

Restaurants Industry

Restaurants Weekly: Will increased promotions mean decreased margins?

Industry Overview

W/e 1/19: Restaurant Index outperforms, WING leads

For the week ended 1/19, the S&P Restaurant Index (+1.8%) outperformed the market (S&P 500: +1.0%). This week's leaders include WING (+4.1%), Pizza restaurants (PZZA, DPZ), and CMG (2.9%), which may reflect investors' preference to own high quality, segment leaders with positive demand fundamentals. QSR (-2.0%) underperformed following the company's 1/16 announcement that it will acquire Carrols Restaurant Group (TAST, not covered by BofA Global Equity Research) for an aggregate enterprise value of ~\$1 bb. Given that the transaction is expected to be EPS neutral and cash flow neutral over time— QSR will fund remodels through TAST operating cash flow – the greater implications are for what the acquisition says about the limits of the asset-light approach (see link to our report: [QSR for TAST: Asset light just got a little heavier](#)). Year-to-date, WING, DPZ, and CMG lead the sector, with gains of 6.5%, 3.6%, 2.5%, respectively.

Charts of the week: Promotions and margins

This week's charts of the week draw from our 2024 industry outlook (see a link to the report: [Year Ahead: Business as usual?](#)). As talk of promotional activity has ramped up, we have fielded questions about the impact of discounting on restaurant companies' margins. The restaurant industry has tended to increase promotional intensity when inflation has waned (as in 2016-17) and pulled back on promotions when inflation has accelerated (2014, 2018). Looking at the 2016-2017 period, when promotional activity increased (as indicated by y/y changes in promotional mentions), we see that revenue weighted restaurant-level margins actually expanded, suggesting that lower input prices more than offset lower menu prices. That said, we're not sure restaurants are entirely out of the woods: while promotional activity may not translate into margin pressure, we see some risks that restaurants will need to increase ad spending – particularly for full service restaurants - after pulling back significantly on spending during the pandemic.

Industry relative valuation & restaurants comps sheet

Relative to the broader market, the S&P 500 restaurants index is trading at a 10% discount (vs the 10-year average relative P/E multiple of 1.3x), lower versus a 4% discount in December. Our restaurants valuation and KPI sheets can be found on page 6.

Upcoming events: Investor Day, BROS Bull/Bear, QSR call

Upcoming events include the Jack in the Box Investor Day, which will take place on 1/24 in San Diego, CA. On 1/26, we will host a joint conference call on QSR/TAST with Bill Reuter, US High Yield senior analyst covering Restaurants at BofA. Please contact us to register for this event: Call: QSR's TAST acquisition – Asset light just got a little heavier. We also highlight that on 1/29, we will host a BROS Bull/Bear debate at 2PM ET.

22 January 2024

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United States
Restaurants

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Stock symbol key:

BLMN: Bloomin' Brands
BROS: Dutch Bros
DRI: Darden Restaurants
CAKE: Cheesecake Factory
CBRL: Cracker Barrel
CMG: Chipotle
DNUT: Krispy Kreme
DPZ: Domino's
EAT: Brinker International
FWRG: First Watch
JACK: Jack in the Box
MCD: McDonald's
PZZA: Papa Johns
PTLO: Portillo's
QSR: Restaurant Brands Int'l
SBUX: Starbucks
SG: Sweetgreen
SHAK: Shake Shack
TXRH: Texas Roadhouse
WEN: Wendy's
WING: Wingstop
YUM: Yum Brands

Glossary of terms:

SSSG – same-store sales growth, or comparable sales ("comps")

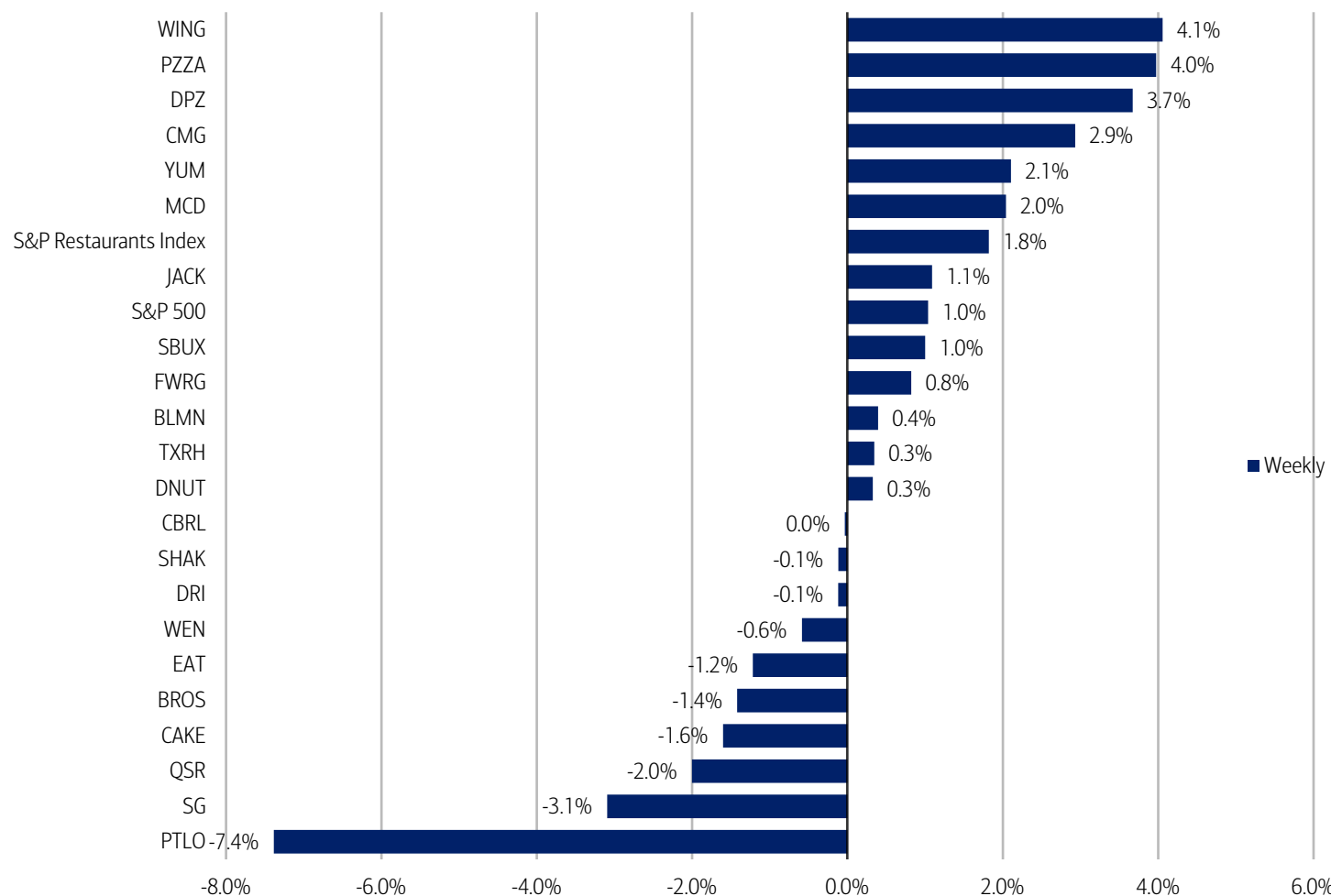
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Timestamp: 22 January 2024 05:00AM EST

Exhibit 1: Restaurant stocks outperformed the market last week

BofA Restaurants Coverage Weekly (5-day) Share Price Performance

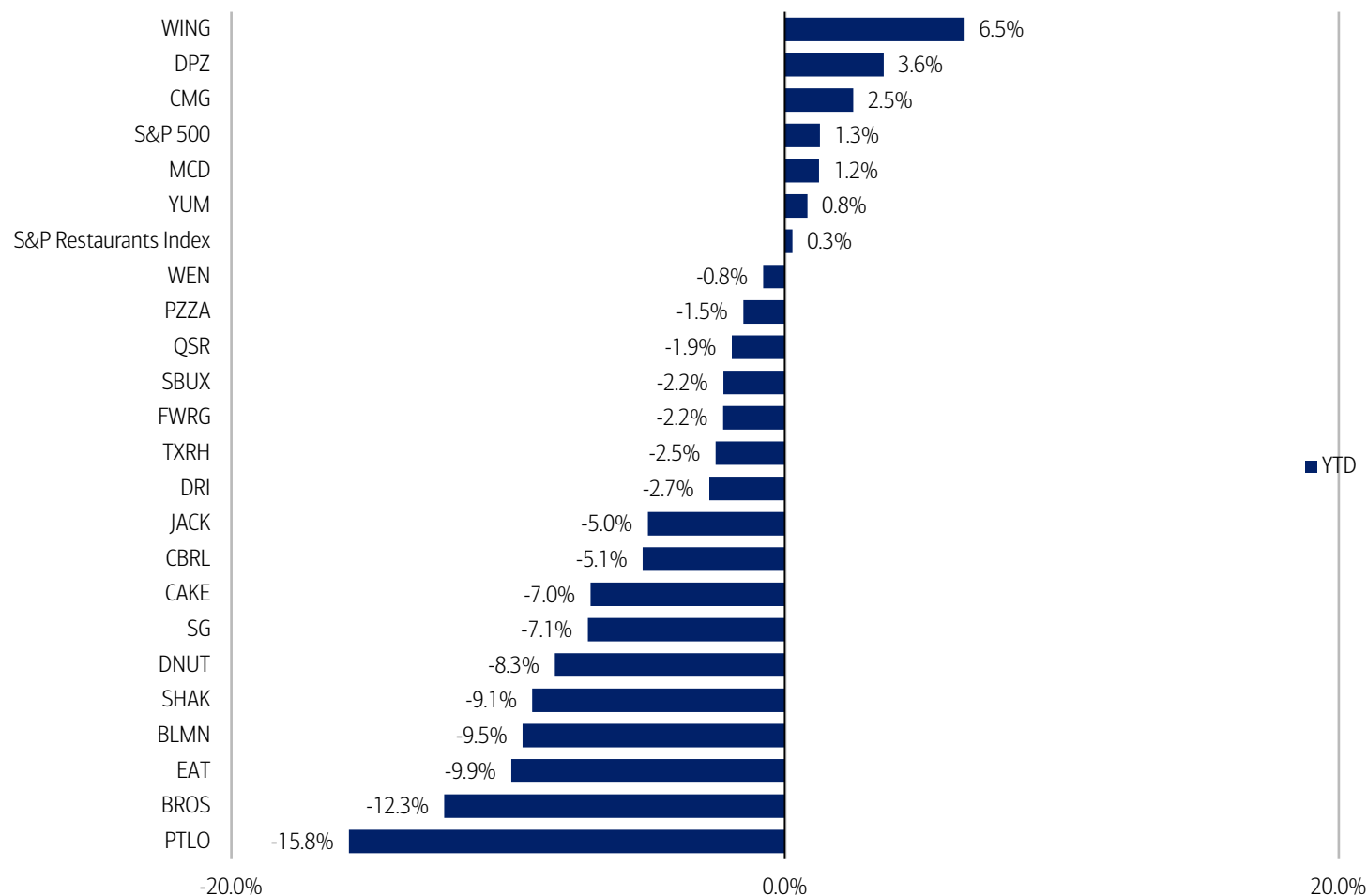


Source: Bloomberg

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Exhibit 2: YTD, WING and DPZ lead

BofA Restaurants Coverage YTD Share Price Performance



Source: Bloomberg

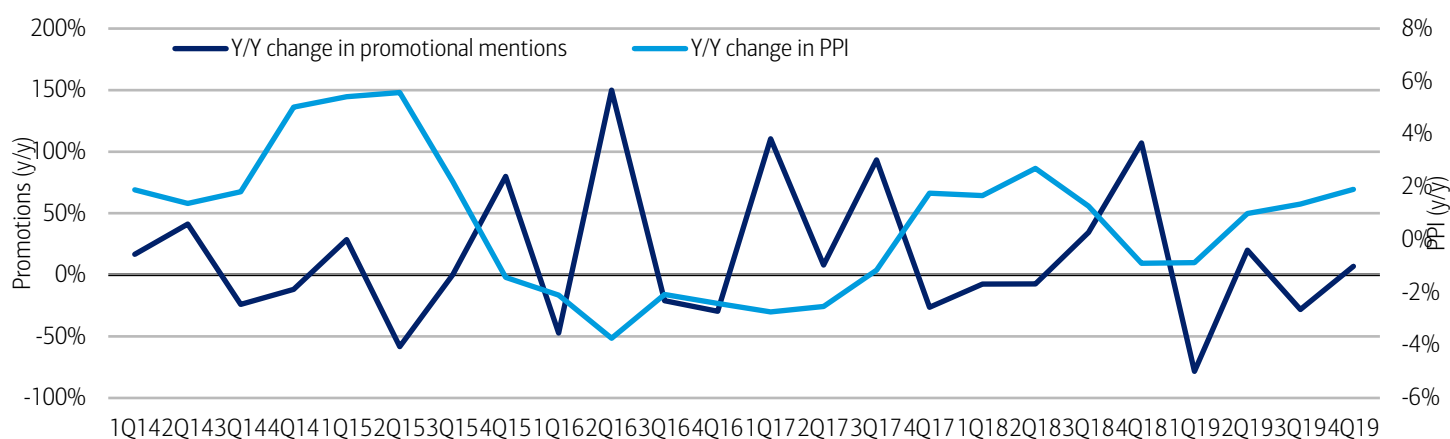
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Chart of the week: Promotions and margins

This week's charts of the week draw from our 2024 industry outlook (see a link to the report: [Year Ahead: Business as usual?](#)). As talk of promotional activity has ramped up, we have fielded questions about the impact of discounting on restaurant companies' margins. The restaurant industry has tended to increase promotional intensity when inflation has waned (as in 2016-17) and pulled back on promotions when inflation has accelerated (2014, 2018). Looking at the 2016-2017 period, when promotional activity increased (as indicated by y/y changes in promotional mentions), we see that revenue weighted restaurant-level margins actually expanded, suggesting that lower input prices more than offset lower menu prices. That said, we're not sure restaurants are entirely out of the woods: while promotional activity may not translate into margin pressure, we see some risks that restaurants will need to increase ad spending – particularly for full service restaurants - after pulling back significantly on spending during the pandemic.

Exhibit 3: The restaurant industry has tended to increase promotional intensity when inflation has waned (as in 2016-17) and pulled back on promotions when inflation has accelerated (2014, 2018)

Y/Y change in promotional mentions vs Y/Y change in PPI

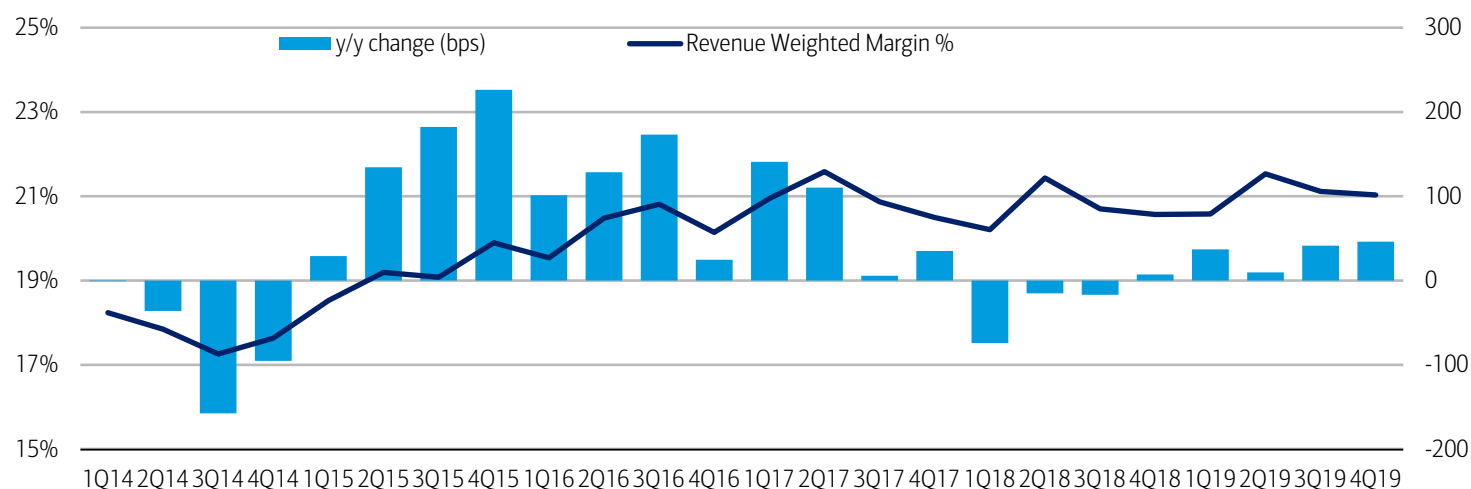


Source: Bloomberg, Haver

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Exhibit 4: Despite an apparent increase in promotional activity in 2016-2017, average restaurant level margins increased

Revenue weighted average restaurant level margin rate and year-over-year changes



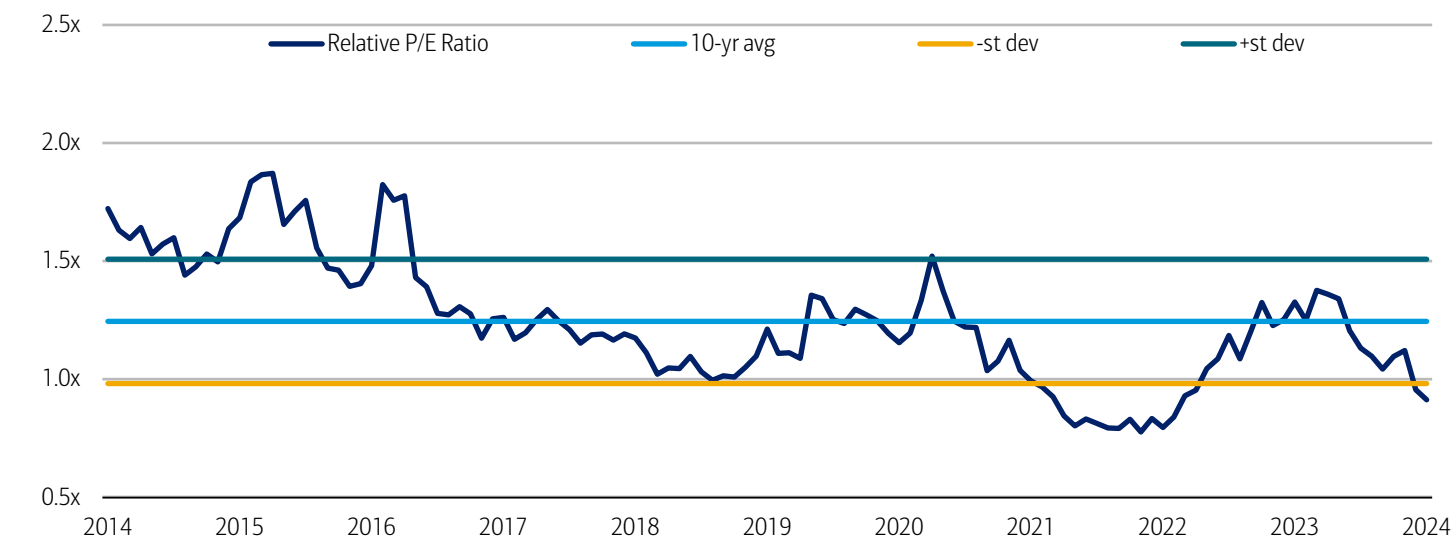
Source: Company reports, BofA Global Research estimates

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Valuation & comps sheet

Exhibit 5: The S&P 500 Restaurant Index Relative P/E is below its 10-year average

S&P 500 Restaurants Index P/E (10-year history)

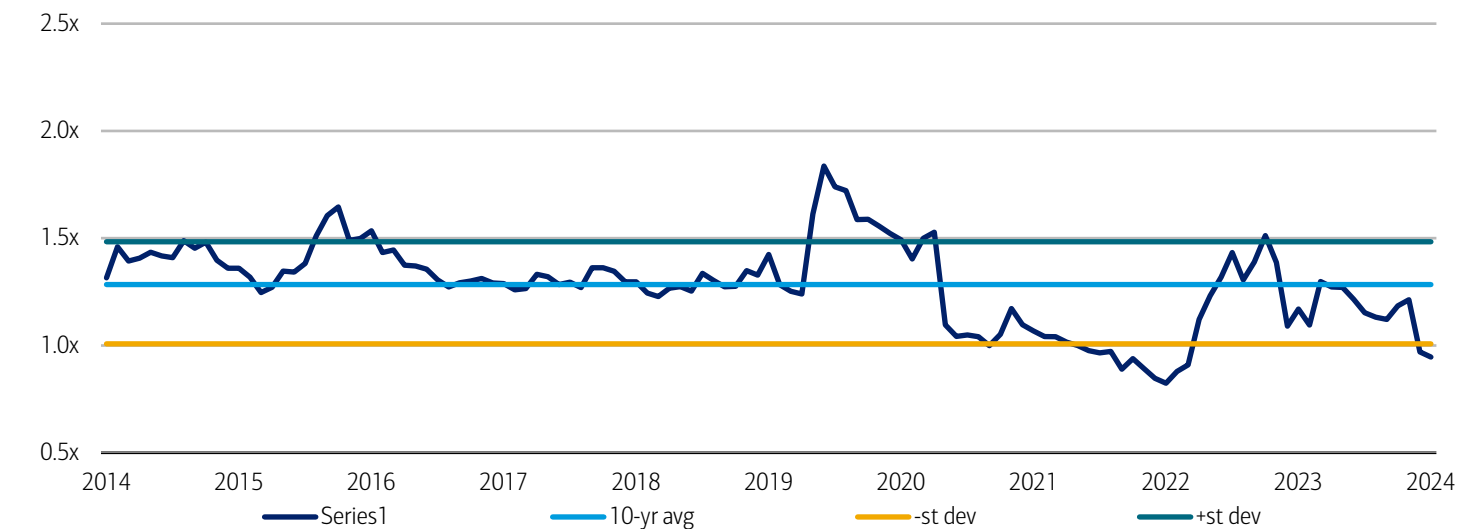


Source: Bloomberg

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Exhibit 6: The S&P 500 Restaurants Index Relative EV/EBITDA is below its 10-year average

S&P 500 Restaurants Index Relative EV/EBITDA (10-year history)



Source: Bloomberg

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Exhibit 7: Restaurant companies across the Limited Service and Full Service industries

Restaurants valuation sheet

\$ in mm except per share values						Price Performance					EV/EBITDA			P/E			EBITDA			EPS		
Company	Rating	Last Price	Price Objective	Upside/Downside to PO (%)	1 wk	3M	YTD	Market Cap	Enterprise Value	2022	2023E	2024E	2022	2023E	2024E	2022	2023E	2024E	2022	2023E	2024E	
Limited Service																						
Dutch Bros	BROS	Buy	\$27.58	\$48	74%	-2%	9%	-13%	\$4,885	\$4,851	54.4x	31.3x	24.2x	166.5x	93.4x	72.8x	\$89	\$155	\$200	\$0.17	\$0.30	\$0.38
Krispy Kreme	DNUT	Buy	\$13.77	\$19	38%	0%	8%	-9%	\$2,321	\$3,222	16.9x	15.1x	11.6x	46.1x	44.0x	30.3x	\$191	\$214	\$278	\$0.30	\$0.31	\$0.45
Starbucks	SBUX	Buy	\$93.48	\$128	37%	1%	-1%	-3%	\$106,259	\$118,981	18.9x	16.6x	14.4x	31.6x	26.4x	22.8x	\$6,304	\$7,163	\$8,237	\$2.96	\$3.54	\$4.10
Domino's Pizza	DPZ	Buy	\$426.75	\$483	13%	4%	24%	4%	\$14,885	\$19,761	23.3x	21.9x	19.4x	34.1x	29.2x	25.9x	\$848	\$903	\$1,019	\$12.53	\$14.63	\$16.51
Jack in the Box	JACK	Buy	\$76.97	\$97	26%	0%	19%	-6%	\$1,519	\$3,258	5.8x	10.0x	9.7x	NM	12.8x	11.9x	\$559	\$324	\$336	\$6.25	\$6.02	\$6.44
Papa John's	PZZA	Buy	\$75.06	\$90	20%	4%	13%	-2%	\$2,459	\$3,241	15.5x	14.9x	13.8x	25.6x	29.4x	26.0x	\$209	\$217	\$234	\$2.93	\$2.56	\$2.89
Carrols Restaurant Group	TAST	NC	\$9.41			13%	75%	19%	\$485	\$921	5.5x	6.3x	6.1x	-13.4x	NM	17.6x	\$168	\$147	\$152	-\$0.70	\$0.48	\$0.54
Restaurant Brands International	QSR	Underperform	\$76.36	\$65	-15%	-2%	16%	-2%	\$35,182	\$46,821	21.3x	19.8x	18.4x	24.7x	24.2x	23.4x	\$2,201	\$2,366	\$2,542	\$3.09	\$3.15	\$3.27
Wendy's	WEN	Underperform	\$19.18	\$21	9%	-1%	0%	-2%	\$3,956	\$6,224	12.5x	11.5x	10.9x	22.3x	19.2x	17.8x	\$498	\$539	\$572	\$0.86	\$1.00	\$1.08
Wingstop	WING	Buy	\$273.60	\$285	4%	4%	51%	7%	\$8,048	\$8,682	80.4x	62.1x	54.3x	149.3x	112.8x	90.7x	\$108	\$140	\$160	\$1.83	\$2.42	\$3.02
Chipotle Mexican Grill	CMG	Buy	\$2,342.74	\$2,570	10%	3%	27%	2%	\$64,296	\$63,087	43.0x	33.4x	27.9x	71.5x	52.9x	43.3x	\$1,468	\$1,888	\$2,258	\$32.78	\$44.26	\$54.13
Portillo's	PTLO	Buy	\$13.36	\$25	87%	-8%	-10%	-16%	\$974	\$1,267	15.6x	12.7x	12.0x	17.0x	19.7x	18.3x	\$81	\$100	\$105	\$0.79	\$0.68	\$0.73
Sweetgreen	SG	Buy	\$10.39	\$16	54%	-4%	-5%	-8%	\$1,168	\$923	-19.0x	-210.6x	62.9x	-10.3x	-16.3x	-28.3x	-\$49	-\$4	\$15	-\$1.01	-\$0.64	-\$0.37
Shake Shack	SHAK	Neutral	\$66.70	\$75	12%	-1%	20%	-10%	\$2,822	\$2,840	24.9x	22.1x	18.8x	NM	NM	NM	\$114	\$129	\$151	-\$0.31	\$0.41	\$0.55
Cava	CAVA	NC	\$45.82			7%			\$5,205	\$5,196	94.1x	72.9x	66.2x	NM	NM	NM	\$55	\$71	\$78	NM	\$0.13	\$0.14
Limited Service Average											22.4x	9.1x	20.7x	42.6x	34.0x	28.6x						
Full Service																						
BJ's Restaurants	BJRI	NC	\$33.28			3%	38%	-8%	\$773	\$853	6.7x	8.1x	6.9x	NM	NM	25.7x	\$128	\$105	\$124	\$0.07	\$0.79	\$1.30
Bloomin' Brands	BLMN	Neutral	\$25.41	\$30	18%	0%	7%	-10%	\$2,206	\$3,272	6.5x	6.0x	6.1x	10.1x	8.9x	9.3x	\$506	\$546	\$541	\$2.51	\$2.86	\$2.74
Cheesecake Factory	CAKE	Neutral	\$32.48	\$33	2%	-2%	5%	-7%	\$1,649	\$2,199	7.0x	9.2x	8.1x	21.3x	12.3x	10.2x	\$316	\$240	\$272	\$1.53	\$2.65	\$3.19
Chuy's	CHUY	NC	\$33.62			-1%	0%	-12%	\$583	\$526	7.2x	9.1x	8.9x	24.5x	17.7x	17.4x	\$74	\$58	\$59	\$1.37	\$1.90	\$1.93
Dine Brands	DIN	NC	\$44.48			-5%	-13%	-10%	\$687	\$1,838	9.4x	7.4x	7.4x	7.2x	6.9x	6.9x	\$197	\$247	\$248	\$6.20	\$6.40	\$6.43
Darden Restaurants	DRI	Buy	\$159.42	\$193	21%	0%	12%	-3%	\$19,036	\$20,769	13.6x	13.1x	11.7x	21.5x	19.9x	17.8x	\$1,531	\$1,590	\$1,777	\$7.40	\$8.00	\$8.94
Brinker International	EAT	Underperform	\$38.85	\$37	-5%	-1%	18%	-10%	\$1,717	\$2,674	7.5x	7.9x	6.6x	12.6x	13.7x	11.1x	\$358	\$340	\$408	\$3.09	\$2.85	\$3.51
Dave & Buster's	PLAY	NC	\$48.52			-3%	35%	-10%	\$1,950	\$3,246	5.2x	6.2x	5.7x	NM	14.6x	11.4x	\$629	\$524	\$571	NM	\$3.33	\$4.27
Red Robin Gourmet Burgers	RRGB	NC	\$10.63			-4%	32%	-15%	\$165	\$349	2.7x	4.8x	4.5x	-3.3x	-8.6x	-15.9x	\$129	\$72	\$77	-\$3.26	-\$1.23	-\$0.67
Texas Roadhouse	TXRH	Buy	\$118.91	\$123	3%	0%	23%	-3%	\$7,941	\$7,872	17.2x	15.5x	12.9x	NM	26.0x	21.5x	\$457	\$509	\$609	\$3.97	\$4.57	\$5.54
Cracker Barrel	CBRL	Underperform	\$73.17	\$68	-7%	0%	5%	-5%	\$1,623	\$2,156	8.1x	9.4x	9.6x	12.0x	13.4x	14.2x	\$266	\$229	\$224	\$6.10	\$5.47	\$5.15
Denny's	DENN	NC	\$10.73			1%	24%	-1%	\$570	\$832	11.8x	9.6x	9.1x	20.6x	17.4x	15.3x	\$71	\$86	\$91	\$0.52	\$0.62	\$0.70
First Watch	FWRG	Buy	\$19.59	\$28	43%	1%	12%	-3%	\$1,172	\$1,273	18.2x	13.8x	12.2x	NM	40.7x	38.2x	\$70	\$92	\$104	\$0.22	\$0.48	\$0.51
ONE Group Hospitality	STKS	NC	\$4.50			-19%	2%	-26%	\$141	\$197	4.0x	4.9x	3.6x	NM	20.0x	8.7x	\$50	\$40	\$56	NM	\$0.23	\$0.52
Full Service Average											8.9x	8.9x	8.1x	14.0x	15.4x	13.5x						
SPX			\$4,813.98				1%		\$5,264		14.8x	14.4x	13.1x	23.0x	22.4x	20.0x	\$356	\$367	\$400	\$221.54	\$215.27	\$240.95

Source: BofA Global Research estimates, Bloomberg for companies not covered; NC – Not Covered

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Exhibit 8: Restaurant companies across the Limited Service and Full Service industries

Restaurants key performance indicators sheet

\$ in mm except per share values					EPS			growth y/y (%)			FCF		
Company	Rating	Last Price	Price Objective	Upside/Downside to PO (%)	2022	2023E	2024E	2022	2023E	2024E	2022	2023E	2024E
Limited Service													
BROS	Buy	\$27.59	\$48	74%	\$0.17	\$0.30	\$0.38	-44%	78%	28%	-\$97	-\$87	-\$60
DNUT	Buy	\$13.78	\$19	38%	\$0.30	\$0.31	\$0.45	-11%	5%	45%	\$17	\$19	\$49
SBUX	Buy	\$93.51	\$128	37%	\$2.96	\$3.54	\$4.10	-8%	20%	16%	\$2,556	\$3,675	\$1,457
DPZ	Buy	\$426.95	\$483	13%	\$12.53	\$14.63	\$16.51	-7%	17%	13%	\$388	\$812	\$693
JACK	Buy	\$77.05	\$97	26%	\$6.25	\$6.02	\$6.44	-11%	-4%	7%	\$140	\$78	\$105
PZZA	Buy	\$75.16	\$90	20%	\$2.93	\$2.56	\$2.89	-16%	-13%	13%	\$39	\$110	\$115
TAST	NC	\$9.41			-\$0.87	\$0.48	\$0.54	50%	-155%	11%	-\$17	NM	NM
WEN	Underperform	\$19.22	\$21	9%	\$0.86	\$1.00	\$1.08	5%	16%	8%	\$182	\$267	\$301
WING	Buy	\$273.77	\$285	4%	\$1.83	\$2.42	\$3.02	-24%	32%	24%	\$52	\$71	\$89
CMG	Buy	\$2,340.18	\$2,570	10%	\$32.78	\$44.26	\$54.13	29%	35%	22%	\$493	\$1,245	\$1,510
PTLO	Buy	\$13.39	\$25	87%	\$0.79	\$0.68	\$0.73	NM	-14%	7%	\$2	\$15	\$8
SG	Buy	\$10.39	\$16	54%	-\$1.01	-\$0.64	-\$0.37	-82%	-37%	-42%	\$0	\$0	\$0
SHAK	Neutral	\$67.08	\$75	12%	-\$0.31	\$0.41	\$0.55	-187%	-233%	36%	-\$66	-\$27	-\$9
Limited Service Average													
Full Service													
BJRI	NC	\$33.39			\$0.03	\$0.79	\$1.30	-96%	2523%	65%	-\$27	-\$5	\$3
BLMN	Neutral	\$25.44	\$30	18%	\$2.51	\$2.86	\$2.74	-7%	14%	-4%	\$171	\$310	\$299
CAKE	Neutral	\$32.53	\$33	1%	\$1.53	\$2.65	\$3.19	-42%	74%	21%	\$49	\$167	\$107
CHUY	NC	\$33.61			\$1.29	\$1.90	\$1.93	-32%	48%	2%	\$15	\$21	\$23
DIN	NC	\$44.54			\$6.09	\$6.40	\$6.43	-5%	5%	0%	\$54	\$86	\$107
DRI	Buy	\$159.45	\$193	21%	\$7.40	\$8.00	\$8.94	-112%	8%	12%	\$888	\$988	\$943
EAT	Underperform	\$38.93	\$37	-5%	\$3.09	\$2.85	\$3.51	-1%	-8%	24%	\$132	\$86	\$142
PLAY	NC	\$48.59			\$2.76	\$3.33	\$4.27	NM	NM	28%	\$210	\$111	\$152
RRGB	NC	\$10.66			-\$2.53	-\$1.23	-\$0.67	105%	-51%	-46%	-\$3	NM	NM
TXRH	Buy	\$118.92	\$123	3%	\$3.97	\$4.57	\$5.54	13%	15%	21%	\$248	\$156	\$244
CBRL	Underperform	\$73.39	\$68	-7%	\$6.10	\$5.47	\$5.15	18%	-10%	-6%	\$107	\$123	\$144
DENN	NC	\$10.74			\$0.50	\$0.62	\$0.70	-19%	23%	13%	\$28	NM	NM
FWRG	Buy	\$19.55	\$28	43%	\$0.22	\$0.48	\$0.51	NM	122%	7%	\$0	\$34	\$19
STKS	NC	\$4.50			NM	\$0.23	\$0.52	NM	NM	129%	-\$7	-\$23	-\$9
Full Service Average													
SPX		\$4,810.91			\$221.54	\$215.27	\$240.95	3%	-3%	12%	\$168	\$184	\$213

Source: BofA Global Research estimates, Bloomberg for companies not covered; NC – Not Covered

Exhibit 9: Stocks mentioned

Prices and ratings for stocks mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
BLMN	BLMN US	Bloomin Brands	US\$ 25.36	C-2-7
EAT	EAT US	Brinker Intl	US\$ 38.89	C-3-9
CAKE	CAKE US	Cheesecake Factory	US\$ 32.7	C-2-7
CMG	CMG US	Chipotle Mex Grill	US\$ 2334.6	B-1-9
CBRL	CBRL US	Cracker Barrel	US\$ 73.51	B-3-7
DRI	DRI US	Darden Restaurants	US\$ 159.24	B-1-7
DPZ	DPZ US	Domino's Pizza	US\$ 426.77	B-1-7
BROS	BROS US	Dutch Bros	US\$ 28.22	C-1-9
FWRG	FWRG US	First Watch	US\$ 20.03	C-1-9
JACK	JACK US	Jack in the Box	US\$ 77.99	C-1-7
DNUT	DNUT US	Krispy Kreme	US\$ 13.85	C-1-7
PZZA	PZZA US	Papa John's Int	US\$ 74.97	B-1-7
PTLO	PTLO US	Portillo's Inc.	US\$ 13.44	C-1-9
QSR	QSR US	Restaurant Brands In	US\$ 76.88	B-3-7
YQSR	QSR CN	Restaurant Brands In	C\$ 103.27	B-3-7
SHAK	SHAK.US	Shake Shack	US\$ 67.47	C-2-9
SBUX	SBUX US	Starbucks	US\$ 93.86	B-1-7
SG	SG US	Sweetgreen	US\$ 10.62	C-1-9
TXRH	TXRH US	Texas Roadhouse	US\$ 118.78	B-1-7
WEN	WEN US	Wendy's Co	US\$ 19.19	B-3-7
WING	WING US	Wingstop Inc	US\$ 275.75	C-1-7

Source: BofA Global Research

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Price objective basis & risk**Bloomin Brands (BLMN)**

Relative to the S&P 500, BLMN's present P/E multiple is 0.4x, below its 5-year average (excluding the COVID-19 spike). We believe the multiple is unlikely to expand in the near term given the lack of visibility on the demand environment. We apply this multiple of 0.6x (10.1x absolute) to our 12 month forward estimates - 4Q24-3Q25 EPS of \$2.97- to arrive at our \$30 PO.

Downside Risks: 1) Bloomin' Brands same-store sales growth could be slower than expected if macro headwinds translate into lower restaurant consumption or sales driving initiatives lack traction, 2) Restaurant-level margins could come under further pressure if topline growth falters, 3) Normalizing G&A expense could pressure margins.

Upside Risks: 1) Same-store sales growth could exceed expectations if menu or marketing initiatives prove better than expected, 2) Cost saving initiatives could drive restaurant level margins above historical averages, 3) Ability to improve already low G&A expense ratio could support margins.

Brinker International (EAT)

Brinker's relative valuation to the S&P is 0.6x, in line with its 5-year historical average (0.6x), which we view as the relevant time frame given higher leverage and slower growth vs the more distant past. We valuation to remain in line with the historical range as Chili's growth trajectory normalizes, and the market is less willing to ascribe a premium multiple for a potential turnaround. Applying a 0.6x relative multiple (absolute P/E 9.2x) to our 12-month-forward EPS (F25: \$4.01) we arrive at our \$37 PO.

Upside risks are i) higher-than-expected demand from consumer trade-down into lower price point casual dining brands, which could drive Chili's sales volumes above our forecasts, ii) higher than forecasted debt pay down, which could expand Chili's relative multiple above our target valuation, iii) higher margins and returns at Chili's as a result of moderating commodities and wage inflation.

Downside risks are i) a significant slowdown in consumer spending could pressure EAT's topline growth, exacerbating the risk of company's high operating and financial leverage, ii) increased competitive intensity from casual dining peers, which would put downward pressure on Chili's average volumes and unit level returns.

Chipotle Mexican Grill (CMG)

Our \$2,570 price objective is based on earnings power. At the current unit growth rate, we think Chipotle should be able to reach its targeted 8000 store count in roughly 8 years. By then we'd expect AUVs to be \$4.2 mm - under the assumption that comps increase in-line with cost inflation - and margins to be in line with prior peaks of 27%. Assuming a G&A of 5%, which is more similar to mature company operated systems, this system would generate \$6.8bb in EBITDA. At a 20x multiple, consistent with current valuation multiples on high growth companies, the implied EV would be \$159bb, or \$63bb discounted back to today at WACC of 10%. We then add the current net cash and project out 12 months at cost of equity of 10% to derive our price objective of \$2,570.

Downside risks are: 1) lower than expected consumer uptake of new product innovations or digital ordering capabilities, 2) higher than expected food or labor costs that Chipotle is unable to offset with increased pricing, and 3) macroeconomic pressures that slow consumer income growth or otherwise dampen consumption.

Cracker Barrel (CBRL)

Relative to the market, CBRL's P/E multiple is below its 10-year historical average of 0.9x. We expect valuation to remain compressed as demand headwinds among CBRL's largest customer base (65+ and older, lower income) and broader discretionary spending pressures persist. We apply a 0.7x relative P/E multiple to our forward estimates 12 months from now (2Q25-1Q26, \$5.52) to arrive at a \$68 PO, that translates into an absolute PE of 12.3x.

Upside risks: higher-than-expected same store sales growth from digital/off-premise sales initiatives, faster-than-expected recovery in post-pandemic travel and tourism demand, better-than-expected contributions from the Maple Street Biscuit Company acquisition. Downside risks: higher-than-expected wage inflation, worse-than-expected margin contraction from elevated food costs, sluggish recovery in leisure travel demand.

Darden Restaurants (DRI)

Our 12-month \$193 price objective is based on a target relative P/E multiple (1.0x) on our forward estimates (\$10.25). Our target relative multiple (vs the S&P) is in-line with Darden's 10-year historical average multiple, and implies an 18.9x absolute P/E multiple. While investors remain cautious on restaurant spending, we believe fundamental outperformance by best-in-class operators like DRI will prove attractive.

Downside risks are 1) lower-than-expected customer acceptance of menu price increases, 2) inability to offset higher than expected food or labor costs with increased pricing, 3) macroeconomic pressures that slow consumer income growth, 4) slower-than-expected unit growth as a result of inflationary pressures (i.e., utilities costs) and supply-chain constraints.

Domino's Pizza (DPZ)



Given that Domino's returns and growth have consistently outpaced those of the broader market, we believe its historical range remains relevant and we expect the multiple to be stable. We apply the historical average relative P/E multiple of 1.3x to our EPS estimates 12 months from now (4Q24-3Q25: \$18.14) to arrive at our \$483 PO, or PE of 26.7x.

Downside risks: Market share gains for other larger competitors in the pizza category that impedes Domino's growth, global economic or social issues could disrupt same store sales growth or affect expansion in international markets, and competitive activity in the pizza category remaining high.

Dutch Bros (BROS)

Our \$48 price objective denotes estimated fair value based on normalized earnings power for BROS. We estimate that at \$9.2 bb in sales, assuming stable RLMs and 8% G&A, BROS would generate \$1.5 bb in EBITDA. Applying a 14x multiple and discounting back equates to a \$48 fair value in one year. We believe a 14x multiple is justified by Dutch Bros' long growth runway and high returns, and we note it is comparable to other restaurants and retailers with similar growth profiles that have sustained elevated earnings multiples over time.

Risks to our price objective: Dutch Bros could face execution risks to sustain a mid-teens store growth rate which would impede the implied sales growth of our saturation analysis. Margins and returns could also be lower-than-expected if Dutch Bros faces greater margin pressures than anticipated.

First Watch (FWRG)

We believe FWRG should trade a premium consistent with its faster growth and higher returns. FWRG currently trades in line with its peer group of restaurants and retailers with similar above-market growth rates. We believe a valuation in line with other high growth peers is justified owing to FWRG's faster than average topline growth, extended growth runway, as the brand goes national, and higher incremental returns, with restaurant level ROIs of about 40% or 2x other full service restaurants. We apply a 14x multiple to our forward EBITDA estimates (4Q24-3Q25, \$125mm) to arrive at our \$28 PO. This target multiple is in line with high growth peers' average of 14x.

Downside risks: higher-than-expected cannibalization of existing restaurants due to new store openings, staffing challenges and/or higher-than-expected wage inflation, higher-than-expected occupancy costs as First Watch ramps-up new stores at a faster rate. Upside risks: higher-than-expected AUVs of new units, faster-than-expected SSS growth, lower labor and G&A costs.

Jack in the Box (JACK)

Our \$97 price objective is based on a 0.7x relative PE multiple (13.1x absolute) applied to our 12 month forward earnings estimates (F25: \$7.44). This is a material discount to highly franchised peers MCD, YUM and QSR given historically slower growth and more capital-intensive ownership model.

Downside risks to our price objective are: 1) sales could soften due to economic or competitive pressures, 2) food and labor costs rise and margins come under renewed pressure, 3) execution risk around speed of service, menu and marketing initiatives which are critical to driving sales at Jack in the Box.

Krispy Kreme (DNUT)

We believe a premium valuation is justified owing to DNUT's robust double digit topline growth, extended growth runway, and higher incremental returns. We apply a 13x multiple (similar to high growth peers) to our forward estimate 12 months from now (4Q24-3Q25: \$299mm) to arrive at our \$19 PO.

Downside risks: potential industry headwinds from higher-than-expected wages, logistics, and commodity cost inflation, competition from other indulgence and foodservice businesses, and failure to achieve targeted unit growth due to higher than expected costs or other factors.

Upside risks: faster than expected growth in global access points, organic growth above the company's stated long-term growth targets, higher than expected share gains in the global indulgence and foodservice markets.

Papa Johns International (PZZA)

Our \$90 PO is based on 4Q24-3Q25 EPS (\$3.36) and a 1.5x multiple relative to the S&P (26.8x absolute multiple), in line with its 10-year historical average.

Downside risks: slower-than-expected consumer growth, increased competition in response to slower consumer spending driving promotional intensity, higher-than-expected inflationary pressures, labor shortages.

Portillo's Inc. (PTLO)

We set our \$25 PO based on steady state earnings power. We assume PTLO grows its store base at 13% to reach 725 stores in the long term, and that average volumes grow with inflation. At \$7.7 bb in sales, assuming stable RLMs and 8% G&A, PTLO would generate \$1.4 bb in EBITDA. Applying an 11x multiple and discounting back equates to a \$25 fair value in one year.

Risks to our PO: potential industry headwinds from wage inflation (MSD-HSD run rate for the industry) and food cost volatility, inability to fully offset downward pressure on volumes and margins from new store openings, and execution risks as the company looks to sustain a 10% unit growth rate.

Restaurant Brands International Inc. (QSR / YQSR)

Relative to the S&P 500, currently QSR's earnings multiple stands at 1.1x, in line with its 5-year average. We view this multiple as appropriate as lagging sales trends and greater investment needs drive lower estimate revisions. We apply a 1.1x multiple to our 12 months forward EPS estimate (4Q24-3Q25) EPS to arrive at a price objective of \$65 (C\$89.80). Our 1.1x relative multiple (vs the S&P 500) translates to an absolute P/E multiple of 18.2x.

Upside risks: better-than-expected results on sales trends and market share gains as a result of investments in stores, technology, and marketing spend. Faster-than-expected turnaround in the Burger King brand. Faster-than-expected growth of the Tim Horton's brand.

Downside risks: Higher-than-expected G&A spending, continued lag in topline growth trends relative to competitors, slower-than-expected recovery in supply chain and/or labor constraints associated with COVID-19.

Shake Shack (SHAK)

We set our \$75 PO based on steady state earnings power. We assume SHAK grows its store base at 14% to reach 860 domestic stores in 9 years, and that average volumes grow with inflation. At \$7.3 bb in sales, assuming stable RLM expansion from 18% to 21% and 9% G&A, SHAK would generate \$652mm in EBITDA. Applying an 11x terminal multiple and discounting back equates to a \$75 PO.

Downside risks to our price objective are: 1) lower than expected consumer uptake of new product innovations or other sales drivers, 2) higher than expected food or labor costs that Shake Shack is unable to offset with increased pricing, 3) macroeconomic pressures that slow consumer income growth or otherwise dampen consumption.

Upside risks to our price objective are: 1) higher than expected consumer uptake of new product innovations or other sales drivers (digital, Kiosks), 2) higher than expected menu pricing, 3) higher than expected consumer income growth that exceeds our consumption expectations.

Starbucks (SBUX)

Starbucks should trade at 1.5x relative to the S&P 500. This translates to an absolute multiple of 26.6x. We apply this multiple to our F25 EPS of \$4.81 to arrive at our PO of \$128. We believe that the multiple is justified given tailwinds as China reopens, increased investments associated with labor, operations, and unit development, as well as a return to a higher long term growth algorithm.

Downside risks: Starbucks' comps could decelerate faster than anticipated either from a lack of traction in company initiatives or a deteriorating demand environment. Margins could compress more than expected if Starbucks fails to pass through inflation in labor costs.

Sweetgreen (SG)

Our \$16 PO is based on normalized earnings power. Assuming SG is able to reach its long-term target of 1000 stores in ten years, with 18% restaurant-level margin and 8% G&A, we arrive at \$274mm EBITDA. We apply a 16.5x terminal multiple - consistent with mature growth restaurant peers - after adjusting for SG's domestic, company-operated status - to arrive at EV of \$4.5 bb, or \$1.5 bb discounted back to today at 12%.

Downside risks include i) slower SSSG as a result of lower discretionary spending, ii) inability to gain traction in new markets outside of the urban core, iii) failure to offset food and labor cost inflation through pricing and volume growth, iv) worse than expected development challenges (construction costs, permitting) which could limit unit growth.

Texas Roadhouse (TXRH)

Relative to the S&P 500, TXRH's P/E multiple is below its 5-year average of 1.2x (we exclude COVID valuation spikes from 5-year history). We view its 5-year average as the appropriate target multiple given TXRH's best-in-class traffic trends and topline growth and our expectations for further operating leverage. Our PO of \$123 is based on a relative multiple of 1.2x (vs the S&P 500 index, or a 19.4x absolute multiple) on our 12-month forward EPS (4Q24-3Q25, \$6.36).

Downside risks are: i) lower-than-expected retail beef prices and as a result, decreased value proposition for steakhouses, ii) traffic growth deceleration in response to menu price increases, iii) greater than expected slowdown in consumer spending / macroeconomic risk pressuring discretionary income, iv) slower than expected unit growth at Texas Roadhouse.

The Cheesecake Factory (CAKE)

Relative to the S&P 500, CAKE is trading at 0.6x P/E, 1 standard deviation below its 5-year average (excluding the COVID-spike). With inflation moderating from F22 levels and consumer spending slowing, we believe it will be difficult for CAKE to raise prices and grow SSS meaningfully above its long-term historical average (of 1%). Our \$33 PO is derived by applying a 0.5x relative multiple (9.8x absolute) to our EPS 12 months from now. We validate our PO against a DCF.

Downside risks i) higher than expected wage inflation in California (18% of Cheesecake Factory units), ii) traffic share losses due to consumer trade down, iii) slower than expected demand from higher income cohorts (Cheesecake Factory and North Italia skew higher income). Upside risks i) higher than expected SSS growth from menu price increases, ii) more resilient than expected spending among higher income cohorts, iii)

higher than expected brand resonance in new markets, translating to higher volumes for new units.

Wendy's Co (WEN)

Relative to the S&P 500, Wendy's valuation is currently trading below its 5-year average (1.3x). Despite efforts to bolster the new unit pipeline, we see risks to the unit growth target. We apply a 1.1x relative multiple (17.8x absolute multiple) to our EPS 12 months from now (4Q24-3Q25: \$1.17) to arrive at our \$21 PO.

Upside risks: higher than expected incremental tailwinds / higher sales mix from breakfast or other menu innovation, faster than expected international unit growth, greater than expected market share gains as a result of strategic initiatives or competitive advantages.

Downside risks: comps could disappoint if consumers resume pre-COVID behavior faster than expected, Wendy's could miss international unit growth targets if licensees fail to open new units at the expected pace.

Wingstop Inc (WING)

We set our \$285 PO based on steady state earnings power. We assume WING grows its store base at 14% to reach 9,123 restaurants. Assuming RLMs of 30% and G&A at 1.8% of system sales we arrive at EBITDA of \$1.2bb. Applying a 18x terminal multiple in-line with mature growth franchised restaurants and discounting back we arrive at our \$285 PO.

Risks to our PO: potential industry headwinds from wage inflation, and food cost volatility, inability to fully offset downward pressure on volumes and margins from new store openings, and execution risks as the company looks to sustain a 10%+ unit growth rate.

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We, Sara Senatore and Katherine Griffin, hereby certify that the views each of us has expressed in this research report accurately reflect each of our respective personal views about the subject securities and issuers. We also certify that no part of our respective compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Restaurants Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Chipotle Mexican Grill	CMG	CMG US	Sara Senatore
	Darden Restaurants	DRI	DRI US	Sara Senatore
	Domino's Pizza	DPZ	DPZ US	Sara Senatore
	Dutch Bros	BROS	BROS US	Sara Senatore
	First Watch	FWRG	FWRG US	Sara Senatore
	Jack in the Box	JACK	JACK US	Sara Senatore
	Krispy Kreme	DNUT	DNUT US	Sara Senatore
	Papa Johns International	PZZA	PZZA US	Sara Senatore
	Portillo's Inc.	PTLO	PTLO US	Sara Senatore
	Starbucks	SBUX	SBUX US	Sara Senatore
	Sweetgreen	SG	SG US	Katherine Griffin
	Texas Roadhouse	TXRH	TXRH US	Sara Senatore
	Wingstop Inc	WING	WING US	Sara Senatore
NEUTRAL				
	Bloomin Brands	BLMN	BLMN US	Sara Senatore
	McDonald's	MCD	MCD US	Sara Senatore
	Shake Shack	SHAK	SHAK.US	Sara Senatore
	The Cheesecake Factory	CAKE	CAKE US	Katherine Griffin
	Yum Brands Inc	YUM	YUM US	Sara Senatore
UNDERPERFORM				
	Brinker International	EAT	EAT US	Katherine Griffin
	Cracker Barrel	CBRL	CBRL US	Katherine Griffin
	Restaurant Brands International	YQSR	QSR CN	Sara Senatore
	Restaurant Brands International Inc.	QSR	QSR US	Sara Senatore
	Wendy's Co	WEN	WEN US	Sara Senatore

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Restaurants Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	21	58.33%	Buy	10	47.62%
Hold	10	27.78%	Hold	3	30.00%
Sell	5	13.89%	Sell	4	80.00%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2}Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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