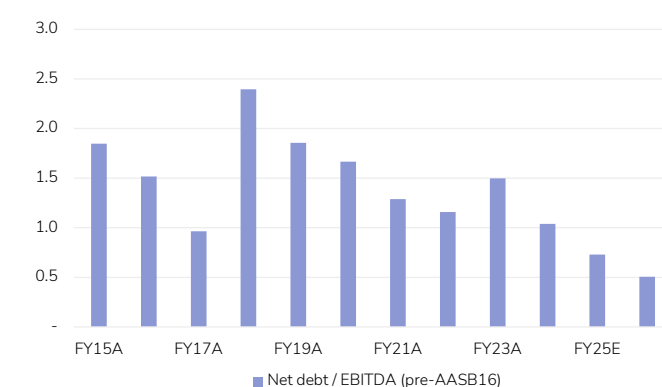
Source: Company data & Wilsons.

Figure 5: KFC Europe segment EBITDA margin



Source: Company data & Wilsons.

Figure 6: Group leverage ratio



Source: Company data & Wilsons.

Figure 7: Summary of earnings pre and post-AASB16

Y/E Apr, AUD		FY18A	FY19A	FY20A	FY21A	FY22A	FY23A	FY24E	FY25E	FY26E
Post-AASB16										
EBITDA norm	\$m				186.3	209.2	205.1	220.8	253.3	281.7
EBIT norm	\$m				102.2	116.1	107.9	111.4	137.1	158.9
PBT norm	\$m				72.8	85.9	75.5	71.0	95.5	116.9
NPAT norm	\$m				47.6	59.7	51.9	49.0	65.9	80.7
EPS norm	cents				40.8	51.2	44.5	41.7	56.2	68.8
Pre-AASB16										
EBITDA norm	\$m	94.2	114.0	120.7	136.4	150.0	141.4	151.6	180.6	205.5
EBIT norm	\$m	64.2	76.8	80.2	93.5	101.9	93.1	96.4	121.7	143.1
PBT norm	\$m	54.7	66.0	69.5	84.7	94.4	86.1	84.1	109.8	132.5
NPAT norm	\$m	39.0	45.0	47.2	56.7	64.6	59.2	58.0	75.8	91.4
EPS norm	cents	33.9	38.6	40.5	48.6	55.4	50.7	49.5	64.6	77.9

Source: Company data & Wilsons.

Revised Forecasts

Figure 8: Summary of our revised forecasts

Y/E Apr, AUD		FY18A	FY19A	FY20A	FY21A	FY22A	FY23A	FY24E	FY25E	FY26E
KFC Australia	#	223.0	231.0	240.0	251.0	261.0	272.0	281.0	289.0	297.0
KFC Europe	#	33.0	37.0	40.0	46.0	62.0	64.0	74.0	81.0	91.0
Taco Bell	#	1.0	4.0	12.0	16.0	20.0	28.0	26.0	26.0	26.0
Sizzler	#	14.0	12.0	9.0	0.0	0.0	0.0	0.0	0.0	0.0
Total period end stores	#	271.0	284.0	301.0	313.0	343.0	364.0	381.0	396.0	414.0
New new stores	#	47.0	13.0	17.0	12.0	30.0	21.0	17.0	15.0	18.0
KFC Australia SSSg	%	1.0%	3.7%	3.5%	12.9%	1.4%	5.8%	5.0%	2.5%	2.5%
KFC Europe SSSg	%	0.8%	(3.7%)	(5.8%)	(0.6%)	16.8%	13.9%	6.0%	2.5%	2.5%
Taco Bell SSSg	%	n/a	n/a	n/a	0.0	(8.1%)	(4.8%)	0.0%	2.5%	2.5%
KFC Australia	\$m	624.1	722.6	791.5	900.4	955.4	1,051.3	1,131.3	1,192.8	1,254.1
KFC Europe	\$m	91.6	123.8	134.1	134.9	190.4	249.5	306.5	337.4	369.6
Taco Bell	\$m	1.3	7.5	17.8	28.0	35.8	43.3	55.2	53.9	55.3
Sizzler	\$m	54.9	45.5	37.7	1.6	2.8	4.1	0.6	0.0	0.0
Group sales revenue	\$m	771.9	899.4	981.1	1,064.9	1,184.4	1,348.2	1,493.6	1,584.1	1,678.9
Growth	%	22.8%	16.5%	9.1%	8.5%	11.2%	13.8%	10.8%	6.1%	6.0%
KFC Australia	\$m	99.3	120.0	132.7	198.5	206.9	201.6	215.0	237.4	254.6
KFC Europe	\$m	6.6	6.8	6.8	12.0	27.6	32.8	39.5	50.8	63.1
Taco Bell	\$m	(0.2)	(1.0)	(2.0)	0.2	(0.4)	(1.5)	(0.3)	0.5	0.6
Sizzler	\$m	4.6	4.9	3.4	1.6	1.7	2.9	0.4	0.0	0.0
Shared services / other	\$m	(16.1)	(17.0)	(20.4)	(26.0)	(26.6)	(30.7)	(33.8)	(35.5)	(36.5)
Group EBITDA norm	\$m	94.2	113.7	120.5	186.3	209.2	205.1	220.8	253.3	281.7
Growth	%	16.2%	20.8%	5.9%	54.6%	12.3%	(2.0%)	7.7%	14.7%	11.2%
Margin	%	12.2%	12.6%	12.3%	17.5%	17.7%	15.2%	14.8%	16.0%	16.8%
KFC Australia EBITDA margin	%	15.9%	16.6%	16.8%	22.0%	21.7%	19.2%	19.0%	19.9%	20.3%
KFC Europe EBITDA margin	%	7.2%	5.5%	5.1%	8.9%	14.5%	13.1%	12.9%	15.1%	17.1%
Taco Bell EBITDA margin	%	(15.4%)	(13.3%)	(11.2%)	0.7%	(1.1%)	(3.5%)	(0.5%)	1.0%	1.0%
Depreciation and amortisation	\$m	(30.1)	(37.2)	(40.5)	(84.1)	(93.1)	(97.2)	(109.4)	(116.2)	(122.8)
Group EBIT norm	\$m	64.1	76.5	80.0	102.2	116.1	107.9	111.4	137.1	158.9
Growth	%	11.8%	19.3%	4.6%	27.7%	13.5%	(7.1%)	3.3%	23.1%	15.9%
Margin	%	8.3%	8.5%	8.2%	9.6%	9.8%	8.0%	7.5%	8.7%	9.5%

Source: Company data & Wilsons.

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For more information please phone: 1300 655 015 or email: publications@wilsonsadvisory.com.au