Risk Factors

Like other businesses, the Company's business is exposed to various risks. The following risks are what the Company feels that if occurred, they may adversely affect the Company's business, financial position and performance in a material manner. In addition, there could be other risks that the Company has no knowledge of at the moment; or feels, following its consideration, that they could not yet be classified as risks that could materially damage the Company's business.

Risk from potentially intense competition

The restaurant business that the Company is running is indeed a highly-competitive business and competition will be even more intense as days pass by. As a result, the Company's success will depend on its ability to continue to effectively compete with other contenders.

The Company is to compete with a variety of restaurants that include international restaurant chains, well-established local restaurant chains and numerous small-time restaurateurs. In addition, new operators enter the restaurant business each day due largely to the low barrier of entry into this business. As a result, competition in the restaurant business will be based on price and quality of food, variety and value perception of menu, service quality, number and location of outlets, effectiveness in new product development, advertising and sales promotion activities, restaurant decoration and the way the restaurant is maintained to continue attracting customers and, finally, brand reputation and strength. Failure by the Company to constantly and effectively compete with other contenders in these aspects will have a material and adverse impact to the business and its operation.

However, the fact that the Company continues to see its branch, income and performance expanding for more than two decades indicates that it does have an ability to constantly and effectively compete with other challengers.
In other words, the Company has several competitive advantages; namely (1) strong brand recognition as the "MK Brand" is indeed highly recognized and adored by customers; (2) strong financial position which enables the Company to expand business both in the short and long term; (3) capable and

experienced management team which has been in the restaurant business for more than 20 years and which helps making the Company's management effective and efficient; (4) own service training center which enhances management skills of branch managers and, more importantly, trains service staff to provide standardized service at all the Company's restaurants; (5) best strategic locations of more than 500 branches of "MK" and "Yayoi" restaurants nationwide; (6) business size which is large enough to achieve the economy of scale in many areas such as sourcing and procurement, transportation and advertising; and (7) construction of a new and sophisticated central kitchen and a distribution center which will increase the Company's kitchen facilities totaling 3 places in order to support the future expansion.

Risk from volatility of raw material prices

Since costs of food are the Company's most important cost item as it accounts for as high as 33 percent of the Company's revenues from sales and services and since most of them are costs of raw materials, changes in raw material prices at a time the Company could not hike its sales prices to compensate for the rise or if it could only partially compensate such rise due to intense competitions or weakening purchasing power will materially and adversely affect the Company's performance.

Most of the Company's raw materials are fresh produce such as meat, seafood, vegetables, fruits, egg, rice and seasoning of which their market prices and quantities fluctuate at any time according to demand and supply. This is especially the case of volumes being produced which could be negatively affected by unfavorable weather condition, natural disaster or contagious diseases in animals or plants, all of which are beyond the Company's control. When raw material prices are up due to depleting production volumes affected by negative factors mentioned above, the Company is required to buy raw materials at higher price and volume that it has not projected. This could eventually make a negative impact to the Company's performance.

To minimize risk from the fluctuation of raw material prices, the Company has embarked on several measures to properly control the costs of raw materials. Significant measures are (1) estimating demands of raw materials that could materially affect the Company's total costs of raw materials in order to plan the sourcing for an amount and within a timeframe as required by the Company's sales plan; (2) the estimated demand of raw materials should allow the Company to have a better negotiating power with manufacturers or distributors thanks to a huge volume of raw materials to be bought and a definite delivery

schedule; (3) to prevent risk from price fluctuation, a future sales contract will be signed with reliable manufacturers or distributors where parties will be bound to each other within an agreed timeframe such as within three months, six months or a year; and where the contract will clearly specify the prices, volumes that will change hands and delivery dates; (4) the sourcing of raw materials of which prices are seasonally fluctuated and which could be properly stored without materially jeopardizing their quality will be made in advance in preparation for consumption during the period when their prices are up; and (5) a comparative report will be regularly made to inform changes of raw material prices that could make a material impact to the total costs of raw materials as this will be used as a guideline to hike menu prices when necessary and if possible. These measures were carried out to reduce volatility from the change of raw material prices as well as to keep the costs of raw material in control. So far, the results have been quite satisfactory as evident from the costs of food as a percentage of revenues from sales and services in 2012 and 2013, which was 32.6 percent and 33.1 percent, respectively, or a rise by merely 0.5 percent and which negatively affected the Company's net profit after tax by merely Baht 54 million.

Risk from additional costs of employee

The restaurant business is a labor-intensive industry which depends very much on employees especially service staff who will make customers happy through their services. As a result, costs of employee are the second most important cost item of the business only after the costs of food. As of end of 2013, the Company had a total of 19,394 employees and the total costs of employees in 2013 amounted to Baht 3.78 billion which accounted for 27 percent of the Company's sales revenues of Baht 13.969 billion. As a result, if the cost keeps rising and the Company could not hike its sales price to compensate for an increasing employee expense or if it could only partially cover the expense due largely to intense competition or weakening purchasing power or any other factor that may prevent the Company from raising its sales price, this will negatively affect the Company's performance in a material manner.

To minimize the risk from the increase of employee costs as described above, the Company has conducted various

measures to keep the cost within an optimal level. The measures are
(1) setting and adjusting the number of staff in each restaurant to reflect its traffic volume to maximize efficiency while enabling to maintain quality service to customers at a standard level envisioned by the Company;
(2) monitoring each restaurant's staff productivity and ensuring that it is in line with the productivity standard developed by the Company.
In addition, to encourage restaurant managers to pay attention to this subject, staff productivity has become one of the Key Performance Indicators (KPI) used in the evaluation of each restaurant's performance;
(3) introducing a computerized technology to the restaurant which will not only enhance staff efficiency but will also improve service quality as the technology will speed up the service and make it more accurate; and
(4) staff especially service employees will be constantly trained to enhance performance and standardize service quality. By seriously and incessantly pursuing these measures and by hiking sales prices when necessary and if doable, the Company has managed to control the costs of employees to remain at an optimal level vis-à-vis its revenues and at the same time reduced its loss resulted from staff oversupply and employee underperformance.

Risk from the shortage of branch operational employees

The Company's business is a service business which heavily relies upon people as its driving force.
The Company plans to open new branches each year and each branch needs approximately 30 - 40 staff.
As a result, the Company has to recruit a large number of new staff to accommodate new branch opening.
As of December 31, 2013, the Company boasted a total of 17,776 employees in branch operation of whom 72 percent were full-time and 28 percent were part-time. The total staff turnover rate was averaged at 10 percent.
Failure to recruit new staff to accommodate expansion or to replace resigning staff in a timely fashion will materially affect the Company's service and operation.
However, it has committed to resolve this problem by retaining staff to work as long as possible with the Company and by giving priority to the concept of working under the "MK Culture" where employees of all levels are taken care of. Capable staff are given a chance to rise along their career path to executive positions in the future. In addition, the Company takes a great care by giving employees fair remunerations and welfare as well as skill-enhancing training and by treating them as family members. As such, the Company continues to attract candidates. New recruits are to attend a training course held by the MK Service Training Center to acknowledge the MK corporate culture and to perform his/her duty based on the Company's standards. So far, the Company has had no problem recruiting new personnel with required qualifications.

Risk from failure to find leased space and to renew the leased space under a condition deemed appropriate by the Company

As the competition in the industry is getting intense and as there is an increasing number of restaurateurs entering the market, leased space for new restaurant has become rarer. This could expose the Company to a risk from not being able to find and lease space to open a new branch as planned.

However, the Company has been a business partner with several lessors who operate shopping malls, modern-trade outlets and community malls in Bangkok and provinces. Besides, the Company is Thailand's leading restaurateur who offers products and services highly desirable by consumer. As a result, this is unlikely to prevent the Company from finding the leased space. Meanwhile, most of the lease agreements offer a lease term of three years at a time which is renewable 3 - 5 times for another three years on each occasion. Failure to renew the lease agreement may affect the Company's operation. Yet, the Company has had a warm and long-lasting relationship with the lessors. Together with its excellent rent payment track record, its compliance with the lease agreements, the fact that it has never had problem with the lessors and that it has the lease agreements renewed all the time, not mentioning the fact that the Company and the lessors sometimes joined force to resolve problems of unimpressive branches which had to be closed down for the best interest of both parties, the Company therefore is of the opinion that the risk from not finding leased space and not renewing lease agreement should not be an obstacle to continue its business.

Risk from new branch opening

The Company aims to grow constantly and opening new branch is a factor to achieve the goal. As the competition in this industry has become tougher than before together with the fact that newcomers step into the industry every day, the Company therefore is exposed to a risk that its new branch may not generate sales up to a target and thereby not yield a satisfying investment return. It needs approximately Baht 8 - 10 million to open a branch. The fund is used for design, construction, mechanical & electricity (M&E) system, furniture, kitchen equipment and other office equipment. The Company plans to constantly expand its MK Suki Restaurant and Yayoi Japanese Restaurant. Locations of newly-opened outlets however may overlap with existing branches located nearby and this could affect the Company's sales and performances in the longer run.

However, to open a new branch, the Company has to do a lot of work studying the branch opening plan. A newly-opened branch must yield a good investment return based on required criteria. The Development and Engineering Department will be responsible for surveying location, population density, target groups of customers and performance of nearby branches. It will also conduct a financial analysis by looking at, for example, payback period and return on investment (ROI) which must not be less than a required level. This information will be used in considering a new branch opening. In addition, the Company has had experiences in this business for more than 25 years with highly-recognized products and services desirable by customers. At the other end, shopping mall owners, modern-trade outlet and community mall operators are, too, looking for reputable restaurants to lease their space in order to attract customers. That's why the Company has been offered attractive packages of ideal location, space size and rental term. The Company studies every leased premise being offered as well as conducts a financial analysis before making an investment decision at an appropriate site that could general high yield. The Company is confident that new branch opening that covers more extensive service areas should increase its capacity to generate higher profits to shareholders and to reduce its operation risk in the long run.

In addition, the Company also takes into consideration sales amounts of nearby branches and population density in the same area to ensure that a new entrant will not affect the business of existing branch nearby but rather is an appealing alternative for customers living in the area and works strategically to expand the Company's service areas to help maintain its market share.

Risk from failure to renew the Yayoi franchise

MK Interfood Co., Ltd. ("MKI") has been licensed to operate a Japanese restaurant in Thailand by Plenus Co., Ltd. under the "Yayoi" branch. The franchise term is three years and is renewable for three years on each occasion unless either party notifies the other to terminate the agreement 180 days before each expiration date. As a result, termination of the franchise agreement could prevent the Company from continuing the Yayoi restaurant business which will inevitably affect the Company's operation.

The Company has already operated the Yayoi Japanese Restaurant business for eight years. As of December 31, 2013, it had a total of 113 Yayoi branches. So far, it has strictly complied with the terms and conditions of the franchise agreement where menus and operation procedures of "Yayoi Ken" under the franchise system of the rights owner and its knowhow are actively implemented in the business. Others include style of the restaurant, menu change, choices of raw materials, product development, staff training, commercial and production operation as well as on-time payment of the franchise fee. In addition, the Company is truly committed to expand the Yayoi branch as evident in 2013 where 22 new branches were opened with more planned openings in the future. More importantly, Yayoi Restaurant's operation has been growing quite steadily. Its sales growth rose on average 40 percent during the past four years (2010 - 2013) while the net profit went from being in red or a net loss of Baht 48 million in 2008 to a net profit of Baht 147 million in 2013. Besides, the Company and Plenus Co., Ltd. are strong business alliances who have joined force to run MK Suki Restaurant overseas. With a long-lasting relationship between us and the fact that the Company has duly complied with conditions in the concerned agreement, the Company is of the view that it should be trusted to continue having the franchise contract renewed.

Risk from the information technology (IT) system

To enhance the Company's customers service capacity, it has introduced the IT system in the food ordering process where the system will directly and immediately send orders to the kitchen to shorten service time and to minimize errors. The IT system is also a crucial component of the Company's home delivery service as it receives orders from customers before sending them to various branches to execute delivery. The system is also prominent in other management processes.
If the system is malfunctioned or in case of an unforeseeable event that may paralyze the system, this could affect the Company's operation.

Having realized the importance of the IT system, the Company has adopted a guideline to modernize the technology with a focus at systems considered crucial to its business; namely accounting, raw material sourcing and procurement, inventory management, product distribution and communication system between the head office and branches nationwide. The enhanced IT system should gather information and deliver it to executives who need it for analysis and for making crucial decisions. As a result, the Company is confident that as the system has been constantly enhanced, in case of malfunction, the Company will still be able to continue its business as every unit and function does have both manuals and standard operating procedures (SOP) that will help them resolve problems and thereby allow the business to continue running.

Risk from overseas investment

The Company has invested abroad through two joint-venture firms in which it holds 12 percent in Plenus MK Co., Ltd.'s shares to operate MK Suki Restaurant in Japan and 50 percent in Plenus & MK Pte. Ltd.'s shares to run MK Suki Restaurant in Singapore. Each country is exposed to various risk factors such as economic and political conditions, laws, tax and exchange rates. As a result, in case of an event with material impact to business operation in a concerned country, it will inevitably affect the Company's operation.

During 2011 - 2013, the Company enjoyed Baht 9 million, Baht 57 million and Baht 125 million revenues from its overseas business which accounted for 0.1 percent, 0.4 percent and 0.9 percent of total sales revenues, respectively. Yet, the Company conducts an overseas investment study where it surveys the market and looks at population density and target groups of customers as well as other economic factors such as GDP, inflation rate, exchange rates, political stability, investment policy governing foreign entities and tax rates. The Company also conducts financial analysis for ratios and figures which must not be lower than its threshold required for overseas investment. In addition, by having a strong partner like Plenus Co., Ltd. who is Japan's largest bento lunchbox business operator boasting a network of more than 2,900 branches as well as the owner of the ready-to-serve Yayoi Ken Restaurant which commands an overnight success in Japan, the Company therefore is confident in Plenus Co., Ltd.'s leadership vision and management style as well as its potential to make MK Suki brand recognized and to expand MK Suki branches all over Japan. As a result, the Company is of the view that careful investment planning and strong business partnership will help reduce the risk.
In addition, by expanding the business into countries enjoying a high growth rate with a high density of population who have high purchasing power, this could be a great opportunity for the Company to grow even more and also the opportunity to diversify the operation risk.

Risk from epidemic

So far, there have been several bouts of outbreaks that hit the restaurant business hard. For example, in 2002, Bovine Spongiform Encephalopathy or the mad cow disease struck the US and Europe. Three years later, several countries suffered from the bird flu (H5N1) outbreak before the world witnessed the infectious disease of swine influenza (H1N1) in Mexico in 2008. The rampant epidemic did erode customer's confidence to consume meat, chicken and pork, all of which are major raw materials of all restaurants under the MK Group. Future epidemic, if any, therefore may affect the Company's revenues.

The Company places a high priority to the selection of raw materials which will be supplied by selected quality manufacturers and distributors. Every piece of raw materials will have a traceability where product can be traced back throughout the entire food chain from step one to the final stage whether it's about the origin of food, production and transportation. That's why the Company is convinced that every piece of its raw materials meets the standard, is hygienic and, is safe without contaminant. In addition, the Company has the Quality Control Department to verify product quality while the operation of the two central kitchens has been certified by international quality assurance systems which among a few include ISO, HACCP and GMP.

Risk from natural disasters and accidents

Thailand's major flood which started in late July 2011 and last until the end of the year extensively damaged the Thai economy during the latter half of 2011. Water inundated farming areas in the upper Central Plain and industrial sites in the lower Central Plain including seven industrial estates in Ayutthaya and Pathum Thani provinces.
The Company's central kitchen at Nava Nakorn (CK 3) located at Nava Nakorn Industrial Estate, too, was under the water and had to be closed before part of the production was relocated to the central kitchen at Bangna (CK4), which was able to boasts enough production capacity to accommodate demands of all existing branches. However, the Company has already eyed an ideal site for its new central kitchen (CK5). Meanwhile, 55 MK Suki Restaurants and 13 Yayoi Japanese Restaurants suffered from the 2011 tragic flood where they were forced to shut down for an average of 0.5 - 2 months. Most however were not damaged as they were located in shopping malls and modern-trade outlets which had effective flood-protection measures. Yet, the flood did temporarily suspend the operation of certain suppliers which in effect led to a shortage of certain raw materials for a period of time and this inevitably affected the Company's sales revenues. Yet, having realized the effect of natural disaster to its business, the Company has planned protective measures to handle the risk. This includes buying casualty insurance, formulating an emergency operation plan, training staff to handle natural disaster incidents, building a new central kitchen at an ideal site, adding a distribution center to its portfolio to diversify risk, approving an emergency fund to assist employees and communicating with all parties of the management's readiness to bolster confidence of shareholders, employees, suppliers and customers that the Company can indeed continue operating and that it's ready should there be a natural disaster risk.

As for a plan to handle the shortage of certain products, the Sourcing and Procurement Department will select every manufacturer and distributor who can produce products that meet the Company's required standard before closely communicating with them to learn which product they can produce, their production capacity and volumes and dates they can deliver such product. The Sourcing and Procurement Department will coordinate with the central kitchen to encourage direct and clear communication to every branch of shortage items, replacement items and expected delivery time if the product cannot be delivered normally. The communication is to ensure that branches learn how to effectively manage inventories while staff at every branch may directly communicate with customers. While it's true that the 2011 major flood did prevent the Company from providing a full-scaled service, yet, the Company managed to return the business to normalcy as quickly as possible. All customers understood what happened and continued trusting the Company, which convinces the Company that it can and is ready to handle the risk.

Aside from being prepared to protect itself from possible flood and to handle the disaster if occurred, the Company has taken out several types of casualty insurance policies such as accident insurance, third-party liability insurance and property insurance to make itself ready for future incidents.