February 2024

Initiating Coverage | Sector: Internet

DreamFolks

Landing gear retracted; charting a steep trajectory

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DreamFolks

Landing gear retracted; charting a steep trajectory

DreamFolks (DFS) is India's leading airport services aggregator and tech platform, connecting lounges and premium airport facilities with users of bank credit/debit cards. DFS holds a volume market share of over 75% in domestic airport lounges and has 100% coverage. DFS is the go-to partner for banks seeking to provide complimentary lounge access and is highly profitable and asset light. We expect the company to benefit from the rapid growth in the Indian airline industry, driven by competitive fares, rising leisure travel, new airports, and government push. Further, the increasing adoption of bank card (with lounge access as a key benefit) is boosting the pay-per-use revenue model of DFS. This should help it deliver a strong 20% revenue/28% PAT CAGR over FY24E-26E, despite a high base and near-term setbacks due to revised airport charges. We see venturing into international markets as a lucrative long-term opportunity carrying significant potential value. We initiate on the stock with a BUY rating at a TP of INR 650, implying 34% potential upside.

DreamFolks

BSE Sensex	S&P CNX
73,095	22,198

CMP: INR486 **TP: INR650 (+34%)** **Buy**

DreamFolks

Stock Info

Bloomberg	DREAMFOL IN
Equity Shares (m)	54.4
M.Cap.(INRb)/(USDb)	25.6 / 0.3
52-Week Range (INR)	847 / 397
1, 6, 12 Rel. Per (%)	-16/-16/-13
12M Avg Val (INR M)	263
Free float (%)	34.0

Financial Snapshot (INR b)

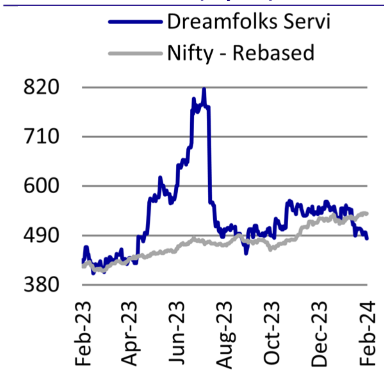
Y/E MARCH	FY24E	FY25E	FY26E
Sales	11.6	13.3	16.8
EBIT	0.9	1.2	1.5
PAT	0.7	0.9	1.2
EPS (INR)	13.2	16.6	21.6
EPS growth (%)	-1.2	25.6	30.5
BV/Sh (INR)	43.4	60.5	82.8
Valuations			
P/E (x)	36.8	29.3	22.5
P/BV (x)	11.2	8.0	5.9
RoE (%)	37.4	33.0	31.2
RoCE (%)	34.3	30.4	28.8

Shareholding pattern (%)

As On	Dec-23	Sep-23	Dec-22
Promoter	66.0	66.0	67.0
DII	9.2	6.1	8.7
FII	5.2	5.6	11.5
Others	19.5	22.2	12.8

FII Includes depository receipts

Stock Performance (1-year)



Landing gear retracted; charting a steep trajectory

International expansion – a multifold opportunity

DreamFolks (DFS) is India's leading airport services aggregator and tech platform, connecting lounges and premium airport facilities with users of bank credit/debit cards. DFS holds a 75%+ volume market share in domestic airport lounges and it is the only player with 100% coverage of airport lounges. DFS is the go-to partner for banks seeking to provide complimentary access to paid airport services lounge and this is a highly profitable and asset light model. We expect the company to benefit from the rapid growth in the Indian airline industry, driven by competitive fares, rising leisure travel, new airports, and government push. Further, the increasing adoption of bank card (with lounge access as a key benefit) is boosting the pay-per-use revenue model of DFS. This should help it deliver a strong 20% revenue/28% PAT CAGR over FY24E-26E, despite a high base, near-term setbacks due to revised airport charges, and a shift to the spending-based model. We see venturing into international markets as a lucrative long-term opportunity carrying significant potential value. We initiate coverage on the stock with a BUY rating at a TP of INR650, implying 34% potential upside.

Fast-growing air travel and card usage to boost lounge usage

- The Indian airline industry is still highly under-penetrated (0.13 passenger seats per capita as per CAPA) and is going through rapid expansion with growing air travel, rising class of leisure travelers, increasing number of airports, and government push under the UDAN scheme. With long-term tailwinds in place, the total number of passengers at Indian airports (International + Domestic) is expected to surge 9x to reach 1.2b by CY40 (Source: F&S).
- The growing adoption of bank cards also presents a substantial opportunity for DFS, particularly given that this segment constitutes its primary customer base. India, with its credit card penetration at a mere 3%, stands among the lowest rates globally for both developing and developed nations. We forecast ongoing growth in the cardholder base, thereby expanding DFS's accessible customer pool.

Asset-light business model, strong growth to drive earnings

- On the back of strong industry tailwinds, we expect Indian lounge access market to register a CAGR of 18% over FY23-26E. Along with growing market share (73% in FY26 vs. 68% in FY23) and increasing revenue per pax, DFS should deliver strong revenue growth (29% CAGR over FY23-26E).
- DFS's asset-light B2B business model and dominant market position enable it to expand without significant expenditure on consumer acquisition or marketing. This results in high profitability (69% of 3QFY24 gross profit converted into EBIT and 52% into PAT). We expect DFS gross margin to bottom out in FY24 at 12.2% (impact of one-time increase in airport charges) and recover to 13.0% in FY25, resulting in a healthy PAT CAGR of 18% over FY23-26E.
- The company operates an asset-light structure, with minimal incremental capital deployment despite fast-growing revenues. This has resulted in DFS generating high return ratios. We estimate an ROE/ROCE of 37%/34% in FY24E.

Market control and structural tailwinds to help tide near-term challenges

- DFS commands a dominant market share, holding over 95% of the card-based access to domestic airport lounges in India. In FY23, it accounted for around 68% of the total lounge access volumes across both domestic and international terminals in India.
- In FY23, there was a sharp increase in the lounge access, marking 132% YoY increase in the number of passengers. This sudden rise led to congestion problems in lounges across major cities, despite considerable expansion in capacity. Anticipating this trend to continue, we foresee further expansions in lounge capacity, especially with new airports coming into play. This should help alleviate the ongoing capacity issues.
- The record jump in air passengers accessing Indian lounges over the last two years (conversion rate doubled to 5.0% in FY23) should lead to near-term growth moderation as banks tweak offers to manage costs. We expect growth to rebound post a rebasing over the next few quarters, given structural tailwinds.
- The company experienced a margin impact in FY23 from an exceptional revision in CAM (common area maintenance) charges, following a pause during the pandemic. We do not anticipate this to recur, but remain watchful of any future changes.

International expansion provides large option value

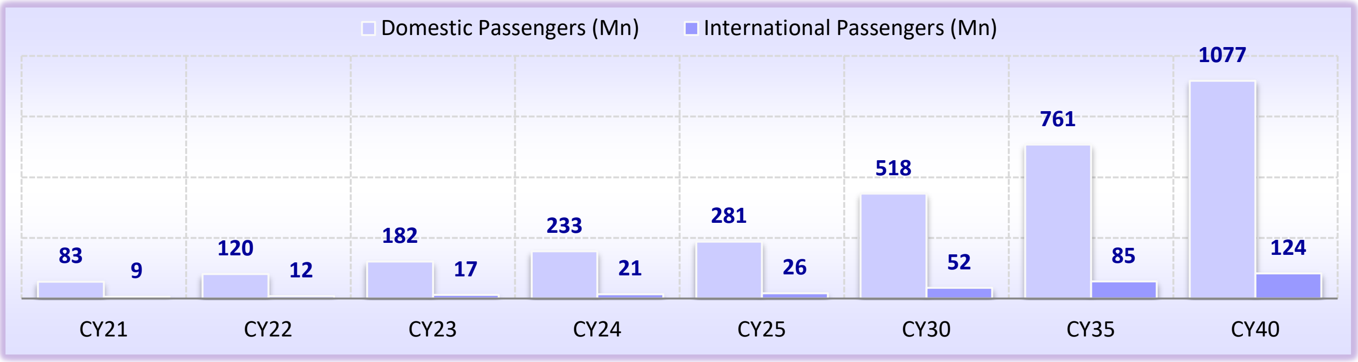
- Over the last decade, DFS has effectively disrupted the Indian market, overtaking existing players and securing a substantial market share. This can be attributed to the company's differentiated real-time reconciliation software compared to peers with legacy offerings, helping save time and streamline banking processes. DFS aims to replicate the success in other geographies with dominant legacy models.
- DFS has started to establish its presence internationally by setting up wholly owned subsidiary in Singapore and establishing partnerships in Malaysia.
- While we do not factor in any revenues from its international expansion, any success would meaningfully enlarge its customer base and disproportionately impact revenue and earnings growth. We see a significant option value in international expansion for DFS, which is not factored into current valuations.

Valuation and View: Initiate coverage with a BUY rating

- Given the strong industry tailwinds, we expect strong sustained growth for DFS over the medium term. We forecast a 29% revenue CAGR over FY23-26E.
- We expect DFS to deliver gross margin closer to the upper end of its 11-13% guidance range from FY25, after bottoming out in FY24 (at 12.2%). It can further improve (not factored in our estimate) as the share of other higher value services increase over the medium term. This should result in a healthy FY25/FY26 EBIT margin of 8.7%/8.9%, and a 18% PAT CAGR over FY23-26E (28% CAGR over FY24E-26E).
- We see a significant option value from the nascent expansion into international markets and diversifying into other sectors. This can significantly enhance the value of the business through an expansion of addressable customer base.
- With visibility of good earnings growth over the medium term and strong option value from the expansion plans, **we initiate coverage on DFS with a BUY rating and a TP of INR650 (premised on 30x FY26 P/E), implying a 34% upside potential.**

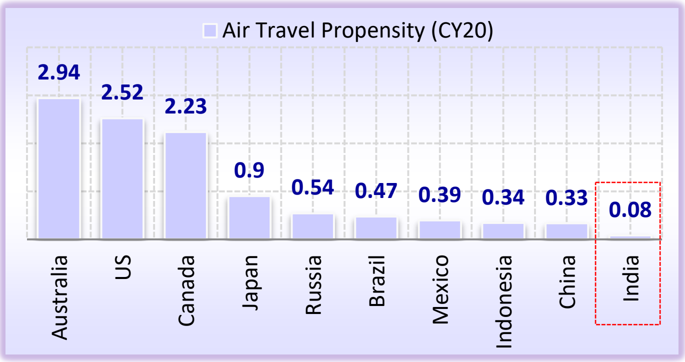
STORY IN CHARTS

Passengers travelling by airlines to increase exponentially going forward



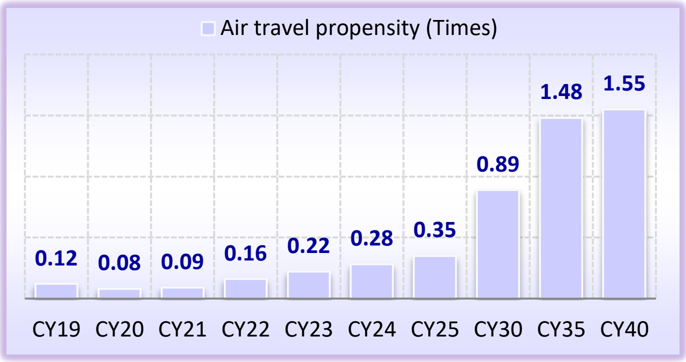
Source: MOFSL, F&S Report

India has one of the lowest air travel propensity…



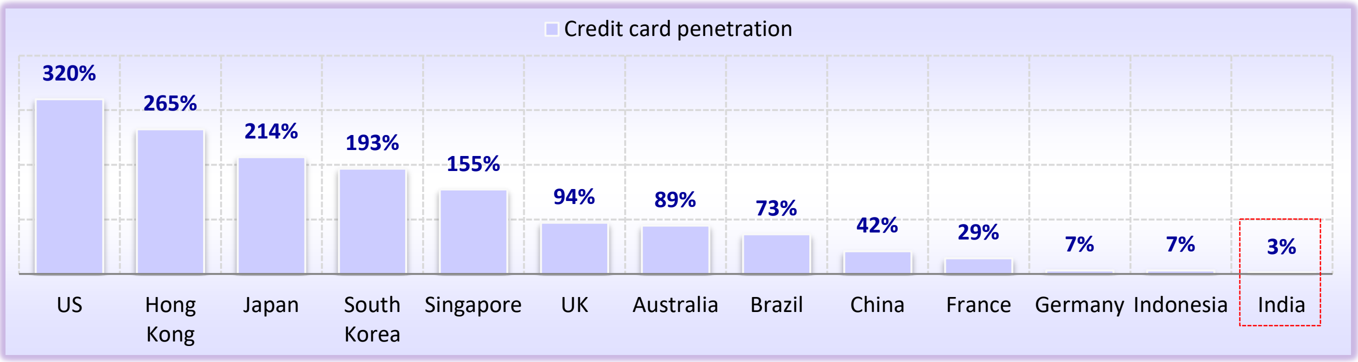
Source: MOFSL, F&S Report

…which presents massive opportunity ahead



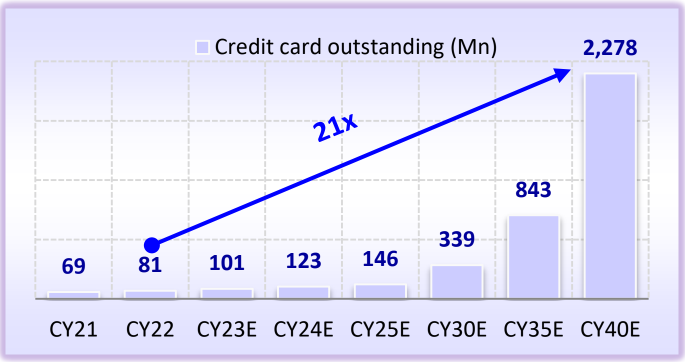
Source: MOFSL, Company

Credit card penetration remains the lowest among the developing and developed countries

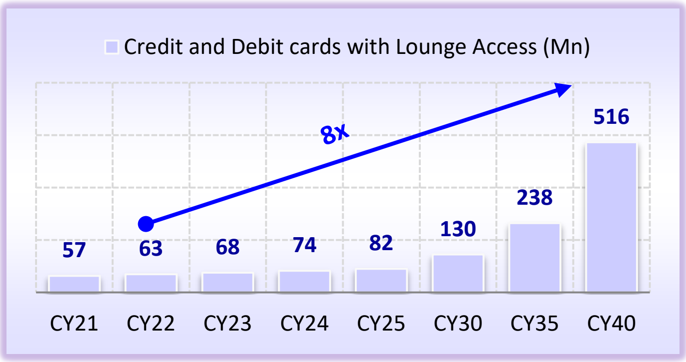


Source: MOFSL, F&S Report

Number of credit cards to massively increase…

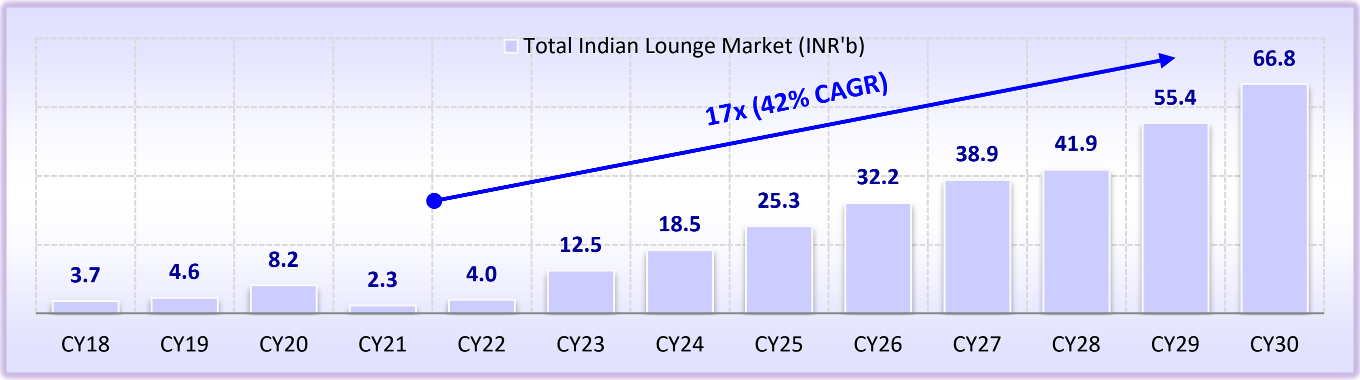


…resulting in an 8x increase in cards with lounge access



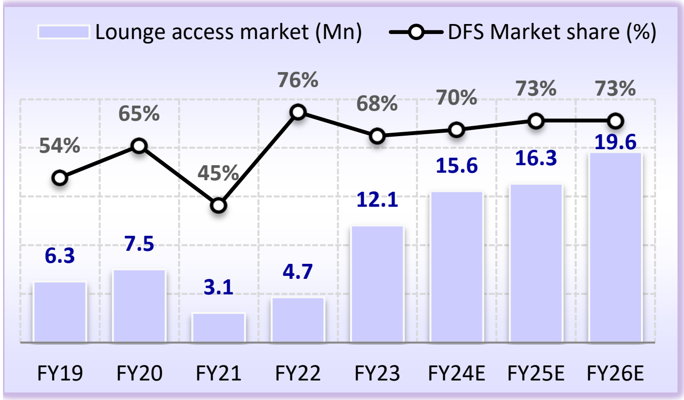
Source: MOFSL, F&S Report

Expansion of air travel and cards to result in a massive jump in Indian lounge market



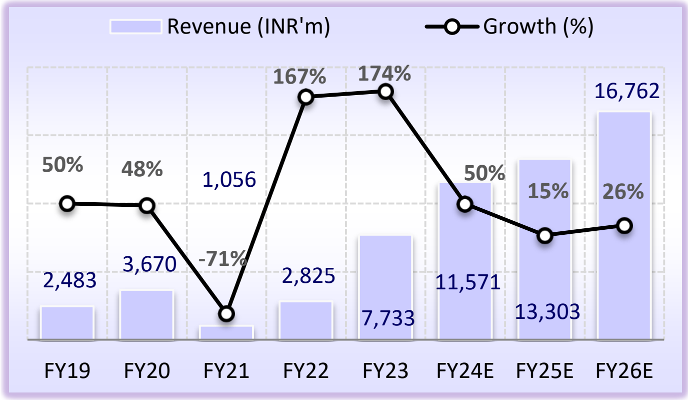
Source: MOFSL, F&S Report

Strong industry growth and increasing market share…



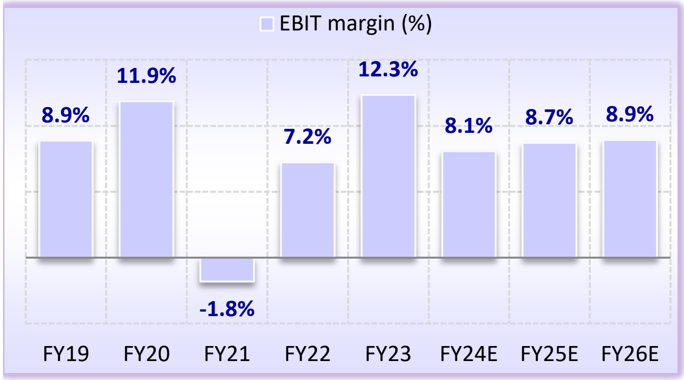
Source: MOFSL, Company

… to drive strong revenue growth



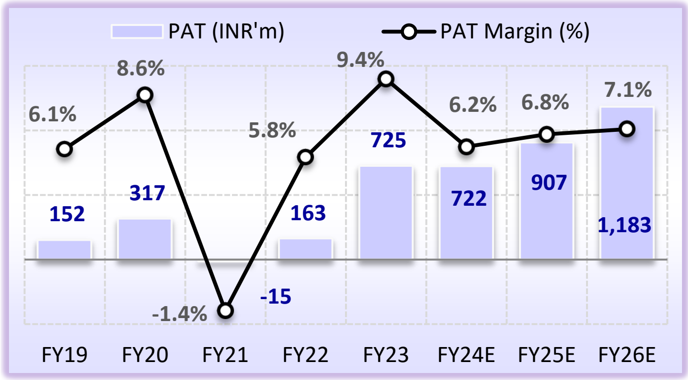
Source: MOFSL, Company

EBIT margin to stabilize post FY24 reset



Source: MOFSL, Company

PAT to register strong 17% FY23-26E CAGR



Source: MOFSL, Company

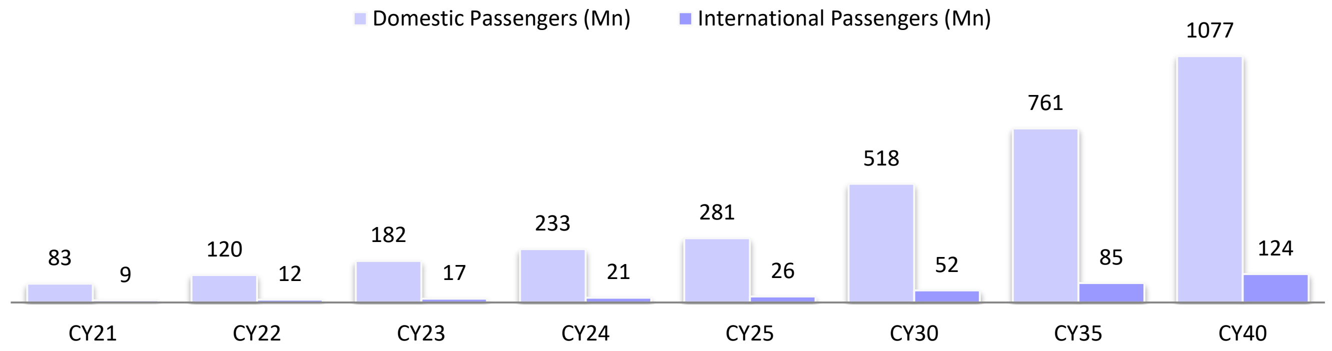
Air travel – ready to take off

Government's robust initiatives to fuel accelerated growth

The number of passengers (Domestic + International) is expected to grow 9x to reach 1.2b by CY40

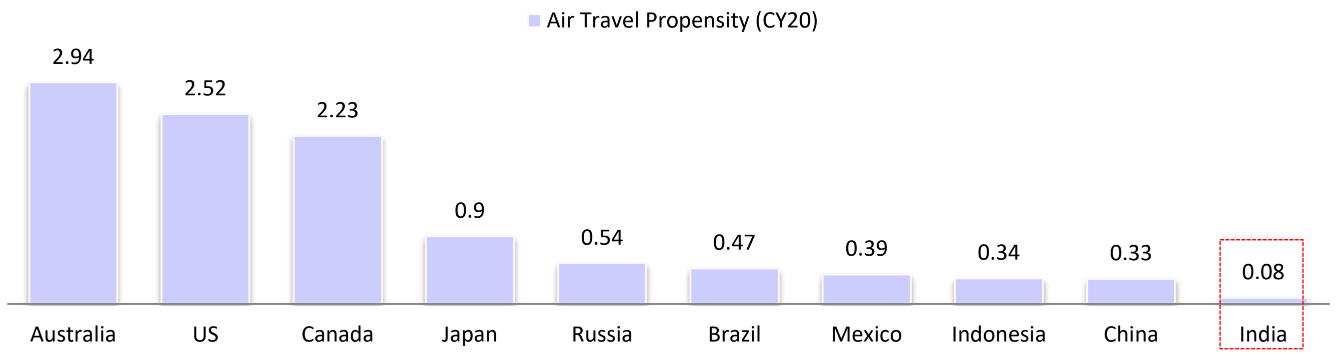
With increasing per capita income, larger demographic dividend, infrastructural developments, government initiatives, and strong GDP growth, Indian air travel is all set to grow at high sustainable growth rates over a longer period. The Indian airline industry is still under-penetrated and in a high growth phase with growing air travel, rising class of leisure travelers, competitive fares compared to AC railway coaches, increasing number of airports, and increased government push. The Indian aircraft fleet is expected to grow 3x and reach around 2,360 aircraft by CY40. Also, air travel propensity (0.16 in CY22 to 1.55 in CY40) will provide strong tailwinds to air travel in India. With the long-term tailwinds in place, the number of passengers (Domestic + International) is all set to grow 9x to reach 1.2b by CY40.

Exhibit 1: Passengers travelling by airlines to increase exponentially going forward



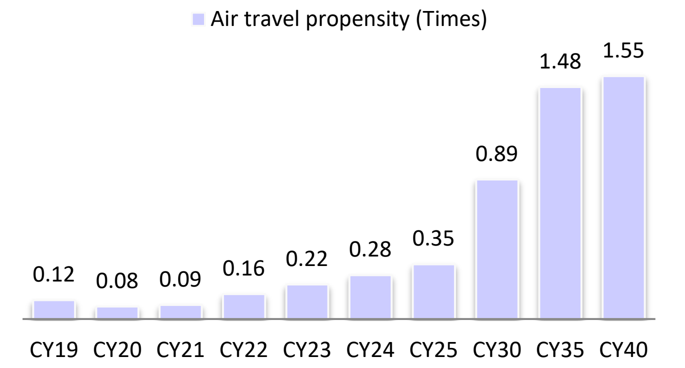
Source: MOFSL, F&S Report

Exhibit 2: With one of the lowest air travel propensity…



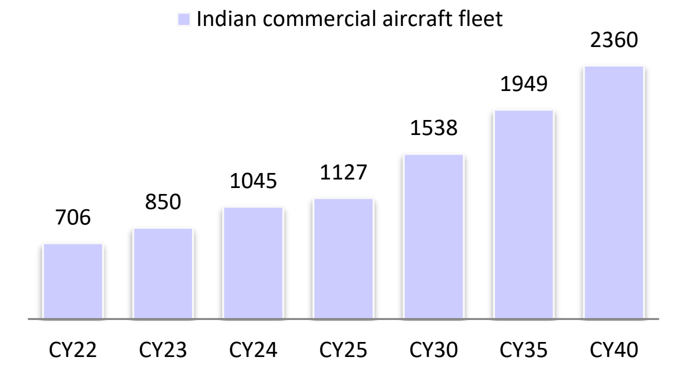
Source: MOFSL, F&S Report

Exhibit 3: …India presents massive opportunity ahead



Source: MOFSL, Company

Exhibit 4: India to add a large commercial aircraft fleet

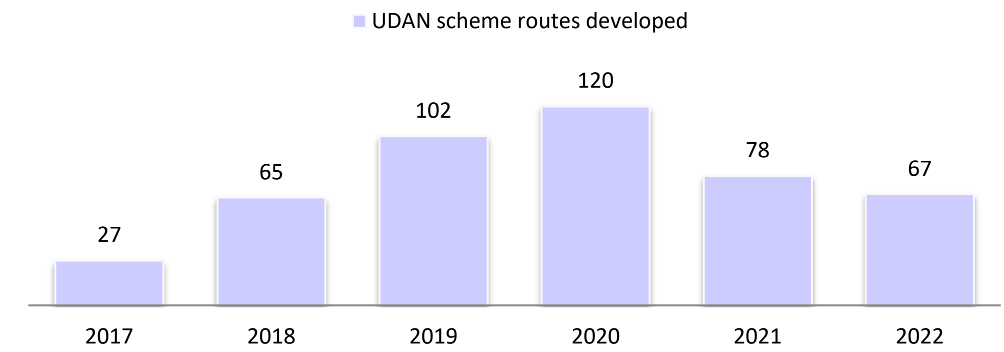


Source: MOFSL, Company

Strong push from government to further boost air traffic

There is a strong push from the government to support the airline industry through UDAN 5.0 (UdeDesh ka Aam Naagrik) scheme, establishing connections with airports that have been historically underserved. The underlying goal of the Regional Connectivity Scheme (RCS) is to enhance inter-regional connectivity by establishing air links between 70 airports, facilitated through 128 routes that are operated by five prominent airlines. The Ministry of Civil Aviation has approved 780 new air routes as part of the UDAN scheme for regional air connectivity. With 425 new routes initiated, UDAN has provided air connectivity to more than 29 States/UTs across the country. More than 10m passengers have already availed the benefits under this scheme. We expect the increased air travel to be followed by an increase in lounge setup and usage across the newer airports, and resulting in a larger customer base for DFS.

Exhibit 5: Routes developed under RCS UDAN scheme



Source: MOFSL, Company

Wider adoption of cards to boost lounge access market

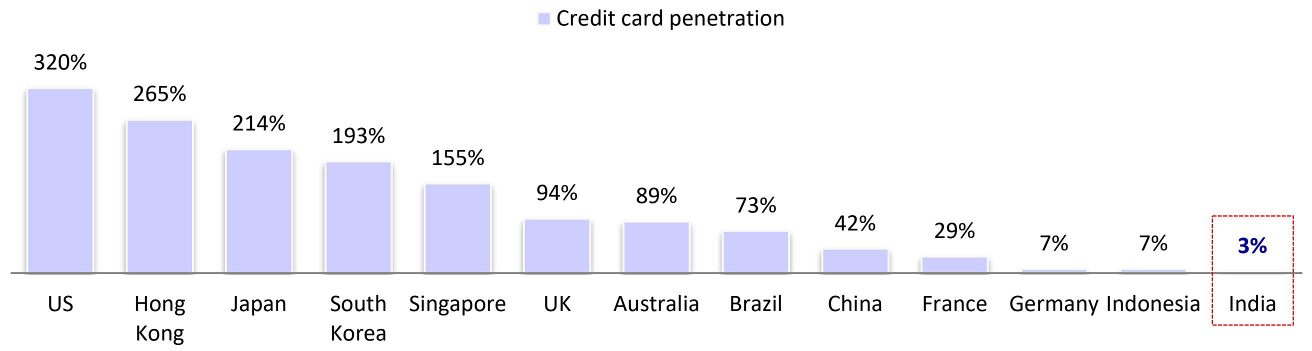
Untapped Market: Maximizing growth with low card penetration

Credit card penetration in India is minuscule (3%) compared to the US (320%)

Cards form an important part of the lounge access ecosystem. Banks reward card users with benefits to promote their card business. As part of their rewards, many banks offer complimentary airport lounge access to their premium card customers. Therefore, cards not only serve as a means to access lounges, but also boost lounge occupancy by providing rewards.

The card market in India is massively underpenetrated, presenting a vast opportunity for DFS to directly benefit from this untapped potential. India has one of the lowest credit card penetrations among developing and developed nations. Credit card penetration stood at just 3% vs. 320% in the US.

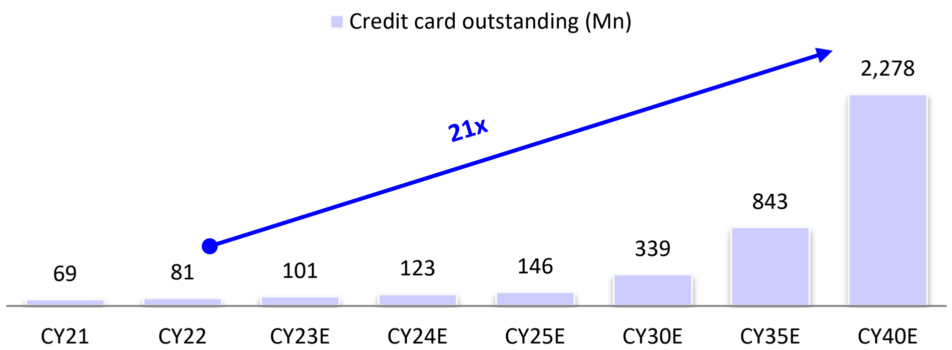
Exhibit 6: Credit card penetration remains the lowest among the developing and developed countries



Source: MOFSL, F&S Report

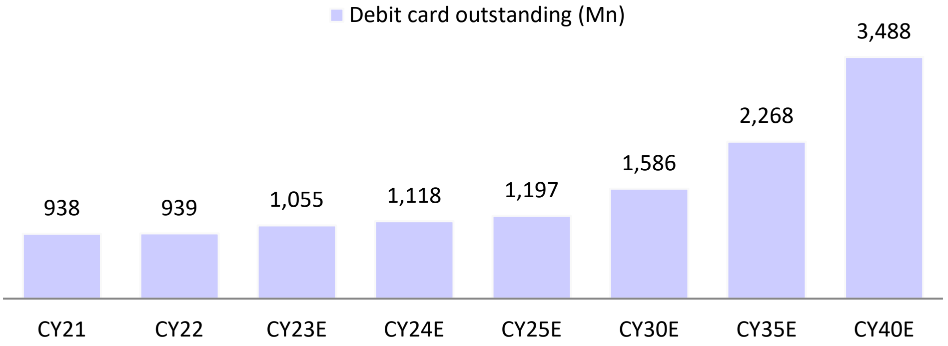
Low penetration, increasing digitalization, increasing e-commerce, urbanization, increasing propensity to spend, and availability of easy financing options are all leading to strong growth in the credit card market. The number of outstanding credit cards is all set to witness a very strong growth of 21x by CY40. At the same time, cards with complimentary access to lounges will see 8x growth. As this will increase the propensity to use lounges, DFS would be one of the beneficiaries of the same.

Exhibit 7: India to witness exponential surge in outstanding credit cards…



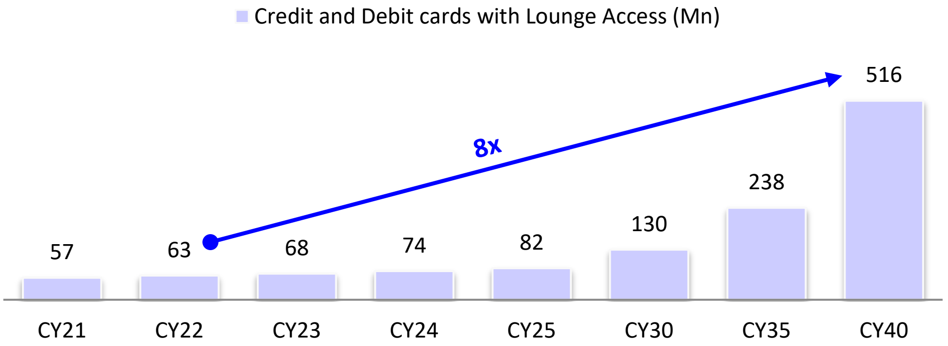
Source: MOFSL, F&S Report

Exhibit 8: and debit cards, which should translate to…



Source: MOFSL, F&S Report

Exhibit 9: …strong growth for cards with lounge access



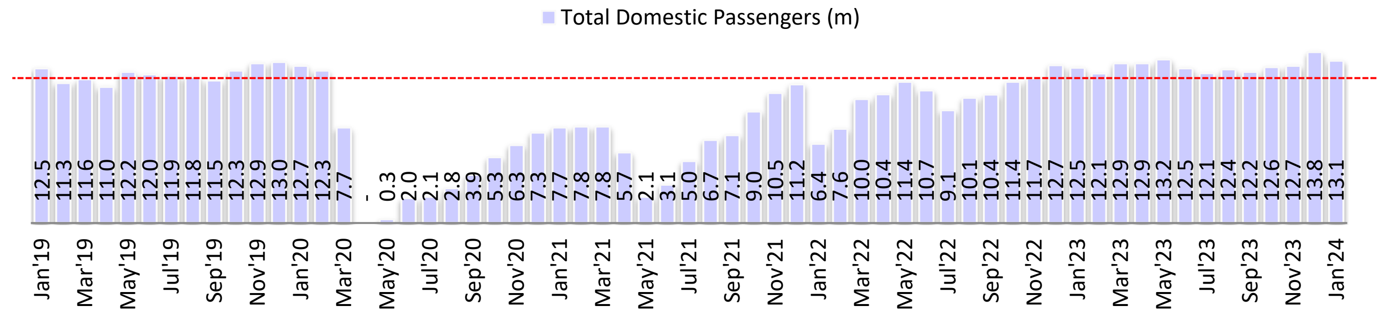
Source: MOFSL, F&S Report

Structural tailwinds to drive long-term industry growth

Lounge access is still in its early phase with a large untapped market

The aviation industry was heavily impacted by the pandemic-induced lockdowns. The domestic traffic plunged to zero in Apr'20 and saw sharp drops in May'21 and Jan'22 on consequent lockdowns. The domestic air traffic has now seen a sharp recovery and has already surpassed pre-Covid levels and expected to grow at healthy levels going forward.

Exhibit 10: Domestic air traffic has already surpassed the pre-Covid level

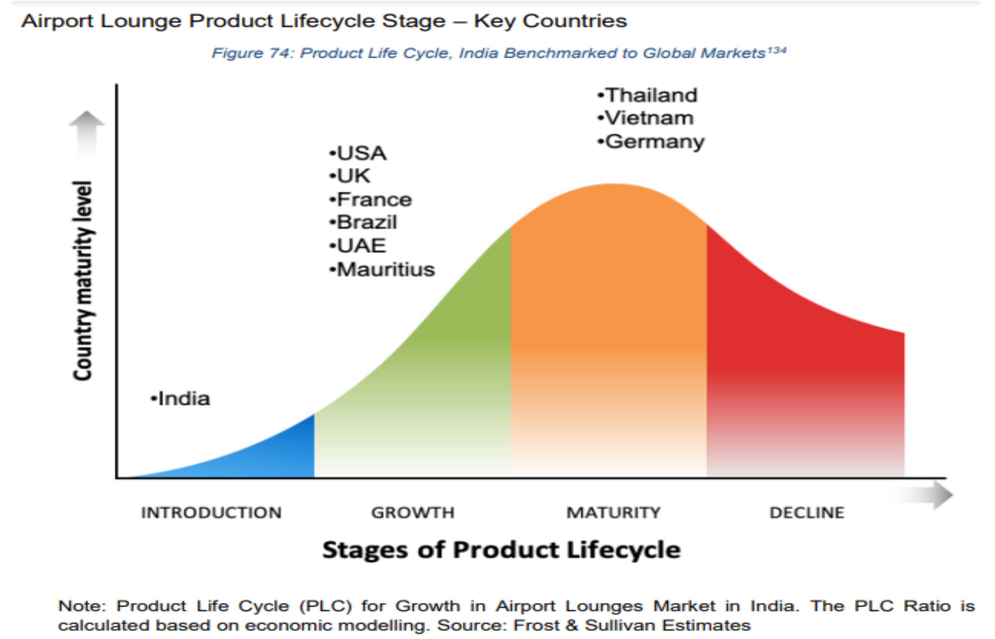


Source: MOFSL, DGCA

India is still in the introduction phase of airport lounges. The number of people using lounges is expected to grow exponentially going forward.

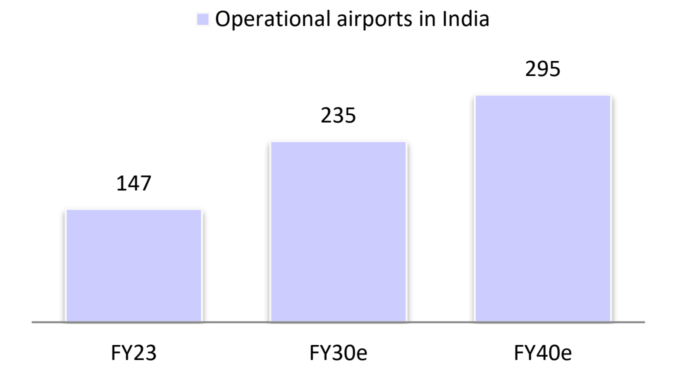
India is still in the introduction phase of airport lounges and is yet to witness structural long-term high growth (Exhibit 22). With strong expected growth in air travel and increasing popularity of cards, the number of people using lounges are expected to grow exponentially. Operational airports/Airport lounges are expected to reach 295/200 by FY40 vs. 147/61 in FY23. The average lounge size has increased to 17,914sq feet in CY21 from 2,169sq feet in CY14. With increasing air travel, the number and size of airport lounges will continue to increase.

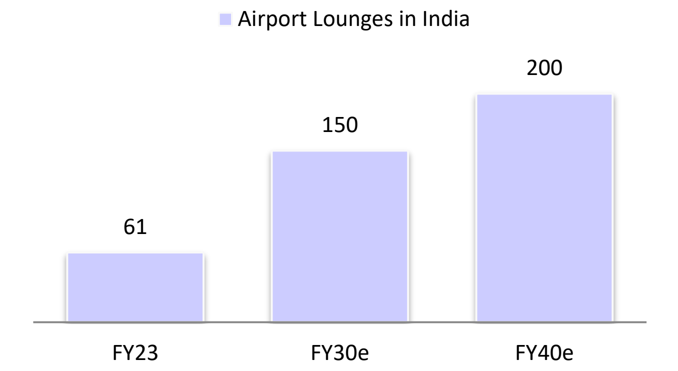
Exhibit 11: India is still in the introductory phase of airport lounges



Source: MOFSL, F&S report

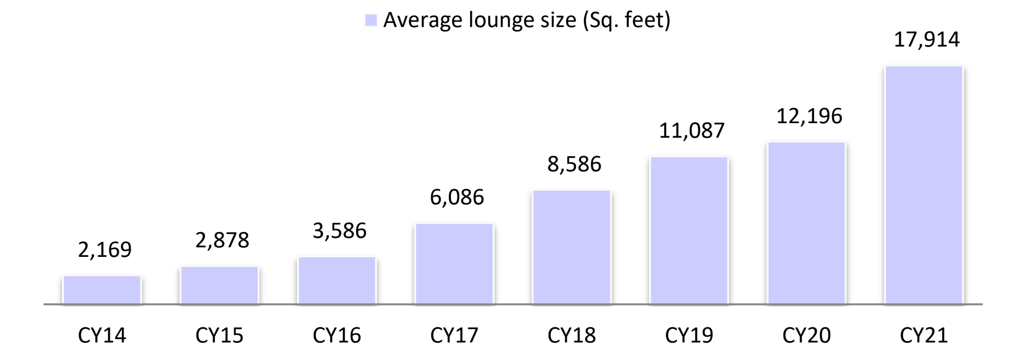
Exhibit 12: Operational airports and airport lounges to see **Exhibit 13: strong uptick going forward**





Source: MOFSL, Company

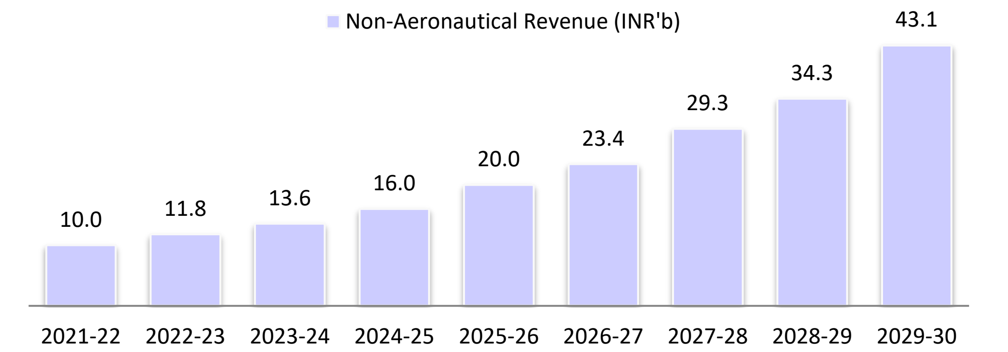
Exhibit 14: India has seen a massive increase in average lounge sizes over the last few years



Source: MOFSL, F&S Report

Airports are experiencing a notable rise in non-aeronautical revenue generated from ancillary services. Private airports such as Delhi, Mumbai, and Bengaluru have witnessed a significant range of 50%-70% (FY21) of their total revenue from non-aeronautical sources. However, non-aeronautical revenues from airports managed by AAI account for 10%-15% (FY21) of their overall earnings. This trend underscores how passengers are increasingly willing to invest in enhanced services, ultimately bolstering sectors like the lounge market and other retail expenditures by travelers. The trajectory suggests a continued upward trend in non-aeronautical revenue (including for lounges).

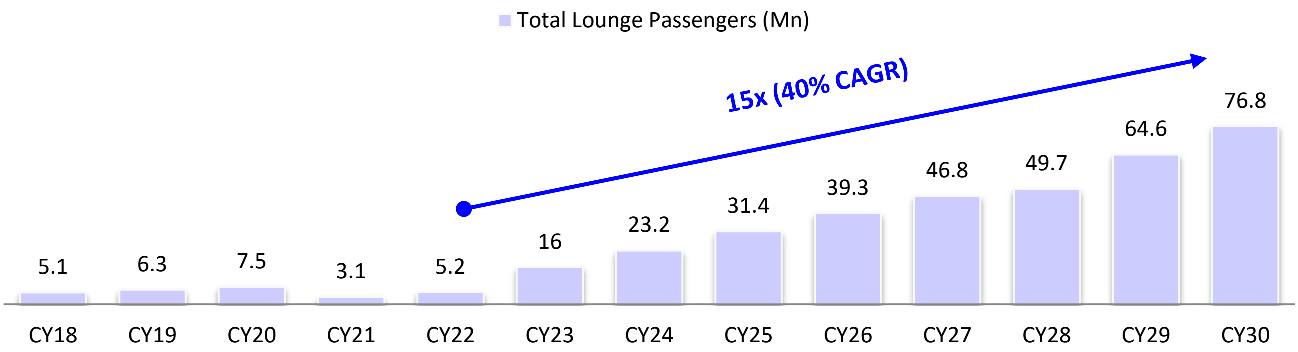
Exhibit 15: Non-aeronautical revenue is expected to see continued growth



Source: MOFSL, F&S

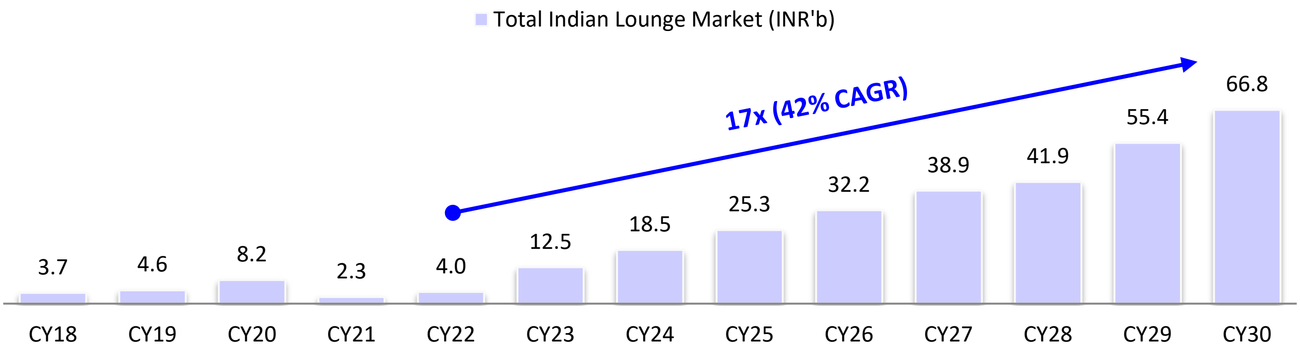
All-in-all, the airline industry is witnessing strong structural tailwinds on account of all the aforesaid discussed factors. The total number of people visiting lounges is expected grow 15x by CY30 (40% CAGR) and at the same time, the Indian lounge market is expected to grow at an exponential 17x by CY30 (42% CAGR). DFS will be the direct beneficiary of the strong growth in the lounge market going ahead.

Exhibit 16: With strong industry tailwinds, lounge passengers are expected to register a CAGR of 40% CY22-CY30…



Source: MOFSL, F&S Report

Exhibit 17: …which will translate to a strong 42% CAGR for the Indian lounge market over the same period



Source: MOFSL, F&S Report

Dominant player with a strong moat

Unlocking opportunities by expanding into new areas

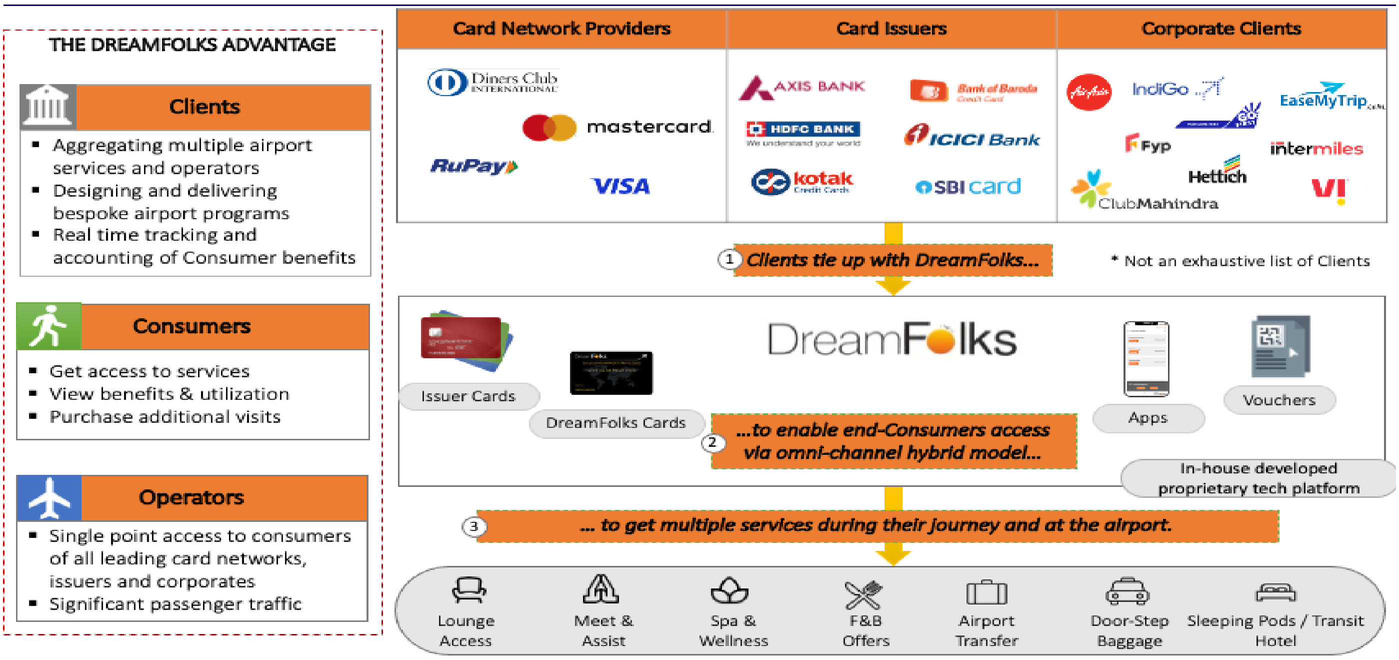
DreamFolks (founded in 2012-13) is a dominant player and India's largest airport service aggregator platform. It has an asset-light business model, which integrates global card networks, card issuers, and other corporate clients, including airline companies with various airport lounge operators and other airport-related service providers on a unified platform. It facilitates customers (of clients) access to - (i) lounges, (ii) food and beverage (iii) spa, (iv) meet and assist, (v), airport transfer, (vi) transit hotels /nap room access, and (vii) baggage transfer.

DFS enjoys over 95% airport lounge access through India-issued credit and debit cards (Card Based) and around 68% of the overall lounge access volume in India

Currently, it extends its coverage to all 58 operational lounges in India, encompassing 100% reach. It commands a dominant market share, accounting for over 95% airport lounge access through India-issued credit and debit cards (Card Based) and around 68% of the overall lounge access volume in India during FY23. It also has a global footprint extending to 1,500+ touch-points in 121 countries across the world.

Card networks and card issuers provide complimentary lounge access and access to other services to the consumers under eligible credit and debit cards programs, and DFS enables this access across services. It offers clients and consumers immediate access to transaction updates in real-time, which enhances transparency. This not only minimizes the risk of billing conflicts but also furnishes clients with a framework to execute targeted campaigns centered on usage patterns and expenditure.

Exhibit 18: Business Model

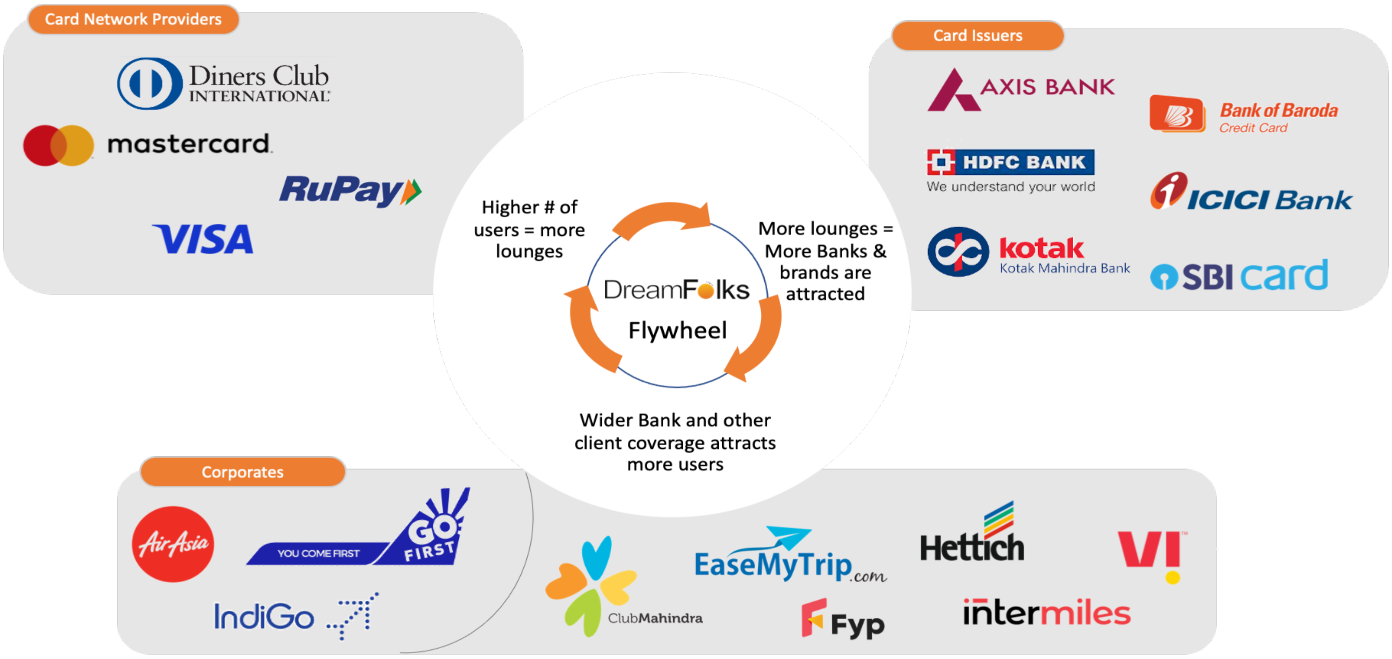


Source: Company

Strong business moat

Given its dominant position in the airport lounge access market, it has been successful in building a bridge between its clients and airport lounge operators. Its position in the industry enables it to create interdependencies for its service offerings, enabling it to attract newer clients and operators, which help it to further strengthen its position in the market.

Exhibit 19: Flywheel effect creates strong business moat



* Not an exhaustive list of Clients

Source: Company

For its clients, it provides comprehensive airport lounge coverage in India and a single-point access to all lounge operators in India. For banks, it provides a vital link to manage customer loyalty and retention/enables them to provide its customers value-added services as part of their customer engagement and loyalty management programs. Moreover, its platform is intricately integrated with the information technology systems of its clients, enhancing the stickiness of the business. Similarly, for lounge operators, it has tie-ups with all card networks with operations in India and some of India's largest card issuers facilitate a steady stream of lounge users being routed through it.

DFS is expanding its presence in newer industries which will not only unlock more opportunities but also help DFS reduce its exposure to airline industry.

Expansion to new areas to unlock more opportunities

DFS has acquired a 60% stake in golf club aggregator Vidsur golf clubs to capitalize on a growing golf market in the country and expand its portfolio of service offerings to include golf sessions and golf lessons. In Dec'22, DFS had announced its partnership with Vidsur golf to gain access to 40+ golf clubs in India and 1,800+ globally. With this acquisition, DFS gets access to global clients of Vidsur golf, which shall also help with its regional expansion plans.

Besides the golf sector, DFS is actively engaging with companies across various industries to expand its existing offerings, enabling enterprises to deliver comparable services to their clientele. These initiatives, though small, will not only help DFS to diversify and reduce concentration to the airline industry, but also provide potential opportunity in the form of future growth engines. Railway is another area where there is good long-term opportunity for DFS.

Exhibit 20: DreamFolks golf cup in collaboration with Vidsur Golf

Source: MOFSL, Company

Plaza premium partnership to help expand global reach

Recently, DFS also announced its collaboration with Plaza Premium, a global leading airport hospitality provider with the world's largest network of independent airport lounges. This collaboration is to include over 340 Plaza Premium Lounges in more than 70 major international airports into the DFS global lounge network, offering an enhanced travel experience to its members worldwide. This collaboration will facilitate an extensive coverage of Plaza Premium Lounges across four continents including key travel hubs, such as Australia, Canada, the United Kingdom, Hong Kong, Florida, Brazil, Italy, Indonesia, Malaysia, Singapore, Dubai, Saudi Arabia, and Jordan.

Shift to spend based model to trigger a needed reset

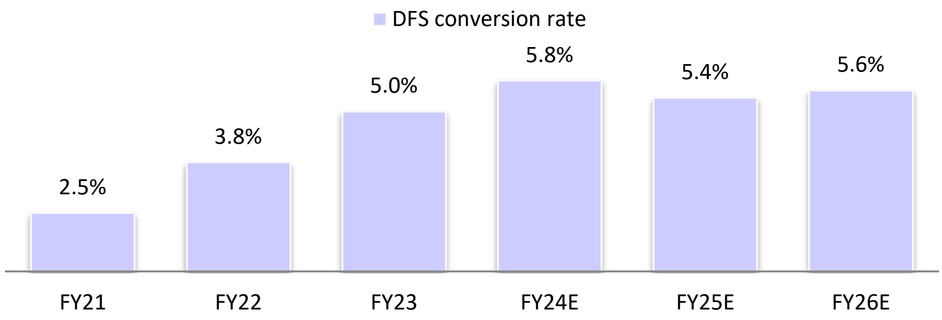
Expect strong sustainable growth post reset

Most of the card issuers are making a revamp in their reward mechanism where they are moving to a spend-based model. Under this model, the rewards are awarded based on fulfillment of certain spend criteria. Until now, many card issuers offered complimentary lounge access for cards beyond a low threshold and were surprised by the increase in the number of customers accessing lounges. With the shift to spend-based model, we expect a near-term adjustment in the number of air passengers accessing lounges (conversion rate).

In our opinion, the current lounge access volume growth is unsustainable in nature (DFS conversion rate moved from 4.6% to 6% over last six quarters) and shift to spend-based model would provide a structural rest for the industry, post which, the growth would be more sustainable in nature. Despite the near-term pain, this much needed reset should be positive for the ecosystem to sustain in the long run.

DFS has seen strong uptick in conversion rate from 4.6% to 6% over last six quarters. Expect some moderation going forward as issuers move to a spend based model.

Exhibit 21: DFS may see some moderation in conversion rate after peaking in FY24



Source: MOFSL, Company data

DFS, in its 3QFY24 earnings call, warned about near-term impact of change to spend-based model by card issuers on lounge access volumes. Though this likely would have an impact in the near term, the management suggested that its commentary was conservative and it saw no material impact from few issuers who have already moved to a spend-based model.

Our discussion with the management suggested that premium cards drive a large portion of lounge access volumes. As, initially, only lower-end cards would move to a spend-based model, the impact is likely to be gradual in nature. Also, in the near term, as the issuers move to a spend-based model, customers are likely to switch to other players who would still be offering those benefits. This should provide a near-term cushion. We expect near-term impact, post which, the industry should continue to see a healthy growth.

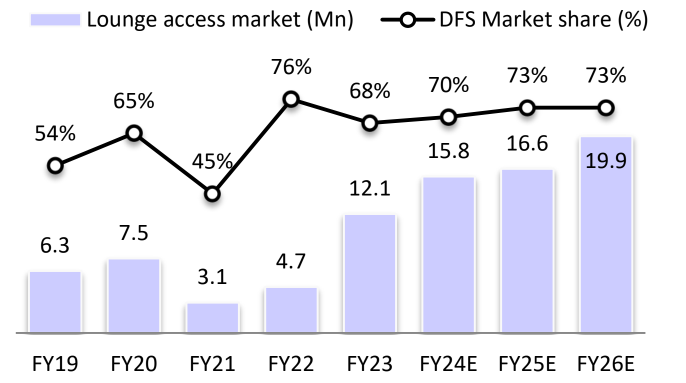
Strong growth and stable margins to drive earnings

Asset-light model with strong operating leverage

After registering a CAGR of 75% over FY16-20, DFS revenues faced a decline of 72% in FY21 due to the impact of Covid-related restrictions on air travel. However, there was a recovery in revenue during FY22, demonstrating resilience and ultimately reaching a robust INR7.7b in FY23 (>2x of pre-Covid levels of FY20).

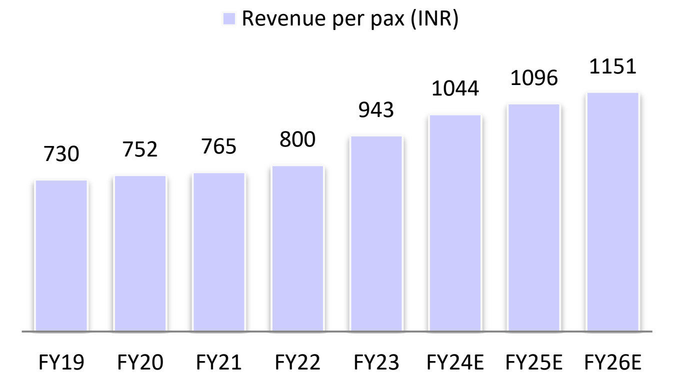
Although there will be some near-term pressure owing to the transition to the spend-based model, we expect lounge access market to register a CAGR of 17.6% over FY23-26E, primarily driven by strong industry tailwinds. With increasing market share (73% in FY26 vs. 68% in FY23) and increasing revenue per pax (INR1,151 in FY25 vs. INR943 in FY23), DFS should register faster growth in revenue. We expect DFS to deliver revenue CAGR of 29% over FY23-26E.

Exhibit 22: Increasing share in growing market and…



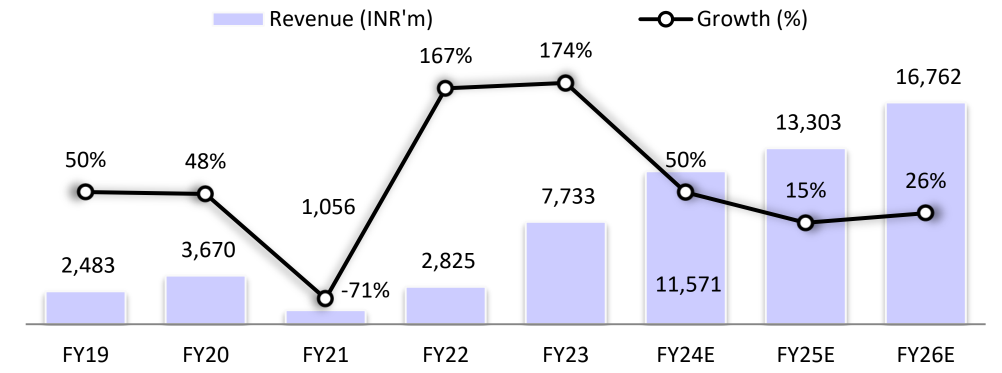
Source: MOFSL, Company

Exhibit 23: …increasing revenue per pax…



Source: MOFSL, Company

Exhibit 24: …to drive 29% revenue CAGR for DFS over FY23-26E



Source: MOFSL, Company

Strong operating leverage and asset-light business model

DFS, given its business model, is able to grow its consumer base of air traffic passengers and card users without incurring any consumer acquisition cost as the consumer acquisition is done by its clients as part of its loyalty programs. This ability to scale revenues without incurring any direct costs leads to strong operating leverage for DFS.

The business model is also asset-light and requires minimal incremental capital deployment with growing revenues. The business model is not human resource intensive. As on FY23, work force comprised 60+ employees. Strong operating leverage and asset-light nature of the business help DFS deliver extraordinary return ratios (FY24E ROE – 37%).

Gross margin reset due to one-time hit from CAM charges increase

After a strong FY23, DFS gross margin (share of lounge access payment by customers post payout to lounges) was impacted by a large one-time increase in common area maintenance (CAM) charges at airports. During the three-year hiatus caused by the COVID-19 pandemic, the DGCA (India's aviation authority) granted airports the leeway to impose an unprecedented 200% increase in CAM charges. This increase was allocated between lounges and DFS, yet DFS successfully negotiated to significantly mitigate its impact. This has resulted in DFS gross margins declining from 16.5% in FY23 to 12.2% in FY24 (estimated), with management guiding for a wider band of 11-13%.

While we remain watchful of any future changes in airport charges, we currently see a low probability of similar revisions in future, given the one-off nature of the pause followed by the increase. Going forward, as the share of other high value services increase, we see a possibility of gross margins improving from current levels. We expect DFS gross margin to bottom out in FY24 at 12.2% and recover to 13.0% in FY25.

Exhibit 25: Gross margin to see a reset in the near term…

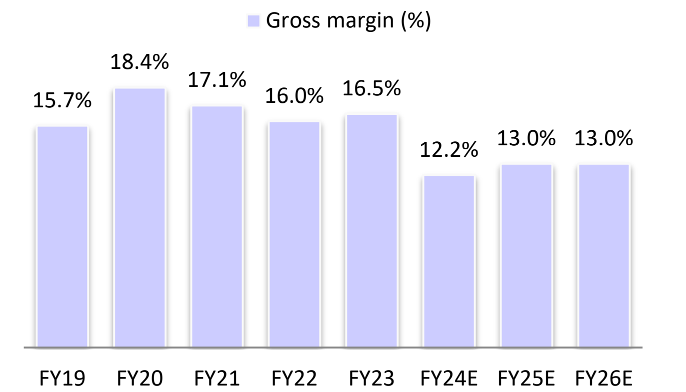
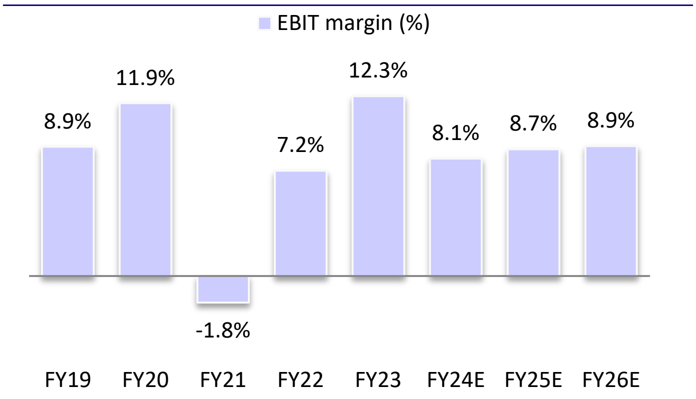


Exhibit 26: …which is passing down to EBIT margin as well

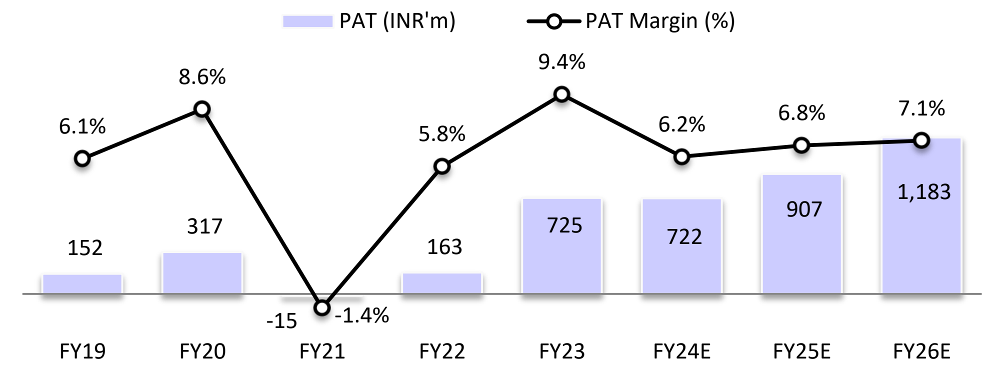


Source: MOFSL, Company

Low operating costs help drive majority of gross profits into earnings

DFS asset-light B2B business model and market leadership allows it to grow without incurring any meaningful consumer acquisition or marketing costs. This results in high profitability (69% of 3QFY24 gross profit converted into EBIT and 52% into PAT). Strong growth (29% CAGR over FY23-26E) and gradual margin recovery should help DFS drive a 18% PAT CAGR over FY23-26E and 28% CAGR over FY24E-26E.

Exhibit 27: Earnings growth to remain strong at 18% CAGR over FY23-26E



Source: MOFSL, Company

International expansion provides large option value

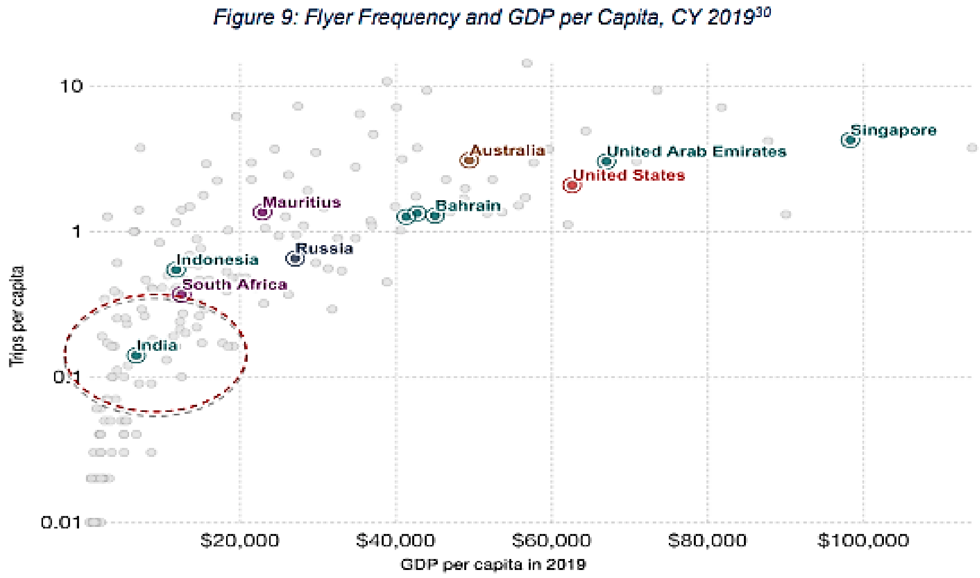
Easily scalable business model without the need of high Capex

DFS has already started to establish its presence internationally by setting up wholly owned subsidiary in Singapore and a lounge partnership in Malaysia.

After gaining success in displacing existing players in India and gaining large market share, DFS plans to replicate the success in other geographies. DFS has already started to establish its presence internationally by setting up wholly owned subsidiary in Singapore, which will support its expansion plans in CEMEA (Central and Eastern Europe, Middle East and Africa) and South East Asia. As the business model is asset light, it would not require large investments and would fund any investments needed with internal cash flows.

We recognize a strong opportunity for international expansion for DFS, as it can leverage its remarkable success in India. With a proprietary platform at its core, established relationships with domestic and international clients and card issuers, and a business model that is highly replicable and scalable without necessitating substantial additional investments, the prospect holds significant value. International expansion would meaningfully widen the revenue prospects which would have a disproportional impact on earnings with a lean operating model.

Exhibit 28: Flyer frequency data suggests long runway ahead



Source: MOFSL, F&S

DFS has started to establish its presence internationally by setting up wholly owned subsidiary in Singapore and establishing partnerships in Malaysia. While we do not factor in any revenues from its international expansion, any success would meaningfully enlarge its customer base and disproportionately impact revenue and earnings growth. We see a significant option value in international expansion for DFS, which is not factored into current valuations.

Strong growth and profitability at attractive valuation; Initiate with BUY

Given the strong industry tailwinds, we expect strong sustained growth for DFS over the medium term. We forecast a strong 29% revenue CAGR over FY23-26E. We expect DFS to deliver gross margin near the upper end of its 11-13% guidance range from FY25, after bottoming out in FY24 (at 12.2%). It can further improve (not factored in our estimate) as the share of other higher value services increase over the medium term. This should result in a healthy FY25/FY26 EBIT margin of 8.7%/8.9%, and a 18% PAT CAGR over FY23-26E (28% CAGR over FY24E-26E).

We see a significant option value from the nascent expansion into international markets and diversifying into other sectors. This can significantly enhance the value of the business through an expansion of addressable customer base.

With visibility of good earnings growth over the medium term and strong option value from the expansion plans, we initiate coverage on DFS at a BUY rating with a TP of INR650, implying a 34% upside potential. Our target price is based on 30x our FY26 EPS.

Bull & Bear cases

Bull case

- ☑ In our bull case analysis, we factor in a faster ~34% Revenue CAGR over FY23-26E, driven by higher traffic and better realizations.
- ☑ We also expect higher gross margins at 13.5% for FY24 and FY25, which translate to 9.3/9.7% EBIT margin for FY24/FY25.
- ☑ This should drive a PAT CAGR of 25% over FY23-26E.

Bear case

- ☑ In our bear case analysis, we factor in a slower ~20% Revenue CAGR over FY23-26E, factoring in slower growth in air traffic and realizations.
- ☑ We also expect lower gross margins at 12.2% for FY24 and FY25, which translate to 7.5% EBIT margin for FY24 and FY25.
- ☑ This should drive PAT CAGR of 4% over FY23-26E.

Exhibit 29: Scenario analysis – Bull case

INR b	FY24E	FY25E	FY26E
Sales	11.3	13.9	18.6
EBIT	0.9	1.3	1.8
PAT	0.7	1.0	1.4
EPS (INR)	12.8	18.5	25.9
EPS growth (%)	-4.4	44.9	40.0
RoE (%)	36.4	36.5	35.5
RoCE (%)	33.4	33.7	32.9
Target price (INR)			**880**
Upside (%)			**81**

Source: MOFSL, Company

Exhibit 30: Scenario analysis – Bear case

INR b	FY24E	FY25E	FY26E
Sales	11.3	11.7	13.5
EBIT	0.9	0.9	1.0
PAT	0.7	0.7	0.8
EPS (INR)	12.8	12.7	14.8
EPS growth (%)	-4.4	-0.9	16.8
RoE (%)	36.4	26.5	24.0
RoCE (%)	33.4	24.2	21.9
Target price (INR)			**450**
Upside (%)			**-7**

Source: MOFSL, Company

SWOT analysis

STRENGTH

- Dominant player in the airport lounge aggregation industry in India with strong tailwinds.
- Entrenched relationships with marquee Clients and strong business moat due to the flywheel effect led by Clients and Operators network.
- Asset and human resource light business model.

WEAKNESS

- The business is dependent on the success of the travel industry.
  - At present, its operations are solely confined to the Indian market.

OPPORTUNITY

- There exists a substantial opportunity to penetrate international markets, given the highly replicable and scalable nature of the business model.
- Following the success in the golf sector, diversifying into various other industries could potentially unlock significant growth opportunities in the medium term.

THREAT

- RBI has invited views to cap MDR on credit cards, which could directly impact revenues for DFS.
- Rising air fares could dampen the volumes.
- There's a potential risk of a competitor disrupting the current monopoly

Key management personnel

Liberatha Kallat – Founder & MD

- Liberatha holds a Bachelor in Science from Andhra University. She has experience in the hospitality sector. She has been associated with the Company since 2014 and is responsible for the strategy and overall management of the company.
- She has, in the past, been associated with Indian and global multinational companies such as Indian Hotels Company Limited, PepsiCo. India, Plaza Premium, and Pernod Ricard India (P) Limited.

Balaji Srinivasan – CTO

- Balaji holds a Diploma in Software and Systems Management from NIIT, New Delhi. He has been associated with the Company since 2019. He has experience in the technology sector.
- Prior to joining the Company, he held senior management positions at start-up ventures such as FarEye and also held the position of Vice-President at Genpact India Private Limited.

Giya Diwaan - CFO

- Giya is an alumna of Indian Institute of Management, Lucknow, and a fellow member of the Institute of Chartered Accountants of India. She has significant experience in business operations, corporate finance, accounting and strategy across fintech, internet commerce, and consumer technology companies.
- Prior to joining the Company, she was associated with Times Internet Limited as Chief Strategy Officer (Dineout), Musafir.com as Country Head-India, Awfis as Chief Financial Officer, Itz Cash Card Limited (as it then was) and Resources Global Professionals (India) Private Limited.

A strong ESG profile

- **No physical foot print –** DFS, a software company, specializes in offering lounge access and various services to its clients' customers. Notably, DFS operates solely in the digital realm, possessing no physical infrastructure. As a result, its operations have a negligible environmental impact.

- **Comprehensive ESOP coverage** – Along with other benefits offered to the employees, DFS has comprehensive ESOP pool coverage for its employees. This helps employees to take part in the success journey of the DFS.

- **High on corporate governance** – DreamFolks has a good share of woman leaders in KMP with Liberatha leading the show. Though the company had made a non-operational real-estate investment with a related party when it was held private, DFS has already reversed the same during the IPO and currently does not have any such related party transactions.

Key Risks

High dependence on Travel Industry

DFS is inordinately reliant on the air travel industry for its business. The travel industry is also generally affected by various factors such as increase in the fuel price, government policies applicable, in particular, to the airline industry, failure of airlines, etc. Any downturn in the travel industry, in general, and in the air travel industry, in particular, could adversely impact DFS.

Business is dependent on new and existing Cards

While consumers can avail of the services facilitated by the company through either card-based transactions or through digital access, DFS is heavily dependent on consumers using credit card or debit card to avail the services. Growth in alternative payment options such as mobile payment platforms may also affect usage of credit cards and debit cards. Continuing increase in cash spending, coupled with digital transactions, including UPI could impact the relevance of credit cards and debit cards.

Potential saturation of Indian markets

DFS is dominant player in India with a share of over 95% of all-India issued credit card and debit card access to airport lounges in FY23. In light of its expansion ambitions, DFS could potentially face challenges due to market saturation in India. This saturation might impede the company's growth prospects, necessitating a substantial push into global markets to sustain its growth trajectory.

Threat of increase in airport operator charges and forward integration

With the unprecedented increase in CAM charges in FY24, there is a risk of ongoing escalation in airport charges, which will negatively impact the gross margins of DFS. Moreover, with airports in India consolidating under a few private operators, they can establish direct partnerships with banks and this could lead to the risk of margin squeeze for DFS.

Financials and valuations

Consolidated - Income Statement

(INR m)

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Sales	**3,670**	**1,056**	**2,825**	**7,733**	**11,571**	**13,303**	**16,762**
Change (%)	47.8	-71.2	167.4	173.7	49.6	15.0	26.0
Service Charge Expenses	2,996	875	2,373	6,454	10,159	11,574	14,583
Gross Profit	**675**	**181**	**452**	**1,279**	**1,412**	**1,729**	**2,179**
% of Net Sales	18.4	17.1	16.0	16.5	12.2	13.0	13.0
Employee benefit expense	179.3	126.4	165.5	174.4	293.4	352.9	415.4
Other Expenses	45	58	61	115	145	173	218
EBITA	**451**	**-4**	**225**	**989**	**974**	**1,204**	**1,546**
% of Net Sales	12.3	-0.4	8.0	12.8	8.4	9.0	9.2
Depreciation	16	16	21	35	40	47	50
EBIT	**435**	**-19**	**204**	**954**	**933**	**1,157**	**1,495**
% of Net Sales	11.9	-1.8	7.2	12.3	8.1	8.7	8.9
Other Income (net)	1	17	1	20	36	60	92
PBT	**436**	**-2**	**205**	**974**	**969**	**1,217**	**1,588**
Tax	119	12	42	249	247	310	405
Rate (%)	27.3	-621.4	20.6	25.6	25.5	25.5	25.5
PAT	**317**	**-15**	**163**	**725**	**722**	**907**	**1,183**
Change (%)	108.0	NA	NA	346.3	-0.5	25.6	30.5

Consolidated - Balance Sheet

(INR m)

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Share capital	48	48	105	105	105	105	105
Reserves	608	595	717	1,467	2,189	3,096	4,278
Net Worth	**655**	**643**	**822**	**1,572**	**2,294**	**3,200**	**4,383**
Loans	20	13	10	9	9	9	9
Other long term liabilities	22	82	81	86	81	76	71
Capital Employed	**697**	**738**	**913**	**1,667**	**2,383**	**3,285**	**4,463**
Net Block	**59**	**112**	**94**	**84**	**89**	**96**	**113**
Intangibles	1	3	45	40	40	40	40
Other LT assets	153	490	268	87	199	305	416
Curr. Assets	**1,165**	**620**	**1,280**	**3,019**	**4,375**	**5,476**	**7,210**
Debtors	685	395	907	2,019	2,695	3,098	3,904
Cash & Cash Equivalents	321	100	11	190	496	942	1,567
Bank Balance	0	0	135	623	823	1,023	1,223
Other Current Assets	158	124	228	187	361	413	517
Current Liab. & Prov	**680**	**488**	**774**	**1,563**	**2,320**	**2,632**	**3,316**
Net Current Assets	**484**	**132**	**506**	**1,456**	**2,054**	**2,844**	**3,894**
Application of Funds	**697**	**738**	**913**	**1,666**	**2,382**	**3,284**	**4,462**

Financials and valuations

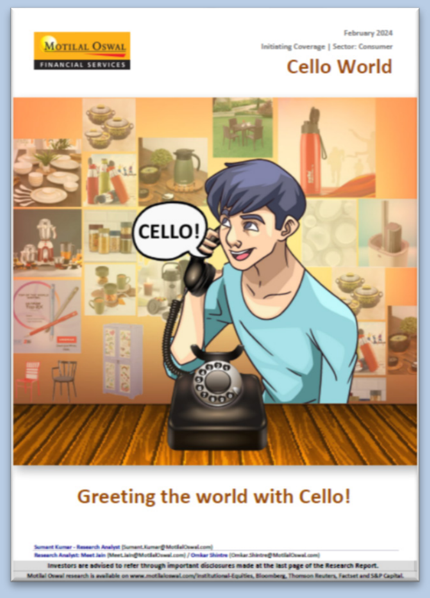
Ratios

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
EPS	**6.1**	**-0.3**	**3.0**	**13.4**	**13.2**	**16.6**	**21.6**
Cash EPS	6.4	0.0	3.5	14.6	14.4	18.0	23.3
Book Value	12.5	12.4	15.7	30.1	43.4	60.5	82.8
DPS	0.0	0.0	0.0	0.0	0.5	1.0	2.0
Payout %	0.0	0.0	0.0	0.0	3.8	6.0	9.2
Valuation (x)							
P/E	80.2	NA	163.1	36.4	36.8	29.3	22.5
Cash P/E	76.4	NA	138.2	33.4	33.7	27.0	20.9
EV/EBITDA	55.7	NA	112.6	25.5	25.9	20.6	15.6
EV/Sales	6.8	23.7	9.0	3.3	2.2	1.9	1.4
Price/Book Value	38.8	39.1	30.9	16.2	11.2	8.0	5.9
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.1	0.2	0.4
Profitability Ratios (%)							
RoE	63.6	(2.2)	22.2	60.6	37.4	33.0	31.2
RoCE	59.7	(19.4)	19.6	55.1	34.3	30.4	28.8
Turnover Ratios							
Debtors (Days)	68	137	117	95	85	85	85
Fixed Asset Turnover (x)	61.9	9.4	30.1	92.2	129.7	138.8	148.9

Consolidated - Cash Flow Statement (INR m)

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
CF from Operations	293	17	164	833	726	893	1,141
Cash for Working Capital	-69	45	-286	-337	-204	-249	-336
Net Operating CF	**224**	**63**	**-121**	**496**	**522**	**644**	**805**
Net Purchase of FA	-71	-282	191	51	-46	-53	-67
Free Cash Flow	**153**	**-220**	**69**	**547**	**476**	**591**	**738**
Net Purchase of Invest.	74	14	-132	-346	-154	-127	-91
Acquisition of subsidiary	0	0	0	-8	0	0	0
Net Cash from Invest.	**3**	**-269**	**59**	**-302**	**-200**	**-180**	**-158**
Proceeds from LTB/STB	10	-11	-7	-3	0	0	0
Others	-3	-5	-19	-18	-15	-18	-22
Cash Flow from Fin.	**7**	**-15**	**-26**	**-21**	**-15**	**-18**	**-22**
Net Cash Flow	**234**	**-221**	**-89**	**174**	**307**	**446**	**625**
Opening Cash Bal.	**87**	**321**	**100**	**16**	**190**	**496**	**942**
Add: Net Cash	234	-221	-89	174	307	446	625
Closing Cash Bal.	**321**	**100**	**11**	**190**	**496**	**942**	**1,567**

RECENT INITIATING COVERAGE REPORTS


MOTILAL OSWAL FINANCIAL SERVICES

February 2024

Initiating Coverage | Sector: Consumer

Cello World

Greeting the world with Cello!

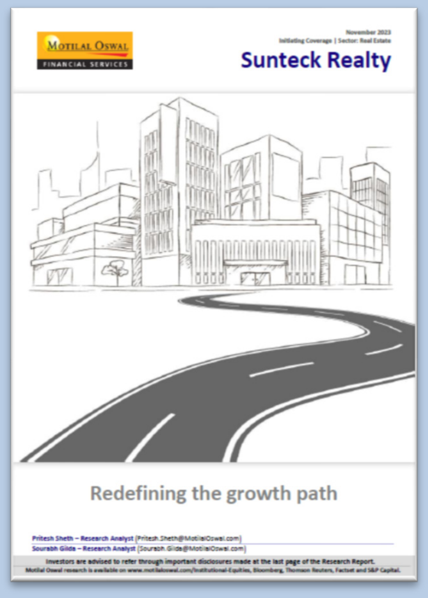

MOTILAL OSWAL FINANCIAL SERVICES

January 2024

Initiating Coverage | Sector: NBFC

IIFL Finance

Mastering the asset-light model for sustained profitability


MOTILAL OSWAL FINANCIAL SERVICES

November 2023

Initiating Coverage | Sector: Real Estate

Sunteck Realty

Redefining the growth path


MOTILAL OSWAL FINANCIAL SERVICES

October 2023

Initiating Coverage | Sector: Ports and Logistics

Adani Ports & SEZ

Sailing towards new horizons

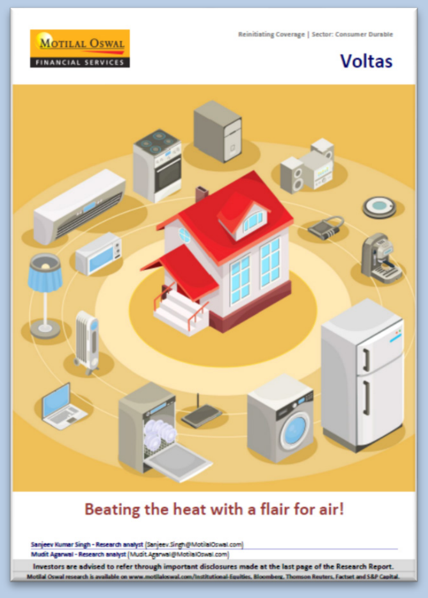

MOTILAL OSWAL FINANCIAL SERVICES

September 2023

Initiating Coverage | Sector: Healthcare

Global Health

Crafting a differentiated ecosystem in healthcare


MOTILAL OSWAL FINANCIAL SERVICES

Reinitiating Coverage | Sector: Consumer Durable

Voltas

Beating the heat with a flair for air!


MOTILAL OSWAL FINANCIAL SERVICES

September 2023

Initiating Coverage | Sector: Retail

Raymond

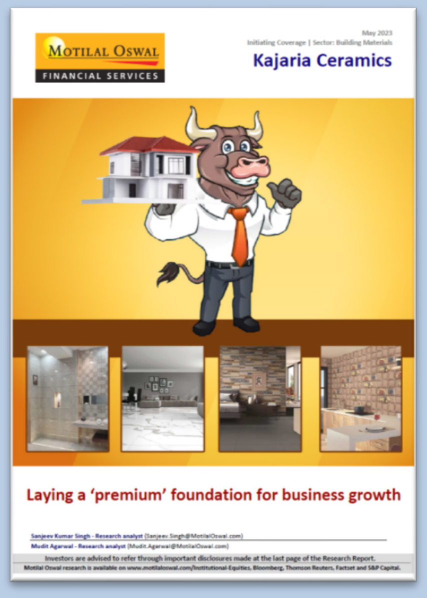
Rejuvenating the Brand


MOTILAL OSWAL FINANCIAL SERVICES

Reinitiating Coverage | Sector: Consumer Durable

Havells India

Powering growth with a diversified product portfolio


MOTILAL OSWAL FINANCIAL SERVICES

May 2023

Initiating Coverage | Sector: Building Materials

Kajaria Ceramics

Laying a 'premium' foundation for business growth

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall be within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

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