Indebted Taste bets on Starbucks

By Marc Hasenfuss

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Pretax losses at franchising group Taste Holdings widened to R45.5m in the six months to end-August, but the longer-term profit potential of the Starbucks coffee brand has started to percolate through since being launched in April.

Carlo Gonzaga and Howard Schultz.Picture: Freddy Mavunda

Taste CEO Carlo Gonzaga said the three Starbucks outlets were trading well ahead of initial company forecasts.

For the four months of trading during the interim reporting period, the first two stores — Rosebank and Mall of Africa — generated combined revenues of R18m and were producing positive earnings before interest, tax, depreciation and amortisation (ebitda), Gonzaga said.

The sooner Taste can pour profits from Starbucks the better, as borrowing and bank overdrafts are sitting close to R300m, with cash at about R43m.

Vunani Securities small-to-midcap analyst Anthony Clark expressed concern about how much cash Taste was eating up. "They have raised R500m from shareholders in recent years, which has been spent at a rapid rate. I'm convinced they will need another cash infusion to keep going … which will be difficult at the current share price."

Gonzaga, however, does not foresee another capital raising exercise. "Starbucks looks better than we thought it would be. We foresee having to raise capital only if we want to accelerate our growth plans for Starbucks and Domino's, or make an investment in jewellery inventory."

Taste's jewellery franchising operations were also chipping in encouragingly and had more than doubled interim pretax profits to R14.5m from revenues of R296m.

Despite the lively start by Starbucks, Gonzaga stressed that Taste remained cautious around potential store numbers – reiterating a medium-term goal of between 12 and 16 outlets in the next two years.

"What we are really focusing on is ensuring the highest return on capital we can get at Starbucks. That might mean fewer, larger outlets that are highly cash generative rather than just pushing for store numbers. A 200m² store requires capital expenditure of around R7m, but the returns are in excess of 25% on an internal rate of return."

Gonzaga conceded Taste — which is also rolling out pizza brand Domino's in SA — would continue to see earnings pressure as investment into flagship brands continued.

But he estimated that Starbucks would reach an ebitda breakeven at about five outlets.

Gonzaga also reported that the Domino's business — which has seen existing Scooters outlets converted into Domino's outlets — had started to settle down. "We have seen average weekly sales rise 17% since March 2016."

Domino's ended the interim period with 85 outlets (74 at the end of February) and had already added another two outlets in the second half.

Gonzaga said the Domino's conversion had largely been concluded, with just two opportunities remaining.

He stressed that lessons learnt in the Domino’s conversion and rollout had been executed in the Starbucks business.

"Already in all three [Starbucks] stores, we are transacting more than three times faster than when we launched."

Source: Business Day